**Background and context to trusts and equity**

**Equitable Maxims**

1. Equity will not suffer a wrong without a remedy.

2. Equity follows the law.

3. Where there is equal equity, the law shall prevail.

4. Where the equities are equal, the first in time shall prevail.

5. He who seeks equity must do equity.

6. He who comes into equity must come with clean hands.

7. Delay defeats equities.

8. Equality is equity.

9. Equity looks to the intent rather than the form.

10. Equity looks on that as done which ought to be done.

11. Equity imputes an intention to fulfil an obligation.

12. Equity acts *in personam*.

**Fiduciaries**

**Who are fiduciaries?**

Certain individuals are fiduciaries, and a lot of them make common logical sense. Most people know that lawyers, company directors and trustees are fiduciaries. But many people struggle to draw the line, or explain the difference between the duties owed by a plumber and a lawyer.

* You give your plumber discretion to make decisions and carry out actions on your behalf; you trust them to make good decisions that affect your finances and welfare.
* So why is a plumber not a fiduciary?

Different tests for fiduciary status

*Traditionally*, the courts would establish whether a fiduciary relationship existed. If it did, all duties and obligations were *fiduciary* ones. All breaches were fiduciary. All remedies were fiduciary.

The *modern approach* appropriately views fiduciary duties as a heavy burden. Fiduciaries are expected to act on behalf of, and in the interests of, another party.

* Fiduciaries have power and discretion
* Fiduciaries actions must have the purpose of advancing their principal’s interests. Considering their own interests is irrelevant or improper.

This is why plumbers aren’t fiduciaries. They’re not expected to act only in their clients’ interests. They’re fully within their rights to act in the interest of making a profit for themselves. In fact, there are lots of other duties that will be imposed to protect the plumber’s clients (such as tort, contract, duties of confidence) and none of them are fiduciary.

The UK Law Commission (2015) suggested that fiduciary status depends on whether there is a legitimate expectation that one party will act in another’s interest.

* This is a legitimate statement of what a fiduciary is.
* But shouldn’t the test be centred around when the law will impose fiduciary duties and obligations, rather than around when someone *thinks* there should be one?

When there is an undertaking to act on someone else’s behalf?

* We want people to owe their fiduciary duties if they are a fiduciary.
* They shouldn’t escape those obligations by claiming they did not undertake to perform them.

The law focuses on OBLIGATIONS, DUTIES and REMEDIES. Not on whether someone has a particular status. If a person owes fiduciary obligations, they are a fiduciary.

**What obligations do fiduciaries have?**

Again, there are lots of duties and obligations in common law and equity that require people to act in others’ interests: contract, duties of confidence, undue influence, tort law. Yet there is a higher obligation that can be owed, that makes a person a fiduciary.

*Lord Millett =* the distinguishing obligation of a fiduciary is **loyalty.**

* Fiduciaries must act in good faith.
* They must not make a profit out of the trust.
* They must not place themselves in a situation of conflict of interest.

These are negative duties, not positive ones.

*Paul Finn =* loyalty may be extracted in a draconian way, but NO MORE than loyalty is expected. If there is no issue of disloyalty, usually matters will be actionable through other bodies of law (negligence, breach of contract, breach of trust).

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| *Example:*  If a fiduciary makes a wrongful payment of assets that is contrary to the terms and their principal is harmed, there is strict liability.   * If the payment is made because of poor decision making, this could be breach of contract or negligence. * If a trustee has ‘put their hand in the till’, there is breach of trust and disloyalty.   Wrongful management of assets is usually a claim in negligence as opposed to a claim of disloyalty. |

Why do we put such obligations on fiduciaries?

* Because the principal is vulnerable to them?
* Because the principal has a legitimate expectation of loyalty?
* Because they’re acting on behalf of another person, so they need to meet certain requirements?

**What consequences follow fiduciary status?**

The first key distinction is: is this a breach BY a fiduciary, or a breach OF A FIDUCIARY DUTY?

If you are a fiduciary and you breach your fiduciary obligations, the response is **disgorgement of profit.**

This is the repayment of ill-gotten gains, which can be either a *proprietary* or *personal* remedy.

* If it’s proprietary, the principal will *own* the ill-gained profit in equity, and be able to trace that property to regain it.
* If it’s personal, the principal will *be owed* the ill-gained profit.

This is very useful, because if the value of the profit/property has decreased, or another person has it and it can’t be regained, a personal remedy might put the principal in a better position than a proprietary one. Alternatively, a proprietary remedy means the principal can get their money back, even if a third party has it and the fiduciary is unable to pay the amount owed for a personal remedy.

How might a fiduciary receive an ill-gained profit?

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| They directly deal disloyally with assets themselves. | * Direct conflict between the principal’s interests and the fiduciary’s interests. * Clear breach of loyalty. * Universally accepted that disgorgement is accepted here, and will be proprietary if the property is identifiable (or personal if it’s not) |
| They make a disloyal profit without directly subtracting funds from the fiduciary “pot” | For example, competing with the principal for an opportunity or advantage.   * E.g. In FHR, the fiduciary, an agent, took a 10 million pound bribe (or secret commission) while negotiating the sale of a hotel. The principal sued the agent for disgorgement, and successfully claimed that the remedy was proprietary.   + Issue: the Supreme Court decided that a disloyal fiduciary cannot keep the gains. But they did not say why - other than without good reason otherwise, it seems right to take the simpler approach of proprietary disgorgement.   + Interestingly, this was the traditional approach - equity treats as done what ought to be done.   + Rejected in the case of Lister, which held that this would lead to unacceptable consequences for third party beneficiaries. |
| *Critique/analysis of disgorgement remedy* | There are a few issues with disgorgement in the second example provided above.   * Obligations to hold a trust on behalf of the beneficiaries is a very different obligation than disgorging disloyal gains to a principal * The purpose of disgorgement is that the fiduciary should not have the profit they gained because it was gained wrongfully. In this situation (a bribe), that doesn’t mean it IS the principal’s.   + This is a windfall.   + This also treats the profit/bribe as *already owned by the principal in equity,* because disgorgement is proprietary. This is inconsistent with the nature of bribes - what principal would say they owned bribe money intended to injure them?   This is essentially a matter of policy.   * Either the fiduciary non-compete rule is so important and key to the fiduciary relationship that, if breached, the benefits of that competition should go to the principal, even if this is overprotective, or results in some abstract, conceptual difficulty * The rule of disloyalty is proscriptive (a negative duty). The purpose of its remedy is profit-stripping of the breaching fiduciary - the object of providing this ill-gained profit to the principal is not the focus. Consequently, disgorgement is a personal right. |

**What compensation follows for losses due to breach of fiduciary duty?**

If you are a fiduciary and you breach a NON-fiduciary duty, you could be responsible for compensating your principal for that loss. This type of compensation is usually **equitable compensation.**

This issue was directly dealt with in *AIB.*

In the case, the solicitor (employed by the bank) was responsible for holding funds until they received security from mortgagees. They could then pay out the funds. The solicitors, however, paid them out before receiving security. The mortgagees defaulted, and when the bank went to enforce the security, the property market had collapsed and they faced large losses.

* The Bank argued that funds were meant to be held until authorised to pay them out, according to instructions. The appropriate remedy is reinstatement of the funds that were paid out wrongfully.
* The Solicitors argued that even if they had performed their duties as instructed, the loss would still have been suffered. The loss flowed from the collapse of the property market, not from the solicitor’s breach of duty.

The Court decided that the first step was to identify the relevant breached duty: the obligation to ensure the trust fund is duly administered.

* This is not a ‘fiduciary duty’ by nature. It’s a duty of management - a positive duty of performance.
* Consequently, the solicitors must make good the loss suffered from the breach of this duty by equitable compensation.

However, there are a few issues with this approach, laid out by *Sarah Worthington:*

The relevant duties and remedies:

* There is a duty to perform the trust (primary)

The remedy is specific performance.

* There is a duty to compensate for losses or faults arising from non-performance (secondary)  
  The remedy is an order of repair or damages.
* There is a fiduciary obligation not to compete, and not to put your interests above your principal’s (fiduciary)  
  The remedy is proprietary disgorgement.

The Court wrongly considered this under the duty to compensate for losses or faults arising from non-performance. However, the same decision (solicitors winning) can be reached under an alternative head, analysing breach of the primary duty.

Primary duty

The primary duty of the solicitors is not to pay an agreed sum or to hold a specific fund. It’s to go through a series of steps to meet a particular end result. In addition, the object of trustee obligations is to ensure custody and management of the trust assets, to ensure the trust ‘pot’ is kept in the state it ought to be in, or returned to the state it should be in if there’s any ‘slippage’.

* If specific performance were ordered, they would need to take all the steps required by instruction - not merely one or two. However, ordering damages for breach on the basis of *one* of those steps is doing exactly that; preventing the solicitors from completing their obligation.
* The court should assess what state the trust assets ought to be in at that date, considering the trustees’ ongoing duties, up until the date of assessment. This includes consideration of all elements (including the market).

**Fiduciary obligations in practice**

*Keech v Sanford*

Before the expiry date of a lease, the renewal was refused to the infant. The trustee took the lease personally, to prevent it being lost. It was held that he must convey the lease to the infant and account for the profits.

* No fraud. No action that could have benefitted the infant. Yet the court held that the trustee was the *only person in the world who couldn’t take the lease.*
* This reflects the strict liability nature of fiduciary relationships. But why does this need to be so strict?
  + To protect principals from dishonesty?
  + To prevent loss or injury to the principal?
  + To protect those who enter into fiduciary relationships?

Admittedly, the above reasons are strong. But why could liability not turn on dishonesty, loss or injury? There may be no *need* for such strict liability. This is an example of the onerous burden of fiduciary duties, and how central and important the courts view loyalty - it’s not just being loyal, but avoiding situations that could be seen as disloyal or result in disloyalty.

*Boardman v Phipps*

Facts

Boardman was a solicitor and Phipps a beneficiary of the trust. The trust was created when Phipps Sr passed. The trust had some shares in a company called Lester & Harris Ltd.

Boardman and Phipps went to the AGM, and found that they were dissatisfied with the management of the company. They suggested that the trust purchase shares - the active trustee was against this, and said he would not contemplate the trust doing so.

Boardman and Phipps then decided to purchase shares themselves.

There were a number of negotiations about purchasing controlling shares. Boardman requested a lot of information (which the acting trustee was privy to) for the trust, and for themselves.

Boardman used this information, and information he had sourced himself from travelling to visit the assets, to make an offer on the trusts (after lots of negotiating and ‘attrition’.)

When he and Phipps had controlling shares, the company began to make a profit. The trusts shares increased in price, and Boardman and Phipps made a profit.

The trust is requesting that Boardman and Phipps account to the trust for that profit; that they made that profit under a constructive trust for the beneficiaries.

Held

The appellants are liable to account to the trust for the profits made. They are permitted to retain a certain amount.

Ratio

Two possible approaches to the ratio of the case:

* Fiduciaries have a negative duty not to take opportunities or information made available to them for the benefit of their own interests, regardless of whether this injures or harms the principal in any way, because it is the property of the trust.
* Fiduciaries will be liable to account to their principals if they put themselves into a position where their personal interests conflict with, or may possibly conflict with, their principals.

Previous precedent

Regal

Those in a fiduciary position who make a profit are liable to account. This isn’t based on fraud, but on whether the circumstances meant that the fiduciary should have been acting for the principal rather than themselves.

In this case, the profit was gained due to an opportunity and knowledge provided by their fiduciary position, and the profit was therefore accounted to the principle.

A defence to this is knowledge and consent of the principal.

Judgment

The judges in Boardman v Phipps had various conceptions of the case. Mostly, it turned on different formulations of

* Trust property
* The no conflict rule

The **majority** considered that the information was not public information - it came about in circumstances where the fiduciary was acting on behalf of the trust. Therefore, the opportunity to invest (and possibly the information) is property of the trust, and can’t be used for the fiduciary’s own gain.

Consent IS acknowledged as a defence, but wasn’t given because:

* The widow was never consulted (admittedly, she was senile)
* Possibly requires independent legal advice to be considered “fully informed consent”

The majority considers *Regal* to be authoritative law regarding fiduciary obligations where information and opportunities arise from their fiduciary position.

The minority don’t seem to view *Regal* as authoritative. They distinguish it based on its facts - because in *Regal,* the trust could have purchased the shares but chose not to. The possibility of conflict still existed. On the other hand, this is more about trust property than conflicts of interest.

Is this simply an approach based on the justice of the case? Are the minority simply trying to find arguments to justify their conclusion, rather than the other way around?

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| *Lord Cohen (M)* | * Information and opportunity arose in the course of exercising fiduciary obligations on behalf of and for the benefit of the trust - the Regal principle applies   + Critiqued the minority for not attaching enough weight to this factor * Could have been a possible conflict. Could not have advised the trustees on the deal while he was negotiating it (irrelevant that there would need to be a court order) |
| *Lord Hodson (M)* | * Position as fiduciary enabled him to gain information on behalf of the trust. The information is confidential “know how” and can be regarded as trust property * Inability to buy shares does not excuse liability - it imposes a constructive trust (*Keech v Sanford*) * Remote possibility of conflict, but nevertheless a possibility |
| *Lord Guest (M)* | * Information received could ONLY be gained through his fiduciary position, acting on behalf of the trust. * This special fiduciary position in negotiations provided him with the opportunity to profit. * Strict rule of equity = can’t profit from trust property. *Implies he considers this opportunity and information trust property.* * Irrelevant whether the trust is injured, or whether fiduciary obligations were neglected. |
| *Viscount Dilhorne (m)* | * It can’t be said that the opportunity, information and purchase came about only by virtue of the fiduciary relationship.   + The fiduciary engaged in personal enquiries, research and used their own business knowledge and acumen.   + Majority of information was public   + The active trustee was aware of all information and circumstances * The information could not be owned by the trust because it was not within the scope of the trust’s ability or intention to act. The information *could not have been used* by the trust. * No possibility of conflict arising because the trust did not want and could not purchase the shares themselves.   + Regal distinguished on this ground, because in that case *it was* intended that the trust purchase the shares. |
| *Lord Upjohn (m)* | * Fiduciaries can act against their principals as long as they aren’t using their information or putting themselves in a position of conflict.   + To be protected information, either confidential information, or fiduciary information that could lead to conflict of interest   + Neither grounds are satisfied here * To find a possible conflict the reasonable person must be able to see a real, sensible possibility. Conflict here would be too remote. |

Consequently, it’s clear that information or opportunities you receive because of your fiduciary position may result in obligations of confidence/a negative obligation not to use them.

*Arklow*

Facts

Plaintiffs have an idea to purchase a forest on Matakana Island. They have an idea on what the seller will accept, and have a really good idea on how to make a profit from the idea.

The one thing they don’t have is the money to complete the deal.

They seek to employ someone that can advise on this - how to put the plan together, seek funding etc. They approach a merchant bank to ask on this. It’s discussed in confidence - clear on both sides. In doing so, they give up some of the information they have.

At the end of it, the plaintiffs end up without the forest - the merchant bankers have partnered with other companies to purchase the land.

Brought two claims: one in breach of confidence, and one in breach of fiduciary obligation.

Held

* High Court - There was a fiduciary duty that was breached. Found a remedial constructive trust.
* Court of Appeal - No fiduciary duty. No breach of confidence. Thomas J dissenting.
* Privy Council - No fiduciary duty. No breach of confidence.

Judgment

* Accepting some sort of duty or obligation *doesn’t* mean you owe fiduciary obligations.
* Looked to *Blake v A-G;*
  + a spy and traitor published a book and wished to retain the worth. The claim was to return royalty payments to the UK govt.
  + **A fiduciary relationship is one of trust and confidence. The core obligation is loyalty. But this duty only lasts while the relationship lasts.**
  + On the other hand, a duty of confidentiality is imposed whenever information is imparted in confidence. It exists beyond the term of the relationship, but only while information remains confidential/private.
* A duty of confidence is an equitable obligation, but that doesn’t mean it is a fiduciary one.
* No obligation of confidence because D didn’t actually use the information. It only “sped up” their process/decision making.
* The nature of the information given was arguably minimised by the court
  + The merchant bankers already knew of the deal Arklow told them about. Anything extra could have been determined themselves based on information in the public domain (the prospectus); research they had already done; or by working it out themselves.
  + The information Arklow DID share were their plans. But this was nothing revolutionary: it was a relatively common structure. The parties outlined in the plan were never contacted.
* No fiduciary obligation because **P did not accept D’s offer to act on their behalf.** If they had, they would have *at least had* a contractual obligation of loyalty.
  + You cannot use equity to give you what you haven’t bargained for.
  + Why should the merchant bankers not be able to pursue their own interests when they offered to act on another’s behalf and weren’t taken up on it?
  + *At the time, a general sense that equity would intervene and give you a remedy if you hadn’t gotten something in ‘good faith’.   
    This case was an almost revolutionary response, demonstrating that if you WANT duties of loyalty, you should contract for them - the courts will not always find them. If you don’t want people to misuse your information, don’t give it to them until you have an agreement.   
    Return to a cold, contract-driven capitalist world?*
* The finding of a fiduciary obligation is not remedy-led. The courts will first find whether such a relationship exists, and then determine the remedy in response. There is an obligation not to misuse confidential information, but a fiduciary obligation does not necessarily follow (Gault J)

*Chirnside v Fay*

Facts

Two acquaintances are seeking an opportunity for property development together. They are aware that Speights Brewery is moving and will open up a very central, desirable site for development. They have both entered into a joint venture together before.

Negotiations commence. Mr Chirnside’s interest in a neighbouring property that can provide parking spaces makes the deal better.

The arrangement is for Mr Chirnside to do most of the work, and Mr Fay would contribute to paying necessary funds. However, both parties worked on the proposal and dealt with third parties and advisers. Mr Fay was included in the planning and execution of the venture, including contact with Harvey Norman.

Mr Chirnside then decided to carry out the deal himself because he had found an alternate means of obtaining funds. He lied to Mr Fay and said he has a purchaser, but is bound by confidentiality. He later further misleads him, until Mr Fay finally sues.

Despite the existence of drafts, there is no finalised agreement between the two parties.

Held

* Court of Appeal awarded damages, including lost opportunity damages.
* Supreme Court found a fiduciary duty.

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| *Test for a fiduciary obligation*  *Blanchard and Tipping JJ* | A joint venture relationship is, by nature, fiduciary. Figured this out by:   * Analogy to partnership   + Traditional fiduciary relationships involved exchanging duties of loyalty and good faith.   + Must always put the interests of the partnership above their own * Examination of particular aspects   + If a relationship entitles P to trust and confidence, it is prima facie fiduciary   + No need for any ‘undertaking’ to act on behalf; this would undermine equity and reduce its reach * Pursuit and reliance on common objectives   + Joint ventures proceed on the basis that you act in each other’s interests. Entitled to expect loyalty: trust and confidence     - *But there’s no contract. No certainty of any structure, responsibilities or anything of the sort*. *If you want these sorts of rights, shouldn’t you contract for them?*     - *E.g. comparison with the ‘hard line’ taken in Arklow.* |
| *Test for a fiduciary obligation*  *Elias CJ* | Elias CJ took a far more direct approach than Tipping J  She found that because the parties had entered into a venture with a view of sharing profit, they owed each other a duty of loyalty. This is the distinguishing obligation of a fiduciary, so they are fiduciaries and subject to the no-conflict rule.  No person can benefit from their own wrongdoing, though it is not necessary that the wrongdoing be in bad faith or a conscious wrong. |
| *Breach and remedy*  *Blanchard and Tipping JJ* | The defendant took for himself an opportunity that arose out the fiduciary arrangement - self dealing.  The normal remedy for this is account. CA felt that, due to uncertainty, equitable compensation was more fair.   |  | | --- | | The issue with this is that account and compensation are philosophically very different.   * Account is not a measure. It is a proprietary right over property *belonging* to the venture (ie: the opportunity). Its focus is on D’s wrongful gain, not on what P should have. * Compensation is discretionary according to the court’s judgement. It is a measure that makes P good for what he has lost. |   SC found account to be the appropriate remedy [according to the breach of fiduciary obligation] but that D should receive a discount due to the effort and skill he put into achieving the profit for the following reasons:   * The division of labour/skill is not equal.   + Mr Chirnside did far more work than Mr Fay.   + He should be compensated for his skill and the work he put in.   + It is appropriate that this is done, based on the judgment in Boardman v Phipps. |
| *Remedy*  *Elias CJ* | No person can benefit from their own wrongdoing, though it is not necessary that the wrongdoing be in bad faith or a conscious wrong. It’s part of the wider no-conflict rule that ensures fidelity. Consequently, we look to D’s gain rather than P’s loss.  The remedy for breach of fiduciary obligation is account. If the court decides account is appropriate, the defendant is obliged to give the property back.   * Boardman v Phipps is different; there was no sense of infidelity or disloyalty   + He acted with the intention of benefitting his principal * Here, Chirnside could have acted in both interests, consistently with his duty of loyalty, but chose not to. * His use of skill and labour was a consequence of his breach and should not be considered. * You might be permitted to make an allowance if the profit made was **outside the scope of the fiduciary obligation.** But here, the work was what was anticipated to be done in the scope of the joint venture.  |  | | --- | | This seems like a gut instinct approach: the intentional misconduct means that any discount or excuse of liability should not be justified. | |

There are clearly circumstances where a fiduciary obligation will be owed, even if no contract exists. This could be read as the court trying to justify their gut instincts.

However, another interesting note is the approach to account. All judges seem to consider account a discretionary court remedy, yet there doesn’t seem to be anything discretionary about ordering a return of property, and the court does not seem to be making any distinction here between Chirnside’s property and Fay’s property - although perhaps they are implicitly.

*Mothew*

Facts

Solicitor responsible for paying $$ to people taking out mortgages. The bank instructed the solicitor not to pay the money out until they had confirmation that the mortgage would be the client’s only loan. When negotiating with the clients, the solicitor was not aware that they had a loan. However, he became aware of this later [it was an old loan, but terms were re-contracted]. He neglected to mention this to the bank, and paid the money.

The bank sought to enforce security when clients defaulted. The property market had crashed.

The bank brought two claims: breach of fiduciary obligation and misrepresentation.

Held

Not every breach of a duty by a fiduciary will be a breach of a fiduciary obligation. The only fiduciary obligation owed is loyalty, and those sub-duties encapsulated within it.

Judgment

The Court discussed the relationship between the common law claim for misrepresentation and the solicitor’s fiduciary obligation to the bank.

This was an important distinction, because if there was liability at common law, the rules of remoteness and foreseeability applied (*Samco)*. If there was liability for breach of a fiduciary obligation, there could be a strict liability approach.

The Court acknowledged that there was a fiduciary relationship between the solicitor and the bank. However, they decided that **not every breach of duty is a breach of a fiduciary obligation.** They must first examine what duties were owed, what duties were breached, and then remedies.

* The bank is really arguing that the solicitor failed to exercise due skill and care. This is a common law duty, not a fiduciary duty (which only includes loyalty).
* The breach of that duty is not made fiduciary simply by virtue of a fiduciary relationship
* The bank can enforce this duty through the common law.

*Premium Real Estate*

Facts

P gets D to sell their house for them. D advised them that they were expecting too much for their property. The purchaser buys the house off them after it has been on the market for some time. He pays approx $2.5m. The purchaser sells the property for $3.5m.

The purchaser was known to D when they made an offer. D did not tell P that they knew D to be a property investor who purchases cheap and sells for more expensive. D gives P the impression that the purchaser intends to live in the house [misleading].

D had hopes that after purchaser attained the property, they would employ them to sell it on again.

P seeks damages amounting to the profit gained by the purchaser, claiming that, but for D’s actions, they would not have sold the property to him.

Held

Allowing their vendors to operate under a misapprehension was a breach of the fiduciary obligation of loyalty. It was also a misrepresentation under the FTA.

Judgment

The Court reinforced *Mothew’s* point that there is no positive fiduciary duty to exercise due care and skill.

* Fiduciaries have duties of loyalty. If, for example, a duty to exercise due care or skill occurred because of a conflict of interest, there would perhaps be a breach of fiduciary obligation.

*Discussion of obligation to disclose/obligation not to mislead:*

The Court accepts that the reality of the market means you cannot reasonably expect complete loyalty from a real estate agent (especially in a small country like NZ). They will usually be acting for multiple parties at once, due to the nature of their job.

* However, both the majority and minority agreed that by staying silent, the real estate agent contributed to the vendors’ misapprehension.
* Allowing such misapprehension when acting in their interests is both a breach of the agent’s fiduciary duty AND misrepresentation under the FTA.
* He was being disloyal by acting in his own interests. This doesn’t automatically equate to any duty to disclose conflicts of interest [for real estate agents] if they are still acting loyally.
  + If conflicts and material facts did need to be disclosed all the time, real estate agents would be unable to act in the interests of their clients and would breach confidentiality

The relevance of this was left open by the Court.

It would be interesting to see what the Court would have decided if the vendors had not been operating under any misapprehension, but the conflict had existed. Would there be any obligation to disclose the existence of the conflict? This can be read into the Court’s discussion below.

The Court acknowledged that the real estate agent owed some sort of fiduciary duty, and common law duties to the vendors. In establishing the significance of this, the court considered the decision of *Kelly v Cooper*:

A real estate agent acted for both vendors of adjacent properties. Purchaser bought one property - and the agent did not tell the vendors that the purchaser had purchased it. He later purchased property two from the other vendor.

* That vendor claimed that they could have sought a higher price if he’d known.
* It was held that the agent could keep his commission because he had *done his job.*

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| *Elias CJ (minority)*  Seemed to use *Kelly* as support for the proposition that real estate agents cannot owe duties of complete loyalty: vendors hire real estate agents because of their previous transactions. There will be inevitable, or at least possible, conflicts in some scenarios.  To support this proposition, Elias CJ used Lord B-W’s reasoning where he said that “not all fiduciary obligations are the same” | *Blanchard J*  Blanchard J seems to be reluctant to find different kinds of fiduciary obligations - either there are fiduciary obligations or there aren’t.  He seems to suggest that although real estate agents often operate under conflicts of interest, the agent should have disclosed them. |

*Discussion of appropriate remedies*

* All judges agree that the real estate agent’s commission should be returned to the vendors.

The Court decides that the remedy awarded cannot be account, because the ill-gained profit was attained by a third party, not the breaching fiduciary. However, they agree that the profit gained is relevant to assessing what the agent might owe to the vendors.

However, they also noted that equitable compensation could be difficult due to the number of competing measures that could be used.

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| *Majority*  The majority essentially took the “what the vendors could have gotten” approach.   * Market evidence suggested a price of $3.25m. * The house had only been on the market for a few weeks. Without the misrepresentation, they would have had a better understanding of the market and might have held out longer. * In common law, the plaintiffs must prove that they would have acted differently. But here, because the obligation is fiduciary, t**he errant fiduciary has the burden.**    + The Court used this burden to justify using a higher measure of damages.   The real estate agent owes the vendors the price they could have obtained - $3.25m (minus the amount they did get). | *Elias CJ (minority)*  Elias CJ took a “best guess” as to what the vendors would have done if they’d been fully informed.   * On the evidence, all the plaintiffs have proven on the balance of probabilities is that $2.8m is the price they would have sold at. There is no evidence that they would have held out (if offered $2.8m) for an offer of $3.25m. |
| The problem with this approach is that this is entirely hypothetical, based on the chance that the vendors would have held out for $3.25m. Market valuations may say that, but it relies on purchasers offering that much (which in the weeks it was on the market, they did not).  It was also accepted that the initial advice that the property was worth $2.8m was *good advice*. Why then are the courts basically using equitable compensation as a vehicle for account *in personam?*  Is $3.25 million reasonably within the scope of the real estate agent’s relationship with the vendors?  The reasoning behind choosing this measure of damages is relatively incoherent. What legal justification is there? | This measure might be unfair. The vendors were under significant pressure to sell. This estimate of $2.8m depends only on past offers.  But at the time, the vendors believed they were mistaken about the market value and price they could attain. It is entirely possible that with the correct information, a better price could have been attained. |

The biggest difficulty is the lack of clarity. We aren’t sure why the majority or minority chose their respective measures.

Another difficulty is their dismissal of account. In *Chirnside*, Elias CJ was very clear that account was a strict remedy. Why has the court dismissed this remedy in favour for equitable compensation here?

* The person who actually makes the profit is arguably irrelevant for breach of fiduciary obligation.
* In addition, Elias CJ found in Chirnside that no discount should be made for exercise of skill where there has been a breach of fiduciary duty through infidelity. This seems almost exactly like this scenario - there has been infidelity by the real estate agent because he acted in his own interests instead of the vendors’. So why is such a strict approach not being taken?
  + Because $3.25m was never in the *scope* of the vendors’ sale, so it would be wrong to consider a *third party’s profit?*

If the measure had been account, the agent may have been required to account for any profit he made (ie: the commission received from the vendor AND the purchaser). But the vendors may not have received as much money as they did in this case. Perhaps this was another gut instinct response.

**Trustee Duties and Breaches of Trust**

As we’ve already seen discussed in *Boardman v Phipps, Arklow, Chirnside v Fay, Mothew* and *Premium Real Estate,* trustees are fiduciaries who owe duties of loyalty. This includes rules against conflicts of interest and self-dealing.

However, trustees will usually also owe a number of other duties that *aren’t* fiduciary.

**Conflict of Interest**

*Fenwick*

Facts

Trustees made a unanimous decision to enter a joint venture with another trust. Three of the trustees had conflicts (one had 5% shares in the other trust they entered into joint venture; another’s husband had shares). Governed by Te Ture Whenua Act.

Held

Interests will only conflict if they are not *de minimus*, but this threshold is low. Being a trustee or beneficiary on both sides will always be a conflict.

Judgment

If the strict conflict of interest approach is applied, then there is a breach of trust. However, the trustees argued that their interests are very small, and the benefit they might gain is correspondingly small, and not enough to constitute any conflict of interest.

The Court maintained their strict approach to conflicts of interest.

* It doesn’t matter how minimal your interest is if you have a beneficial interest on both sides, or you are a trustee on both sides. This is a clear conflict.

However, the Court acknowledged that had there been only one party with a conflict, that conflict had been a 1% interest, and they had not been a trustee, this may have been a case of *de minimus.*

Clearly, interests need to meet a certain threshold to be conflicts. However, the bar is set very low, and will usually not be met - especially where someone is a beneficiary or trustee on both sides.

The trust was a Te Ture Whenua Maori trust. The relevance of this is that the Act provides factors for the Maori Land Court to consider in deciding whether the joint venture should be set aside/rescinded. However, it’s important to note that Maori culture is of such a nature that conflicts are almost inevitable: land is taonga, and rights to it are conceptualised differently than in Western law. However, it remains true that this could have been included in the trust deed.

Comments

The justification for this strict approach is that fiduciaries are not permitted to make a profit, or put themselves in positions of conflict. This is a strict, inflexible rule.

The trustees could have escaped this rule if they had written an exception to it in their trust deed. The basis for this is that in that scenario, there would be fully informed consent from the settlor, and impliedly the beneficiaries.

**Power to invest**

Previously, the common law gave no duty to invest - it needed to be conferred in the trust deed. The Trustee Act 1956 gave trustees the power to invest. Cl 54 of the Trusts Bill 2017 does the same.

*Re Mulligan*

Facts

A owned a property which on his death in 1949, fell to his estate. The property was sold in 1965 and the balance of the estate was $108,000 (equivalent to $1.3m in 1998). A’s widow, BM, had a life interest in the estate and was also a trustee of it, alongside PGG Trust Ltd. The plaintiffs are residual beneficiaries of the estate. From 1969 until 1990 the estate was invested in fixed-interest investments - local body stock and first mortgages. BM was adamantly opposed to investing in equities. During the course of the trust, rampant inflation meant that interest returns were maximised, but cash assets were degraded over time.

BM received a comfortable income as a result. In 1990, on BM’s death, the capital in the estate stood at $102,000.

The residual beneficiaries are aggrieved that the capital in the estate was allowed to significantly depreciate as a result of inflation. They allege that the trustee, PGG Trust Ltd, was not even-handed in his management, favouring the interests of BM as life tenant rather than those of the residuary beneficiaries. The contention is that investment in fixed-interest securities allowed maximum income, at a drastic cost to the maintenance of the real value of the capital. They argued that the trustees should have invested into a balanced portfolio approach to counter inflation.

The trustees (who were accountants, and made trustees for that purpose) admitted that they would have taken such an approach but for BM’s opposition to balancing the folio.

Held

Judgment

The Court found that trustees have **duties to all classes of beneficiaries***,* not just to the beneficiary set to continuously benefit.

In addition, they found that trustees need to **exercise independent judgement**. The trustees should have realised that BM was aiming to maximise her own profit, and should have made a decision themselves rather than following her instructions.

**Trustees have duties of diligence, care and skill**. Because they are professional trustees, they are held to the standard of care, diligence and skill expected of persons of that profession. They would have taken a balanced, portfolio approach - which was also admitted by the defendant trustees.

* Note that trustees only have duties to take reasonable care and skill - this is only a standard of justifiability. It doesn’t expect prudence.

*Trusts Bill - Power to Invest*

The Trusts Bill lays out mandatory and default duties for trustees. Mandatory duties are compulsory and cannot be contracted out of. Default duties apply unless the trust deed excludes or modifies them (expressly or impliedly).

|  |  |
| --- | --- |
| Mandatory duties | Cl 22 - Duty to know terms of trust.  Cl 23 - Duty to act in accordance with terms of trust.  Cl 24 - Duty to act honestly and in good faith  Cl 25 - Duty to act for benefit of beneficiaries or to further purpose of the trust  Cl 26 - Duty to exercise powers for proper purpose |
| Default duties | Cl 27 - General duty of care  Cl 28 - Duty to invest prudently  Cl 29 - Duty not to exercise power for own benefit  Cl 30 - Duty to consider exercise of power  Cl 31 - Duty not to bind or commit trustees to future exercise of discretion  Cl 32 - Duty to avoid conflict of interest  Cl 33 - Duty of impartiality  Cl 34 - Duty not to profit  Cl 35 - Duty to act for no reward  Cl 36 - Duty to act unanimously |

Clearly, **Clause 28 puts a duty to invest prudently on trustees**. Prudence is a higher standard than reasonableness - it requires a smart decision to be made.

* To enable this, Clause 52 gives trustees all general powers necessary to manage and carry out the trust, including all powers of an absolute owner

The mandatory/default duties and general powers awarded in the Trusts Bill changes the current position. The current approach is that trustees have no powers or obligations unless the settlor gives them. Now, **trustees have all powers and obligations unless excluded.**

|  |
| --- |
| Clause 55 provides a list of considerations to assist trustees in exercising investment powers: (a) the objectives of the trust or the permitted purpose of the trust:(b) the desirability of diversifying trust investments:(c) the nature of existing trust investments and other trust property:(d) the need to maintain the real value of the capital or income of the trust:(e) the risk of capital loss or depreciation:(f) the potential for capital appreciation:(g) the likely income return:(h) the length of the term of the proposed investment:(i) the probable duration of the trust:(j) the marketability of the proposed investment during, and on the expiry of, the term of the proposed investment:(k) the aggregate value of the trust property:(l) the effect of the proposed investment in relation to the tax liability of the trust:(m) the likelihood of inflation affecting the value of the proposed investment or other trust property:(n) the trustee’s overall investment strategy. *Re Mulligan would likely have been assisted by a list such as this, though it is similar to what’s in the Trustee Act 1956.* |

Another change the Trusts Bill makes is to the **distinction between capital and income.**

*Note: the common law has a series of tests to decide whether something is capital or income. The general rule of thumb is that income is the fruits of capital, and capital is the base - imagine capital as an apple tree, and income as the apples. Modern shift has been that no distinction exists (the legal distinction is different any accounting measure anyway).*

Section 15(1)(a) Trustees Act 1956 = power for trustees to make renovations to trust property, and to apportion the costs between capital and income. If mostly charged to capital, can recoup the capital using income.

Clause 56 Trusts Bill abolishes any distinction by giving trustees the power to determine whether return on investments are income or capital.

* Clause 57 limits this somewhat by requiring the decision to be fair and reasonable, and consistent with accepted business practice.
* It could be argued that accounting standards are objectively correct, and should just be used consistently. However, the Bill approaches this from the **policy perspective of encouraging trustees to exercise their discretion - and to protect them, as long as its exercise is legitimate.**
  + If a beneficiary brings a dispute and asks for a review, the Court would be entitled to consider investment strategy under Clause 120.

*Re Mulligan* is a prime example of a case where the ordinary layperson would see no issue, until they delve into the issue of whether the trustees acted reasonably and fairly for both classes of beneficiary. The Trusts Bill aims to provide a framework of guidance for trustees to ensure they’re doing this.

***Liability of Trustees***

It is common for a trust deed to purport to absolve trustees of certain liability for breaches of trust. Such clauses are generally accepted as they make good commercial sense, however it is also agreed that there is an irreducible core of trustee obligations that must continue to apply to trustees in order for there to be a valid trust (*Armitage v Nurse*). As a result, trustees' liability cannot be completely excluded completely. The courts have grappled with the content of this irreducible core, leading to slightly different outcomes in different jurisdictions. In the UK, it can be seen that the most liability can be excluded. In NZ, a fair amount of liability can be excluded while the Law Commissions proposals are the strictest.

*United Kingdom*

There is an irreducible core of obligations owed by trustees to beneficiaries fundamental to the concept of a trust. If the beneficiaries have no rights enforceable against the trustees there can be no trust (*Armitage v Nurse*).

The irreducible core of trustee obligations comprises the duty of trustees to perform the trust honestly and in good faith and for the benefit of the beneficiaries (*Armitage v Nurse*). That said, it does not include administrative duties owed by trustees, such as the duty to exercise skill and care, prudence and diligence, in administering the trust (*Armitage v* Nurse).

The effect of this irreducible core is that it is (*Armitage v Nurse*):

* Possible to exclude liability for all breaches, except those arising from a trustee's actual fraud, being a subjectively dishonest intention. Therefore, the following liability can be excluded:
  + Liability for both ordinary and gross negligence, except for professional trustees who charge for their services;
    - Gross negligence is wilful blindness, or in other words a three monkeys approach.
    - **Note**: Lord Millett believed that if to exclude liability for gross negligence is so morally repugnant Parliament should prohibit it.
  + Liability for a deliberate breach of duty that the trustee believes is in the best interests of the beneficiaries, no matter how unreasonable that belief is (because this does not amount to actual fraud);
  + Liability for breaches of administrative duties, such as the duty to exercise skill and care, prudence and diligence, in administering the trust.
* Not possible to exclude liability for a breach arising from a trustee's actual fraud (*Armitage v Nurse*).

*New Zealand*

In NZ, the content of the irreducible core is the same as in the UK. Accordingly, it is possible to exclude liability for all breaches, except those arising from a trustee's actual fraud (*Spencer v Spencer*).That said, the subjective-objective test for actual fraud in NZ is more expansive than the UK test, meaning that trustees can exclude less liability.

This can be illustrated by an example. In NZ there is actual fraud if, based on the subjective knowledge of the trustee, a reasonable and honest person would not have taken the action that they did (*Spencer v Spencer*). Accordingly, a trustee cannot exclude liability for situations in which they honestly believe that the conduct is in the best interests of the beneficiaries yet a reasonable and honest person would not have taken that action. In the UK it is perfectly legitimate to exclude that liability as it does not fall within the definition of actual fraud.

In establishing actual fraud there is a two step analysis:

* First, the court must establish whether the trustee knew that the conduct was a breach of trust;
  + Constructive knowledge will be sufficient if it arises from wilful blindness, which is shutting one’s eyes to the obvious (*Spencer v Spencer*).
* Secondly, the court must consider whether, in light of what the trustee knew, they acted in the way an honest person would have in the circumstances.

*Law Commission*

The Law Commission intended to codify the irreducible core of trustee obligations that could not be contracted out of through a number of mandatory duties for trustees, such as a trustee must (s 10 TB):

* Be familiar with the terms of the trust;
* Act in accordance with the terms of the trust;
* Act honestly and in good faith;
* In accordance with the terms of the trust, act for the benefit of the beneficiaries;
* Exercise stewardship over the trust property for the beneficiaries; and
  + **Note**: stewardship does not require that the trustee conserves the capital of the trust as the capital of some trusts does not need to be conserved.
* Exercise the powers of a trustee for a proper purpose.

The Law Commission also mandates that the terms of a trust must not limit or exclude a trustee's liability for any breach of trust arising from the trustee's own (s 27 TB):

* Dishonesty;
* Wilful misconduct; or
* Gross negligence.
  + Gross negligence is wilful blindness, or in other words a three monkeys approach.
  + **Note**: the Law Commission prohibits exclusion of liability for gross negligence, differing from the conclusion in *Armitage v Nurse*, in order to prevent trustees who come extremely close to actual fraud but fall just short of it from escaping liability. The Law Commission thinks that trustees in such situations are morally culpable.

Further, the Law Commission recommends that where a professional adviser recommends the inclusion of a liability exclusion clause, they must ensure that the settlor is aware of the implications of that clause prior to establishment of the trust. Where the adviser fails to do so, they will not be able to rely on the exclusion clause for their protection (s 31 TB).

**Note**: under the Law Commission's proposalsliability for honest incompetency can be excluded. If applied to the facts of *Armitage v Nurse*, the trustees would therefore still be absolved of some responsibility.

**Armitage v Nurse (UK Court of Appeal)**

P was a final beneficiary under a trust. The trust deed creating the trust contains the following clause: "no trustee shall be liable for any loss or damage which may happen to Paula’s fund … unless such loss or damage shall be caused by his own actual fraud." P alleges a number of breaches of trust, including that capital should not have been paid to a company to maintain P’s mother’s land, that the trustees failed to supervise the company managing P’s land and that the trustees failed to inquire as to the dramatic depreciation of P’s land. The trustees claim that the exclusion clause absolves them of liability for the alleged breach.

The Court first considered what the scope of the exclusion clause is. The Court held that the clause excludes liability for a breach of trust in the absence of a dishonest intention on the part of the trustee. As a result, the trustee is exempt 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. This is because:

* The meaning is unambiguous;
* Actual fraud excludes constructive and equitable fraud:
* As a result, cl 15 excludes liability for breach of trust in the absence of a dishonest intention on the part of the trustee whose conduct is impugned. A dishonest intention may be an intention to pursue a particular cause of action, either knowing that it is contrary to the interests of the beneficiaries or being recklessly indifferent as to that fact.
  + **Note**: a breach of trust may be deliberate yet not dishonest.

The Court then considered whether a trustee exemption clause could validly exclude liability for gross negligence. It concluded that it could, and as a result the exclusion clause was valid, because:

* Such a clause is not repugnant to the trust:
  + There is an irreducible core of obligations owed by trustees to beneficiaries fundamental to the concept of a trust. However, these core obligations do not include the duties of skill and care, prudence and diligence. **The duty of the trustees to perform the trust honestly and in good faith and for the benefit of the beneficiaries is the minimum necessary for, and is sufficient to give substance to, the trust.**
  + It is possible for contracts to exclude liability for ordinary negligence. The same must be true in trust law. It would be strange to be able to exclude liability for ordinary negligence and not gross negligence as this is merely a question of degree.
* Such a clause is not contrary to public policy:
  + No cases establish that it is contrary to public policy to exclude liability for gross negligence by an appropriate clause clearly worded to have that effect.
  + However, it would be contrary to public policy to allow a trustee who charges for his services to rely on a trustee exemption clause excluding liability for gross negligence.
* If clauses such as s 15 are to be denied effect it should be done by Parliament.
  + **Note**: see Law Commission proposed reforms.

Subsequently, the Court considered whether P alleges dishonesty or any breach of trust for which the trustees are not absolved from liability by cl 15. It concluded that her claims amount to gross negligence, but do not prove a dishonest intention, and so are blocked by the exclusion clause.

**Law**:

Actual fraud means that there is a dishonest intention on the part of the trustee. Constructive fraud is not sufficient however an intention in pursuing a course of action may be dishonest if the trustees either know that it is contrary to the interests of the beneficiaries or are recklessly indifferent as to that fact. Yet it should be noted that a trustee may deliberately commit a breach of trust without a dishonest intention if they subjectively believed that the breach was in the best interests of the beneficiaries.

**Spencer v Spencer (Court of Appeal (NZ))**

Mr Spencer settled a trust, called Trust No. 1. The Family Court ordered that a number of the trust’s assets be resettled on Trust No. 2, with terms substantially similar to those of Trust No. 1. Mr Spencer was both a trustee and a discretionary beneficiary of Trust No. 2. Mr Spencer’s Children were also discretionary beneficiaries of that trust. Under Trust No. 2, the trust was to make payments of $200 per week to Mr Spencer’s disabled son, Robert, as long as there was sufficient net income in the trust to make the payments.

The principal assets of Trust No. 2 are a property, managed by SGL (a company owned and operated by Mr Spencer), and a $195,672 debt owed by SGL to the trust. The trustees made no attempt to recover the debt, however offset management fees charged by SGL against it, until it was reduced to nil.

Further, the trust deed provided that “no trustee acting or purporting to act in the execution of the trusts shall be liable for any loss not attributable to his own dishonesty or to the wilful commission or omission by him or her of an act known to be a breach of trust…"

The payments to Robert stopped and the trustees claimed that the trust was in financial difficulties. Robert sues Mr Spencer alleging a breach of trust.

The Court considered whether the trustees were in breach of trust. It concluded that they were, because:

* *Failing to deal properly with the SGL debt*: the trustees made no attempt to recover the debt owed by SGL. Their attempt to offset management fees incurred by the trust against the debt were unauthorised as the trust was expressly prohibited from employing SGL. This was because Mr Spencer was in control of SGL and the terms of the deed and his role as trustee prohibited him from being employed by the trust. This is a clear breach of trust. If the debt had been recovered, there would have been sufficient income in the trust to pay the payments to Robert;
* *Cash management fees*: further, the trust paid SGL $53,000 in cash as management fees. As discussed above, these are a breach of the express terms of the trust;
* *Failure to require rent*: the trust did not require SGL to pay rent for leasing premises in the building owned by the trust. This was a breach of trust.

The Court then considered whether their liability was validly excluded by the terms of the trust deed. It conluded that it was not, because:

* The exclusion clause states that “no trustee acting or purporting to act in the execution of the trusts shall be liable for any loss not attributable to his own dishonesty or to the wilful commission or omission by him or her of an act known to be a breach of trust…"
* The trustees did not act honestly in relation to breaching the trust by not paying Robert the $200 per week due. Objectively considered, they did not act as honest trustees would in relation to the amounts due to Robert. Accordingly, liability for that breach is not excluded;
* The trustees were not aware of the prohibition on SGL charging management fees until after the last cash payment was made and so the liability for the breach is probably excluded. However, the amount of the fees was excessive for a trust that had no income and so in incurring them the trustees cannot be said to have acted reasonably or honestly. Therefore, they are not excused of liability for this breach.

**Law**:

Once a breach of trust has been proven, trustees bear the onus of establishing that they are protected by an exclusion clause. Any exclusion clause is to be construed narrowly against trustees seeking to rely on it (*Wong v Burt*).

The test for dishonesty on the part of a trustee differs in NZ from that in the UK:

* **NZ**: in NZ the assessment of a trustee’s honesty comprises both subjective and objective assessments. First, the court must establish whether the trustee knew that the impugned conduct amounted to a breach of trust. Constructive knowledge will be sufficient if it arises from wilful blindness, which is shutting one’s eyes to the obvious. Secondly, the court must consider whether, in light of what the trustee knew, they acted in the way an honest person would have in the circumstances. This second step is an objective assessment (*Spencer v Spencer*);
  + As a result, a trustee who believes his or her actions or omissions were in the best interests of the beneficiaries will not necessarily be entitled to protection.
* **UK**: in the UK the assessment of a trustee’s honesty is purely subjective. As a result, even a deliberate breach of trust will not necessarily be fraudulent provided the trustees honestly believed that they were acting in the best interests of the beneficiaries (*Armitage v Nurse*).

**Trust busting**

Characteristics of trusts

* Trustees deal with trust property for the beneficiaries, and is under a fiduciary obligation to act loyally
* Trustees are accountable for the way they carry out their legal duties
* Trusts are defined by relationships: settlor to trustee to beneficiary. Trusts do not exist outside of these relationships.
* Trusts are created by intent and certainty.
* Trusts cannot exist forever - the law on perpetuities limits this.

Considering these obligations and the burden they impose, why would anyone want to be a trustee? Sometimes it can be a lucrative career path (lawyers are often trustees). People may also want to support a cause they care about, serve their communities, or fulfil familial obligations. Consequently, we don’t want trustee duties to be so onerous as to deter trusteeship.

Why do we have a law on perpetuities?

* Historical reasoning - that’s always what equitable courts have done.
* Property wants to be owned. The concept at common law requires an owner. However, trust law is constantly *dividing ownership.* This becomes inefficient and complicated over long periods of time.
* If they are never broken, trusts will grow exponentially until they own too much and cannot be ‘owned’ by other people. On public policy reasons, there comes a time when trust property needs to be broken and distributed amongst legal owners again.

|  |
| --- |
| Constructive trusts   * Remedial constructive trusts in response to a breach of fiduciary obligation (e.g. *Keech v Sanford, Boardman v Phipps*) * Instrumental constructive trusts * Conduct of parties leads to implication that they intended to create a trust.   This last category is best seen in the case of *Lankow v Rose:*  A constructive trust was found on the basis of the following test:   1. Contributions to property 2. Expectation of an interest in the property 3. Expectation is reasonable 4. D should reasonably expect to provide P with an interest. |

**Instrumentalism**

‘Trust busting’ mechanisms such as constructive trusts over express trusts have often been criticised because they are viewed as simple tools for the courts to impose their opinions on moral duties.

*Charles Rickett’s* has a number of reasons for criticising this use of constructive trusts:

* It **ignores the process of legal reasoning**. Instrumentalism finds a desired result and works backwards to justify it, but the law is based on a process of reasoning and application of principles to find a result. This maintains integrity - the alternative is an abitrary application of fairness or justice.
* Trusts have important functions in relationships and maintaining and protecting wealth for families. The creation of such trusts requires express intention and certainty. To impose a constructive trust over an express trust **undermines the strength and legitimacy of a trust** and is not an appropriate mechanism.
  + More appropriate is potentially the road of **unjust enrichment.**
* Trusts are set up so that beneficial ownership vests in the beneficiaries, but legal ownership remains with the settlor. This means that giving property to the settlor’s spouse as relationship property is **essentially an award of a person’s property to an unknown third party and can be equated with stealing.**

There can be a conceptual difficulty ascertaining ownership of trust property, especially for discretionary trusts. In doing so, there could be three formulations:

1. Beneficiaries receive no beneficial ownership until the trustee confers it.
2. Beneficiaries have beneficial ownership from the creation of the trust, but it is suspended until the trust is settled.
3. Beneficial ownership is held collectively by the beneficiaries upon creation of the trust. How this will be constituted is uncertain until settlement, but the beneficial interest exists.
   1. *Both Rickett and Geoff prefer this approach.*

**Sham trusts and alter ego trusts**

*Wilson*

Facts

Reynolds settled a house on trust in 1996 with W and H as the trustees. The property was subsequently sold to Reynolds by the trust. The trust then bought a property in Queenstown, in which Reynolds lived. Reynolds went bankrupt and owed creditors $500,000. The Official Assignee contends that the trust is a sham and that the property held on it should be available for Reynolds's creditors. The trust was never administered well and there was intermingling between the affairs of the trust and Reynolds.

Held

The Official Assignee cannot bring a claim procedurally. In addition, the trust is not a sham because there is no evidence it was created with the intention of it being one.

Judgment

On a procedural basis, the claim could not continue. It was brought by the official assignee, who is acting on behalf of the trustee, and incurs all the official rights of Reynolds. Procedurally, a claim cannot be brought against yourself.

* Note: Insolvency Act 2006 now permits this.

The Court continued on, however, to consider whether the trust was a sham. It decided it wasn’t because:

* A sham trust occurs where there is a **common intention [between settlor and trustees] to conceal the true nature of a transaction.** 
  + For example, this might occur when a settlor intends to dishonestly protect property from tax, but has no intention of benefitting the beneficiaries. The settlor makes himself the sole trustee. The true transaction is tax avoidance, rather than creation of a trust relationship.
* **Intention is ascertained objectively depending on surrounding circumstances** (Robertson and O’Regan JJ), but a unilateral intention may not be enough if there are multiple trustees.
  + Glazebrook J dissented, saying intention should be assessed subjectively because sham trusts, by nature, will objectively appear to be trusts.
* If a trust has been intentionally created, it cannot later become a sham trust, though individual transactions might.
* **Control will not be enough** to establish a sham trust if there is no evidence of intention to create one. In addition, **breaches of trust will not establish a sham.** Rather, they will be treated as breaches of trust.
  + However, only the beneficiaries can sue for breach of trust - not the official assignee.
* The circumstances the Court considered were:
  + The trust transferred the Invercargill property to Reynolds’ possession so he could use it as security. This is not evidence of the settlor or trustees’ intention in *creating* the trust.
  + The trust borrowed extra money to purchase the Queenstown property, and used the remaining money to pay off Reynolds’ personal debts. This was unwise, but doesn’t establish a sham transaction or sham trust.
  + Ms C’s attempts to use trust property as security aren’t evidence to intention because Reynold’s likely didn’t know about it.
  + Poor administration of the trust points to a breach of trust, not to it being a sham.

Criticism

Requiring a common intention between parties is a safeguard to protect commercial certainty in transactions. If the trustee fully intends a trust to be created but the settlor does not, this won’t be sufficient to find a sham trust.

Looking into the circumstances to determine intention allows a certain degree of instrumentalism/moralistic application.

* Alternate approach to this = bind them to the trust deed and the obligations in that.

There is the further difficulty that if breaches of trust are treated only as breaches, and not as evidence of a sham trust, trustees will often escape liability - especially if they are a principal beneficiary as well as trustee. In circumstances like this, it will certainly not appear that an authentic trust exists.

* Is this another instrumentalist way of ‘looking to the reality’?
* Should the courts have the power to strike down or bust trusts?
* Why can the approach not be - is there a trust? If yes, you are bound by certain obligations. If no, you are not. This is the approach taken in the Trusts Bill (note: mandatory duties).

**Constructive trusts over express trusts**

The following two cases demonstrate an interesting balance between instrumentalism and property rights.

*Murrell*

Facts

Murrell and Hamilton were in a relationship. During the relationship, a house owned by the W E Hamilton Family Trust (H’s family trust) was renovated and landscaped. During this period, it was occupied by Murrell and Hamilton before being rented out and eventually sold. The trust had two trustees: Hamilton and Mirkin. Trust transactions were handled exclusively by Hamilton, without any consultation with Mirkin.

A constructive trust was argued to exist over the express trust, on the grounds of *Lankow v Rose.*

Held

The Court imposed a constructive trust over the express trust in the form of a 15% interest in the house.

Judgment

The major issue is whether D should reasonably expect to provide P with an interest (limb 4 of the *Lankow v Rose* test). The Court found that he should because:

* The interest Murrell is claiming isn’t a claim for trust property. **It is a claim for her own property:** the interest she expected to gain from making contributions to the property. It is not a value that should rightfully accrue to the trust.

The **beneficiaries cannot expect to retain a benefit they did not deserve and that isn’t theirs.**

* Despite the other trustee not consenting to this allocation of trust property, he is bound by Hamilton’s actions because he delegated his trustee duties to him. Hamilton **could not rely on the prohibition on delegation of trustee duties and lack of trustee consent to avoid equitable constructive trust obligations.**

Criticism- Instrumentalism.

The instrumentalist approach would argue that this undermines the strength and legitimacy of the clear intention required to create express trusts, and that it equates to theft of trust property. The beneficiaries of the trust are strangers to Murrell and would have no such knowledge of any expectation to pay her for work done on trust property.

The correct approach could be in unjust enrichment. The court is essentially trying to use a constructive trust as a method to counter unjust enrichment: one of the reasons they awarded a constructive trust was because of the ‘windfall’ the trust would receive from Murrell’s work.

*Vervoort*

Facts

Duffy settled a trust in 1994. Duffy and Forest were trustees and the trust owns considerable assets in Fiji and NZ. Duffy and Vervoort commenced a relationship in 1999. In 2000, the trust purchased a family home where Duffy and Vervoort lived. Vervoort helped with the property by refurbishing it and establishing a garden. In 2011, Vervoort and Duffy separated. Vervoort claimed relationship property orders and alleged that the trust was a sham and, in the alternative, that a constructive trust had arisen over the trust property, allowing that property to be included as relationship property.

Held

Judgment

The Court found that the trust was legitimate: despite having complete control, there is no evidence that Vervoort **did not** intend to create a trust, and there is no evidence that it became a sham later.

* A co-trustee was appointed, trust accounts were prepared, properties were purchased in the name of the trust and the formalities of a trust structure were put in place and retained. This is consistent with intent to create a trust.
* The Court acknowledged that deliberate changes in circumstance might create a sham, which would mean no characteristics of a trust are present - and consequently, no trust would exist.
  + The takeaway from this is that subsequent conduct can destroy a trust. Does this mean beneficiaries have a legitimate beneficial ownership over property that could simply be taken away from them upon trustees’ breach of trust? This is inconsistent with the notion of ownership.

The Court distinguished *Murrell* because the nature of the contributions made were different. In this case, the contributions are cosmetic rather than substantial. *Murrell*’s contributions could be treated as her property. Cosmetic contributions cannot. This is a relationship property case, and the plaintiff has already been substantially compensated.

However, in doing so, the Court affirmed the decision in *Murrell,* saying it was an appropriate response looking to the reality of the situation. This approach is only giving the plaintiff their rightful property (in other words, contributions) back. It deprives the beneficiaries not from trust property, but from assets they would not have but for those contributions.

**Other mechanisms/relationship property**

*Clayton v Clayton*

Facts

Mr and Mrs Clayton were married. Mr Clayton owned a sawmilling business and a block of land. In 1999 Mr C executed a trust deed, settling the land and buildings on the VRPT. Mr C was the sole trustee of the trust and one of the discretionary beneficiaries (as well as Mrs C and their two daughters). The two daughters were the final beneficiaries. The trust deed conferred unfettered discretion on the trustee (Mr C), permitting him to

* Appoint and remove trustees
* Act without declaring conflicts
* Have all powers and discretions of a natural person
* The power to pay all capital to any of the discretionary beneficiaries
* The power to exercise power without considering interests of all beneficiaries
* Power to act in a way that might be contrary to the interests of all beneficiaries

Upon their separation, their relationship property agreement means Mrs C gets $10,000 per year of the relationship, up to a cap of $30,000. But considering Mr C is worth $25mill, this seems very unsubstantial.

Held

There is a valid trust, but the wide discretion conferred on Mr C as trustee and beneficiary can be viewed as a right and interest for the purposes of relationship property.

Judgment

The Court first investigated whether the trust was a **sham or illusory trust.**

They rejected the language of an ‘illusory’ trust, and instead simply investigated whether a trust exists or not.

They did this in two steps:

Firstly, did the settlor intend to create a trust? The test for this is ascertained objectively, but subjective intention is a relevant consideration.

Secondly, looking to the **practical effect of the trust deed,** was a trust created?

* The existence of vast powers or wide discretion does not preclude the existence of a trust when they haven’t been used. Though the trust is defeasible, nothing has been done to deprive the beneficiaries or act against their interests.
* In addition, reliance on advisors and lack of knowledge of legal ramifications of a trust do not mean he did not intend to create one.

Despite finding this, the Court made no comment on whether sham or illusory trusts exist in NZ, but commented that **trusts will not be valid unless they have a specified end date** (law of perpetuities makes the maximum length of time 80 years).

Despite finding that a trust had been created, the Court also found that because **Mr C’s discretions and powers were so broad and unfettered, they could be considered as property**, and found a constructive trust in favour of Mrs C. They decided this because:

* The definition of ‘property’ in the PRA includes a ‘right’ and an ‘interest’. This is clearly broadening the scope of relationship property.
* A general power of appointment is tantamount to ownership and can be treated as property. He would be able to allocate all property to himself (expressly permitted in the trust deed) and was not bound to consider other beneficiaries.
* The trust powers should be viewed as rights which give Mr C and interest in the trust property, thus making it relationship property.

Criticism

Given the broad discretions conferred on him, it could be argued that there was never an intention to act in the interest of the beneficiaries, and thus a trust was never created.

Instrumentalist approach - relationship property was always going to be an issue when it’s $30,000 compared to $3 mill. But they had a relationship property agreement, and this was deliberately included as trust property. What happened to freedom of contract and the ability to treat your property as you wish to?

Additionally, the Court has demonstrated that valid, existing trusts can be busted by relationship property claims if they can be conceptualised as rights or interests.

**Constructive trusts**

We’ve already seen constructive trusts used in a few ways: we’ve seen them used over property attained in breaches of fiduciary obligations (*Keech v Sanford; Boardman v Phipps)*, and we’ve seen them used over express trusts (*Murrell; Vervoort; Clayton*).

There are two ways we might use constructive trusts:

1. In the *Lankow v Rose* situation of **contributions; usually related to relationship property** (*Murrell; Vervoort)*
   1. The claimant has made contributions, direct or indirect, to the property in question;
   2. The claimant expects an interest in the property;
   3. That expectation is reasonable; and
   4. The defendant should reasonably be expected to yield the claimant an interest.
2. Where property has been improperly acquired by a fiduciary (*Boardman v Phipps; FHR; Reid)*
   1. **Secret profits** (*FHR; Boardman v Phipps)*, irrespective of whether this was done fraudulently or not *(Boardman v Phipps)*
   2. **Secret commissions**, where commissions are taken in the course of trustee duties, without fully informed consent of the principal *(FHR)*
   3. **Bribery** - if a trustee/fiduciary accepts a bribe in the course of his duties, it’s held on trust for the principal *(Reid)*

*Reid*

Facts

Reid was a prosecutor for the Government of Hong Kong, owing a fiduciary duty to the Crown. Reid accepted a number of bribes from criminals for altering his prosecutions and was subsequently caught. Reid used the bribe to buy three houses in NZ in the names of his lawyer and his wife. The Crown established that Reid was liable for the bribe, yet he was bankrupt. In order to recover the amount owed, the Crown wants to establish a proprietary right in the houses. It claims that the bribe money was held on trust for the Crown and, since the wife and the lawyer are not BFPFVWN, can be traced in equity into the properties.

Held

The purchased houses are held on constructive trust for the Hong Kong government.

Judgment

The Courts were presented with a UKCA decision *Lister v Stubbs* which had decided that agents who take bribes *do not* hold it on constructive trust for their principals. This was based on the principle that you should only have a property interest in gains derived from your initial property (i.e.: theft of your property).

The Privy Council here held that that decision was wrong based on fundamental and well established equitable principles:

* Fiduciaries must not be allowed to benefit from their breaches
* Fiduciaries should account for bribes as soon as they receive them
* Equity regards that done as ought to be done.

Consequently, as soon as Reid received the bribes, they were considered the property of the Crown. Equity acts *in personam.* The entire claim is based on the *unconscionability* of the fiduciary, not on the grounds that the principal has suffered loss. This is viewed in Lord Templeman’s judgment - “bribery is a blight on the world”. This almost implies a public policy approach as well.

The Court also decided that, because it was established in *Boardman v Phipps* that a benefit gained by a fiduciary was on constructive trust for the principal *even if gained honestly and without fraud,* fiduciaries who act dishonestly and criminally in accepting bribes that cause harm must also hold them on constructive trust for their principal.

*FHR*

Cedar acted as FHR’s agent in negotiating the purchase price of the Monte Carlo Hotel. Cedar evidently owed FHR fiduciary duties in this capacity. Cedar had an agreement with the vendors of the hotel that if a sale was successful Cedar would receive $10m. Upon conclusion of the sale, Cedar received that commission. FHR sues Cedar for breach of fiduciary duty, claiming that the commission is held on constructive trust for FHR.

* **Note**: this case can be distinguished from *Reid* as the benefit obtained by the fiduciary here was not illegal, but merely immoral.

Held

The secret commission was held on constructive trust for FHR.

Judgment

Agents owe duties of undivided loyalty to their principals - this is the nature of a fiduciary relationship. He also owes a duty not to put himself in a position of conflict with the principal’s interests. These fiduciary duties and obligations are not debated. A fiduciary who accepts a secret commission is clearly breaching both of these duties.

* Because agents are acting on behalf of and in the interests of their principals, the principals are entitled to the benefit of the agent’s acts in the course of his agency.
* In addition, he will actually suffer detriment if agents accept such secret commissions. He suffers an economic disadvantage, paying more for his property than he would if his agent had been loyal.

The principal should be compensated for these breaches and his economic disadvantage through a proprietary remedy.

The Court considered whether this would prejudice the agent’s unsecured creditors, but decided that it would not because the bribe money should never have been the agent’s property anyway, as it was obtained dishonestly and in breach of his fiduciary obligations. In fact, it would be a windfall for the creditors.

* This could be criticised in saying the money would not be in the estate but for them lending it. However, creditors have the option of security: the principal does not. It’s more justified to go to the vulnerable, unprotected principal.

**Criticism of the ‘constructive trust’ approach**

There is no doubt that breaching fiduciaries owe an obligation to repay the bribe money in a personal capacity. Most of the debate surrounds whether this should be a proprietary right awarded to the principal. The major issue of this approach can be broken into three parts:

* Conceptual problem

By finding a constructive trust where fiduciaries have been acting dishonestly or immorally, the Court is saying the property belongs to the principal, and *has always belonged to the principal.* The issue with this is that the profit was made through dishonest behaviour: through a breach of fiduciary obligation. It makes sense in cases like *Boardman v Phipps,* where the fiduciary was acting openly, and it would have been to the benefit of the trust if they could have acted.

But accepting bribes is not in any way in the interests of the principal. The agent is NOT ACTING FOR THE PRINCIPAL when they accept bribes or commissions. How can it be conceptually justified to say the principal has a property right to that, that the bribe is theirs? How can a principal intend to own property achieved through dishonest acts towards them?

This is also at odds with insolvency law and the principles developed there of ranking creditors. If an agent accepting a bribe or commission is insolvent or bankrupt, why should the principal have any more right to that money than the creditors?

* Precedent problem

*Lister v Stubbs* is clear, strong precedent. What basis does the Court have to depart from this? They clearly have no conceptual basis to do this on. Admittedly, the PC has authority to do this, because that case was decided in a lower court. But courts are usually hesitant to overrule settled law.

The PC justified it on equitable principles, but really it seems to be more of an issue of instrumentalism. Perhaps unjust enrichment would have been more appropriate.

* Consequences problem

Essentially, by finding a constructive trust where fiduciaries have been acting dishonestly or immorally, the Court is saying the property belongs to the principal, and *has always belonged to the principal.* Consequently, the principal can trace bribes or secret commissions, even if they’ve passed into different hands or into different forms of property, because they *own it.* This means subsequent owners can be disadvantaged, and principals are getting a windfall they never technically had a right to.

In fact, in a previous case, Lord Neuberger said that such a proprietary remedy would have negative commercial ramifications, but he has obviously reconsidered this.

Counterargument

On the other hand, why should creditors have any right to money gained at your expense? It’s an unexpected benefit for them, and not one in the ordinary course of business. It’s not a profit they should expect any right to.

**Mechanisms in the Trusts Bill**

|  |  |
| --- | --- |
| *Part 3*  Mandatory and default trustee duties. | A trust cannot exist unless the mandatory duties in the Bill exist. This is based on the ‘irreducible core of obligations’ discussed in *Armitage v Nurse*. |
| *Cl 77*  Trustee liability for expenses and liabilities incurred, and a right to indemnity. | This puts a personal obligation on the trustee to repay debts. We don’t NEED a constructive trust over trust property: the trustee is liable to pay for people’s contributions (e.g. *Murrell)* |
| *Cl 79*  For purposes of 77(1) and despite 77(2) terms of trust can rank the order in which the trust property must be applied in order to reimburse trustees, or pay/discharge an expense or liability. | This is particularly important for Maori trusts which protect taonga.  Indemnities might be severed if there’s evidence of lack of good faith.   * However, the remaining concern is that when indemnities are severed because of bad faith, creditors etc cannot get trust property, and usually that breaching trustee has no assets that can be used to repay debts. |
| *Cl 80*  Creditor’s limited claim to trust property through trustee’s indemnity | This is an attempt to resolve the issue expressed above. It’s on the basis of unjust enrichment (the trust is unjustly enriched because of the creditor’s loss).  However, it doesn’t affect those who are owed money but aren’t creditors because they haven’t given value, like IRD (in the collection of GST). There are a few reasons why:   * Trusts aren’t things, they’re relationships. They can’t incur liabilities like taxes - only the trustees can, so only the trustees can be liable for that. * A conceptual difficulty would also arise where both the trustee AND the trust would have the same liabilities. |

The above claims are*in personam (personal).* This is very different to the claim in Murrell, which was *in rem (property).* It’s on that basis that Murrell was criticised.

**Creating Express Trusts**

In order to create a trust, a certain degree of certainty is required (similar to certainty of contract). The three main ones are:

* Certainty of intention to create a trust
* Certainty of subject matter included in the trust
* Certainty of objects (basically just means certainty of beneficiaries).

**Certainty of intention**

To establish certainty of intention, two things need to be shown.

1. **The substance of the intention - that the intention was to create a trust, rather than to do something else.**
   1. E.g. *Thexton* intention was to do something; carry out some action. Subsequent conduct showed that nothing ever happened, and David Jr never acted in any way that demonstrated he was acting in the interests of David Sr’s beneficial ownership.
   2. E.g. *Jones v Lock* intention was to gift.
2. **The existence of the intention - factual evidence that such an intention existed at the time.** 
   1. E.g. *Korda*,

Dividing the two in analysis is important because it avoids relying too much on hindsight.

*Paul v Constance*

Facts

D separated from his wife, B, however they did not get divorced. D began to see DG and put £950 into a deposit account at the bank in his own name. He stated, on many occasions, that the money in the account was as much DG’s as it was his own. Further, bingo winnings that D and DG had won together were also placed into the account. D died intestate and his wife, B applied for letters of administration. DG applied to have half the money in the account transferred into her name, claiming that an express trust had been established over it with her and D as the joint beneficiaries. The question for the court was whether there was a valid trust.

Held

The Court found that an express trust was created.

Judgment

There was no express intention to create a trust - no clear statement saying “I wish to create a trust”. There was no outlining of any particular terms of the trust.

However, the Court analysed D’s statement ‘this money is as much yours as mine’ and found that, in the context of the relationship between D and B, this was enough.

* Bingo was a joint enterprise. When they won, money was put into a combined pool.
* The words aren’t a clear creation of a trust, but they express joint ownership.
* The use of the **present tense** is key. It doesn’t imply future ownership or any gift, but **current equal ownership.**
  + Contrast *Jones v Lock:* “this money is for the son” when handing over a check is not a creation of trust; it’s a gift (it’s mine now, but I’m handing it over to my son).
  + No way in this instance that you could construe *both the son and the father having ownership of the money.*
* It’s akin to saying “this will be held by me on your behalf, from now on”.
* In the absence of express wording, a declaration of trust is the same as a declaration of ownership right now.

*Thexton v Thexton*

Facts

David Junior started a company, Rio. When David Senior left his ordinary job it was agreed that he would become an employee of the company and hold a 50% shareholding. However, on taking up the position, David Senior was only allocated a 20% shareholding. David Junior held the rest of the shares and during a merger between Rio and Cerebos Greggs it was agreed that David Senior would step back from the business. David Junior contends that him and his father had reached a binding agreement by which David Senior would sell to him his 20% shareholding in Rio for $250,000. David Junior stated that David Senior agreed to hold the shares on trust for him, signing a trust deed backdated from 1997 to 1988. David Senior died before transferring the legal ownership of the shares so now the Court is attempting to determine who has the beneficial ownership of the 20% stake.

Held

There is no certainty of intention to create a trust.

Judgment

The Court found that there was an intention that David Sr would hold 50% of the Rio shares. This is also acknowledged by David Jr. Some sort of promise existed between the two of them. That 50% was never transferred. However, there is no obligation to perform a promise unless it’s legally binding.

* This could be done through contract law. Without consideration, the promise isn’t binding on the settlor.
* **Equity will not assist a volunteer** [someone who has not given valid consideration].

We can still infer an intention to create a trust if the circumstances permit it. However, the Court found that there was no evidence of conduct that shows David Jr was dealing with them in a way so that David Sr would acquire a beneficial interest in them.

While this is using a degree of hindsight to ascertain intention, this isn’t necessarily excluded from the analysis. The biggest difference is that here, there is a promise to do something that was never carried out. It’s very different from saying *“these are yours; you own them just as much as I”,*

*Korda*

*Australian High Court*

Facts

There was an investment scheme in place where investors were entitled to the net proceeds of timber for particular plantation areas of the Forest Company and the Milling Company.

The proceeds (less cost) were paid to the Australian Executor Trustees Ltd (a trustee company) for the purpose of distribution among the investors.

There were multiple agreements between all the parties. However, the Trust Deed in place between the trustee company and the Forest Company had no provision declaring or providing that the arrangement was a trust, and that the Forest Company was to act as trustee.

Consequently, the Court had to establish whether a trust could be inferred by the conduct and circumstances of the parties.

Held

There is no express trust.

Judgment

Intention is assessed by looking at the facts and circumstances at the time the transaction was entered into. The Courts are hesitant to rely too heavily on hindsight.

that this was more likely, after **considering the consequences of finding a trust**:

* The parties would have an entirely unnecessary contractual indemnity: a clause in the agreement permitted the Forest Company to take costs from the money before handing over for distribution. However, if a trust WAS intended, the Forest Company, as trustee, would have the right to be indemnified for their expenses or liabilities.
* There would be different tax treatment of the investment fund depending on whether the parties have a contractual agreement to receive money or beneficially own it. The deal may have been structured specifically to *avoid* beneficial ownership.

The Court found that the **most likely combined intention of the parties was to create a contractual obligation**, not to create a trust. If the milling and forestry company had wanted to create a trust relationship, they could have. However, they chose not to, because contractual obligations suited them more. Freedom of contract principle - can contract for what you want, but the courts won’t give you something you could have bargained for, but didn’t.

The Court acknowledged that AET is a trustee of the funds for the benefit of the investors, but that the forestry and milling companies are not beneficiaires of it.

**Certainty of objects**

Certainty of objects is key to the creation of a trust. If the trust’s divestment clause states that all the trustee’s children will receive equal shares, it’s crucial to know how many children there are because that would completely change the percentage each beneficiary would receive.

*Re Gulbenkian*

*HoL*

Facts

Oil magnate. He has an absolute discretion to pay all or any part of the Trust Fund income to “any person or persons whose house or apartments or company or under whose care or control or by or with whom the said X may for time to time be employed or residing…”

Held

Certainty of objects will be satisfied where it can be said with certainty whether or not a given individual is a member of the class or not - but will not fail simply on impossibility of ascertaining every member of the class.

Judgment

Trust powers are different from fixed interests. They are deliberately set up to give the trustee discretion in its exercise. The power must be exercised, but the way in which it is exercised is left to the trustee’s discretion.

The Court decided that a fixed list is not necessary to have certainty of objects. However, there must be some guidance so as to make the objects identifiable and determinable.

* There will be certainty of object **where it can be said with certainty whether or not a given individual is or is not a member of the class. Yet it will not fail simply because it’s impossible to ascertain *every* member of the class.**

*McPhail v Doulton*

Facts

Baden executed a trust deed and established a fund for the benefit, broadly, of the staff of the respondent company: Matthew Hall & Co. Baden died in 1960 and the executors of his will contest that the trust fails for uncertainty of object.

Judgment

The Court considered *Re Gulbenkian* and affirmed that you do not need a list of all possible objects: an ability to ascertain whether an individual is a member of that class is sufficient for certainty of objects.

They also noted a distinction between ‘trust powers’ and ‘mere powers’.

* Mere powers are powers that can be exercised discretionarily. *Re Gulbenkian* governed: identifiable and determinable class, though certainty won’t fail if it’s impossible to identify *all* objects.
* Trust powers are powers that *must* be exercised. The entire range of objects must be ascertained, or able to be ascertained.

The ‘complete ascertainment’ test is based on the principle that, should the court need to step in and exercise the trust powers, they must be able to identify all beneficiaries in order to distribute trust property evenly.

However, discretionary trusts do not require equal shares - this was not what was envisaged when the trust was made discretionary rather than fixed. Consequently, the same test should apply for both ‘mere powers’ and ‘trust powers’.

The Court draws a **distinction between conceptual uncertainty and factual uncertainty:**

* Conceptual uncertainty, where it is difficult to ascertain what the criteria is for objects, is uncertainty that will void the trust.
* Factual uncertainty, such as difficulty locating family members, will not.

*Re Baden’s Trust Deed; following on from McPhail v Doulton*

The executors submit that the words “relatives” and “dependents” import uncertainty so as to make the trust invalid.

The Court decides that neither term is uncertain.

* ‘Dependents’ are people dependent for the ordinary necessaries of life. As a result, the difficulties in ascertaining if someone is dependent is evidential, and raises questions of fact, not of law. It is not legally uncertain.
* ‘Relatives’ are people who trace common descent from an ancestor. It must be understood as meaning someone who would introduce themselves as a relative. Again, this is a factual issue, not a legal one.

**Certainty of subject matter**

*Goldcorp*

Facts

Goldcorp purchases gold, silver and other metals. Consumers purchase gold from Goldcorp, but sign an agreement that says “Upon payment, you get a non-allocated receipt which verifies your ownership of the metal. It is stored and insured free of charge. You will receive physical delivery upon seven days of notice”.

However, Goldcorp required this notice in order to acquire more gold. They did not have enough in their stock at any given time for all of their customers. They also had floating security charges over their gold from money borrowed from banks. Goldcorp went insolvent - the banks had first priority to the gold, despite the fact that consumers thought they owned it.

Held

There is no means to identify which gold is owned by which consumer because it is a generic bulk of fungible goods.

Judgment

The Court of Appeal decided that despite the contract, and despite the legislation, the plaintiffs owned the gold. However, a number of judges speaking at conferences after this criticised this, saying its **very important to recognise certainty in commercial dealings.**

The gold was non-allocated, and there was not enough in the pool for all consumers to receive what they had paid for. CCLA s 143 (at the time, Sale of Goods Act) = under a K for sale of unascertained goods, no property in goods is transferred to the buyer unless and until the goods are ascertained.

The purchasers had a contractual right to the gold, but no proprietary right, so the bank’s interest took priority.

This would be the case unless the consumers had beneficial ownership over the gold and Goldcorp had been holding it for them in trust. The Privy Council found that there was no certainty of subject matter.

* **These were generic, bulk goods from a pool of the same, fungible assets.** There is not enough in the pool for everyone with a right to it. There is **no basis for identifying *which* gold each consumer’s contractual right attaches to.**
* Although the contract was deficient and the consumers did not get what they contracted for, equity cannot just use trusts as a vehicle to give them what they want.
* The contract is unenforceable due to lack of certainty of subject matter. The same thing cannot be argue for a trust, because the same requirement isn’t met.

Estoppel could not succeed because the defendants were the bank rather than Goldcorp - and the bank made no promises to the plaintiffs.

*Following Goldcorp; Hunter v Moss*

Decided that, where you apportion a certain number of shares in a trust, there is no need to ascertain *which* shares are in the trust, because they are all exactly the same. They have the same value and are completely interchangeable.

*Criticism:* the gold in *Goldcorp* was all of the same value, all interchangeable. The only difference that could be argued here is intangible goods vs tangible goods, but it doesn’t seem as if this is why the case was decided differently.

Lead to uncertainty, which was the context leading in to *White v Shorthall.*

*White v Shorthall*

*NSW Supreme Court*

Facts

“I give a trust over a certain portion/number of my shares”. Is this sufficiently certain subject matter?

Held

Not satisfied with the tangible/intangible distinction in *Hunter v Moss.* To divide and allocate a certain number of shares to someone, need to identify which shares are theirs. However, you can create an interest over the entire subject matter (ie: a 50% interest in all of the shares).

Judgment

The Court was unconvinced by any difference of test for tangible or intangible property, as possibly expressed in *Hunter v Moss.*

However, the Court decided that you could create a trust over the *entirety* of subject matter, and certainty would be satisfied as long as trustees have the power to split that number of shares off from the rest.

So, someone can have a **50% interest in all of the shares in the trust. But they can’t have half of the shares unless it’s been identified *which half.***

*Wakatu*

Facts

Arises out of the Nelson Tenths trust. A NZ Company settlement. One of the Wakefields’ ideas was that a certain portion of purchases should be retained for the benefit of the person who you buy the land off. So much land in Wellington and Nelson is held in a Nelson Tenths trust for the benefit of the tangata whenua. The idea is to put aside one tenth of the land.

Within some time, the NZ govt was taken over by the Crown. The Crown did not honour its obligations under this arrangement. The land was never allocated.

Held

A trust exists. There is certainty of subject matter.

Judgment

Traditional English law would hold that there was no certainty of subject matter, especially because the land is not fungible (ideally, we would promote certainty around goods that aren’t fungible). The material facts are similar to Goldcorp:

* Promise to allocate
* Existence of contract
* Purchase on basis of allocation
* There was no allocation

This implies that the law would find that a trust cannot be found to exist for lack of certainty of subject matter.

Elias CJ finds very clear intention to create a trust. She also finds that there was a **formula** in the contract to determine how the land would be allocated, and an **identified geographical area** to which that formula would apply. She finds that the **reason we don’t know what specific land is allocated is because there was a breach of trust,** not because we don’t have a trust in the first place.

* Elias CJ distinguished this from *Goldcorp* because of a distinction between tangible property and real property. In *Goldcorp*, they were dealing with unidentified, generic goods that were stored in bulk in a pool of identical goods. That is much less certain than here, where we have a specific proportion of land from a fixed, predetermined source. This is weighted even heavier when it relates to native title.

Elias CJ also draws attention to the difference between conceptual uncertainty and factual uncertainty (as discussed in certainty of objects). If there is conceptual uncertainty, there is no trust. Factual uncertainty does not preclude the existence of a trust.

* The test for conceptual uncertainty is whether the Court is able to determine with certainty the limits of the class of subject matter.
* Here, with a formula for allocation, and a specific area to allocate land from, the Court *is* able to determine the subject matter. Legal certainty is satisfied.

Criticism

Elias CJ has made an effort to ground her reasoning on equitable principles and law, rather than any public law notions of sovereignty/native title. However, there are some flaws which indicate that the CJ was attempting to find the right outcome and fitting the law to that, as opposed to reaching a conclusion through legal principle.

The CJ’s distinction between tangible and real property should almost go the other way. Because land is unique and a signfiicant asset, we should promote MORE certainty around subject matter than less. The contrary would be undesirable,

Can it be said that the tangata whenua and NZ government really intended, at that time, to create a trust? Was a trust a concept known to the tangata whenua, or contemplated by the government in its negotiations? It seems as if this is an interesting merge between NZ law and tikanga - is this the future of NZ law? Considering no cases have arisen since, it’s very unclear. It almost comes across as a political trust: the courts trying to correct the Crown’s moral breach of agreement.

**Provision of information to beneficiaries**

Law Commission = there are some trusts that don’t tell anyone they exist, or some trustees that only tell some beneficiaries information about administration of the trust etc.

The common law has always struggled with ensuring that trustee duties are enforced. They can usually only be enforced by the beneficiaries. But if the beneficiaries are unaware of who the trustee is, how the trust is being administered, or who is allocated trust property, they will not be able to enforce it.

This is particularly difficult in NZ, where most of our trusts are discretionary. In fixed trusts, where beneficiaries know what they will get when the trust divests, the right to information can be viewed in a property right itself. But for discretionary trusts, beneficiaries *might* benefit, or they might not. How then is this enforced?

*Erceg v Erceg*

Background context: *Smith v Rosewood (PC)*

The right to information does not turn on the property interest of beneficiaries. Courts have supervisory jurisdiction to ensure trusts are properly administered. The courts best go about this by finding a right of beneficiaries to receive certain information.

Beneficiaries must receive sufficient information to enable enforcement of the trust and its administration. This is not about substantively what the courts would have done, but procedural - did the trustees act reasonably in administering the trust, within the bounds of the trust deed?

Facts

Michael Erceg died in helicopter crash. P got money from will. Later, trust divided up - he was bankrupt - later requested accounts etc from the trust.

Do trustees need to disclose information about the administration of trusts to beneficiaries?

Held

No obligation to disclose information, after considering the interests of all beneficiaries.

Judgment

The Court held that it is up to the Court to ensure trusts are administered correctly. One method of doing so is to order disclosure of information to beneficiaries, to allow them to enforce the trust. The Court (disagreeing with the CA) held that it is up to the discretion of the court as to whether disclosure should have been made.

The Court decided the appropriate way to determine whether disclosure should be ordered is by considering:

* What is best for the administration of the trust
* What is best for the interests of all of the beneficiaries, not just the beneficiary requesting disclosure.

Usually, if there is no other way for beneficiaries to monitor compliance with the trust deed, disclosure will be ordered. For trust documents, there is a general expectation of disclosure, unless circumstances preclude this (note this is only for trust documents, not for the trustees’ reasons in doing something).

In ascertaining this, the Court considered:

* The documents sought (which may sometimes be evaluated separately)
* The context for the request and objective of B in making the request
* The nature of the interests held by B seeking information
* Issues of personal or commercial confidentiality
* Whether the disclosure would disclose reasons for the trustee’s decisions
* The likely impact of disclosure on the trustee and other beneficiaries

On the balance, the Court decided that disclosure was not warranted. He was unable to benefit at the time, and he was likely going to harass the other beneficiaries. In the interests of all beneficiaries, disclosure was not justified.

*The Trusts Bill*

Interestingly, the SC decided *Erceg v Erceg* in the course of the Law Commission’s work on the Trusts Bill, and it actually ended up being very similar to the Law Com’s approach.

As discussed above, the Law Commission is concerned about the enforcement of trusts. Yet the public expressed a real concern that if beneficiaries knew of their position, they may ‘ease up’ on their everyday work life because of their expectation.

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| Trustees must retain documents | * Trustees must keep core documents (cl 41) * Must keep documents where there is more than 1 trustee (cl 42) * Documents must be kept for duration of trusteeship (cl 43) * Trustee must pass on documents (cl 44) |
| Presumption of openness for important trust documents, unless there are exceptional circumstances (cl 47)  This applies to the provision of information and response to requests for disclosure. | Basic trust information is (cl 47):  (3) The basic trust information is— the fact that a person is a beneficiary of the trust; andthe name and contact details of the trustee; andthe occurrence of, and details of, each appointment, removal, and retirement of a trustee as it occurs; andthe right of the beneficiary to request a copy of the terms of the trust or trust information. |
| In considering whether the presumption applies, the trustee/Court should consider certain factors (similar to the factors used in *Erceg).* | Cl 49   1. the nature of the interests in the trust held by the beneficiary and the other beneficiaries of the trust, including the degree and extent of the beneficiary’s interest in the trust and the likelihood of the beneficiary receiving trust property in the future 2. whether the information is subject to personal or commercial confidentiality: 3. the expectations and intentions of the settlor at the time of the creation of the trust (if known) as to whether the beneficiaries as a whole and the beneficiary in particular would be given information:  the age and circumstances of the beneficiary:the age and circumstances of the other beneficiaries of the trust:the effect on the beneficiary of giving the information:the effect on the trustees, other beneficiaries of the trust, and third parties of giving the information:in the case of a family trust, the effect of giving the information on—relationships within the family:the relationship between the trustees and some or all of the beneficiaries to the detriment of the beneficiaries as a whole:in a trust that has a large number of beneficiaries or unascertainable beneficiaries, the practicality of giving information to all beneficiaries or all members of a class of beneficiaries:the practicality of imposing restrictions and other safeguards on the use of the information (for example, by way of an undertaking, or restricting who may inspect the documents):the practicality of giving some or all of the information to the beneficiary in redacted form:if a beneficiary has requested information, the nature and context of the request:any other factor that the trustee reasonably considers is relevant to determining whether the presumption applies. |
| Cl 118 - the Court can review trustees’ act, omission or decision. | This is in place because settlors choose trustees for some reason. The Court takes this seriously: there is a real obligation to carry out the duties the settlor imposed.  The review is based on whether the trustee’s decision was reasonably open in the circumstances. |
| Cl 50(2) The trustee must apply to the court for directions in relation to— Whether the trustee’s determination that there is no beneficiary to whom information can be given, or to withhold information or refuse a request for information, is reasonable in the circumstances; andthe alternative means by which the trustee can be accountable and the trust can be enforced. | Not required to apply if the period where no B has info is less than a year, and at the end of a year, T gives to at least one B, basic trust info and reasons for not providing it earlier.  This is in place because trustees cannot be the safeguard to ensure that their own decisions are correct. *Someone* needs to get the information to ensure that the trust is being administered correctly, and the court has supervisory jurisdiction.  However, going to Court is costly. Will trustees simply ignore this section (how would it be policed or enforced? By the beneficiaries?), or will this over-incentivise disclosure of information? |

The Exposure Draft had a three-pronged approach based on the *Smith v Rosewood* ratio:

* Sufficient info to sufficient beneficiaries in order for the trust to be enforced
* Initial disclosure (must tell B they’re beneficiaries)
* Some degree of continuing disclosure to some beneficiaries

This usually means *qualifying beneficiaries-* those who are likely to benefit. However, this confused people and the feedback relayed concern over the relationship between the first principle and the next two, as well as concern over its application (which beneficiaries? How much information?)

They redrafted to contain two obligations instead:

* Obligation of initial disclosure
* Obligation to consider releasing information upon request from beneficiaries

Both obligations are subject to the presumption laid out in the Bill.

**Court powers and dispute resolution**

As discussed, the court has supervisory jurisdiction over trusts - they need to ensure that they’re administered fairly. So, what is supposed to happen when trustees have acted reasonably and in good faith, but the beneficiaries are aggrieved due to harm caused by the quality of the decision?

There are two potential approaches:

* What would a reasonable person have done?
* Was the decision within the scope of the trustee’s powers and obligations?

The Law Commission found that the purpose of a trust is for trustees to use their discretion to make decisions. The settlor chose them for a reason - because they trusted them to manage and administer the trust. Consequently, the Trusts Bill opted to analyse whether the decision was within the scope.

|  |  |
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| Clause 118 - Court can review trustees’ act, omission or decision | Can review on the ground that the act, omission, or decision was not or is not reasonably open to the trustee in the circumstances, if the claim was brought by a beneficiary. |
| Clause 119 - Procedure for Court’s review | Once the beneficiary has proven a genuine and substantial dispute, the onus is on the trustee to prove that the decision was open to him. |

This is a difficult claim for a beneficiary to prove - especially considering the Court’s review is procedural, and not an outcome-based, substantial review. There are real practical difficulties for beneficiaries bringing these disputes:

* They don’t have access to full information - the only people that do are the defendants.
* Practical difficulty of proving discretion is exercised illegitimately when they have no evidence.
* In practice, Courts frown upon plaintiffs who file multiple claims for discovery.

Clause 119 is intended to resolve some of these dilemmas by reversing the onus to the trustees once a potential claim has been established. However, the Law Commission has received feedback that even this is permitting beneficiaries too much power, and disincentivising trustees from acting.

The Court also has the power to relieve trustees from personal liability. This is in s 73 Trustees Act 1956 (discussed in *Re Mulligan)* and cl 123 Trusts Bill 2017.

* The objective is to protect trustees who act reasonably and in good faith. As shown in *Re Mulligan*, this won’t excuse a trustee who was aware of the course of action they should have taken.
* It also aims to incentivise the use of trustee discretion. The use of discretion doesn’t need to be the *correct,* most desirable use, but it does need to be used, and within the scope of powers and obligations.

This essentially adds another layer of protection for trustees.

**Resulting Trusts**

* Resulting trusts may occur **when a trust hasn’t successfully formed.**

For example, if the settlor intends to create a trust and hands property over to the trustee to manage, but a trust is never formed due to some technicality, a resulting trust over the property may be created for the benefit of the settlor. This is because the property was never intended to be the trustee’s, but a trust was never created to benefit the beneficiary. A resulting trust occurs to ensure the fairest result - the settlor gets their property back, even though the trustee has legal ownership.

* Resulting trusts may also occur **when** **property is handed over, but it’s unclear whether it was a gift or not.**

In such a situation, there is a presumption in law [in absence of evidence of a gift] that the settlor intended to retain beneficial ownership of the property.

This is subject to the **presumption of advancement** - that family members (spouses, parents) intend to gift to each other.

*Crampton-Smith*

Facts

The brother, based in Australia, purchased two plots of land for a combined total of $23,000 and asked his sister to register them in his name and fill out all required documentation. She registers in her own name, works on it, and increases its value. The sister goes to sell the property for $511,000. The brother discovers this and lodges a caveat over the properties.

The sister is arguing that he lent her the money, and she owes him $23,000 in debt, plus interest.

The brother is arguing that he created a trust over the money/property and his sister was acting as trustee, and is correspondingly responsible in equity for the profit she made in breach of that trust.

Held

Remedial resulting trust - when A transfers property to B on an express trust, but the full beneficial interest is not exhausted, the property comes back to A.

Judgment

The Court examined Lord Browne-Wilkinson’s judgment in *Westdeutsche:*

* “Where A makes a voluntary payment to B or pays (wholly or in part) for the purchase of property which is vested either in B alone or in the joint names of A and B, there is a presumption that A did not intend to make a gift to B; the money or property is held on trust for A (if he is the sole provider of the money) or in the case of a joint purchase by A and B in shares proportionate to their contributions.”

Here, the presumption that A intended to retain his ownership in the property applies.

It could be rebutted by a presumption of advancement, or by proof of intent to gift or transfer completely. There was no evidence of either. In fact, evidence pointed AWAY from it being a gift:

* If it were a loan, the money would have been paid directly to the sister
* There was no evidence of any loan arrangement existing
* No evidence of any need for a loan

The Court adopted the remedy of account of profits. There were no facts upon which the Court could justifiably grant an allowance to the sister. Therefore, the brother recovered the full proceeds of the sale of the property.

Criticism

The only issue with this approach is a conceptual one. To create a trust, we usually require certainty of intention. Settlors do not intend to create resulting trusts - they intend to create the initial trust, for the benefit of those beneficiaries. The only way this can be justified is on a **negative intention** basis - that the settlor did not intend the trustee to have beneficial ownership.

**Quistclose trusts**

**Orthodox approach**

*Quistclose*

Facts

Rolls Razor was indebted to the bank to the amount of £450,000. Rolls Razor wanted to declare a dividend to its shareholders and passed the requisite resolutions. Accordingly, Rolls Razor became a debtor of its shareholders.

In order to pay the dividend, RR took a loan from Quistclose, a related company. The amount was paid into a separate account and held in that account by Rolls Razor. Before paying the dividend, however, Rolls Razor went into voluntary administration. The bank combined Rolls Razor’s accounts, including the account holding the loan from Quistclose.

Quistclose seeks to recover the amount loaned from the bank, claiming that it was held on trust.

Held

The money was held on trust for Quistclose. Legal title to the money passed to RR, but an equitable interest remained with Quistclose.

Judgment

The Court found that there were two trusts created:

* Firstly, a trust created for the benefit of RR’s shareholders. The lender acquires an equitable right to restrain the use of property for any other purpose. This trust was created because of the fiduciary obligations imposed by such a specified purpose.
* When that failed, a resulting second trust was created for the benefit of Quistclose.

Logically in such situations, there can be an **interplay of legal and equitable interests.** When a person lends money for a particular purpose, they acquire an equitable interest to ensure its purpose is fulfilled, while the borrower has legal ownership. Once it is, the lender has a common law claim in debt.

If the purpose cannot be fulfilled, and a secondary purpose of repayment to the lender (either expressly or impliedly) exists, the lender can invoke the remedies of equity to get it back.

* This is justified because there are often **practical situations where the courts will recognise a trust** - for example, in cases where third parties pay debts on behalf of others. This is another such practical situation giving rise to a trust.

The Court found that the bank had sufficient notice that the money was held on trust because they **received notice that the money was on loan from a third party for a specified purpose, and should be returned if that purpose was not fulfilled.**

Criticism

As will be seen in the next case, Lord Millett struggles to reconcile the concept of a ‘Quistclose trust’.

In addition, **could this have been a classic failed express trust instead**, and decided on that basis?

* The money was given to RR as trustee for the benefit of its shareholders. There was a specified purpose and a specified amount of money. There is sufficient certainty of subject matter and objects.
* The creation of an express trust was impossible because RR became insolvent. Consequently, the money results back to Quistclose.

This wasn’t considered in the case, and it was possibly the way the judges thought about it - but they never said so, and never explained why it was obvious that the money should result back to Quistclose. Consequently, later cases weren’t decided this way.

*Twinsectra*

Facts

Yardley engaged Leach, a solicitor, to act for him in the purchase of a property. Twinsectra agreed to loan Yardley £1m in exchange for certain undertakings given by a solicitor that the money would only be used for the purchase of property. Leach refused to. Yardley approached Sims, a solicitor who owed money to Yardley, and convinced him to give the undertakings. It was agreed between Yardley and Sims that Sims’ guarantee would operate as though Sims was the principal debtor and he would repay the loan in exchange for Yardley forgiving Sims’ debts.

Twinsectra loaned Yardley £1m, with Sims’ undertaking. Sims transferred the money to Leach, another solicitor, who knew about the undertakings given. Leach then transferred the money to Yardley and a substantial amount of it, £357,000 was used for purposes other than the acquisition of property. Sims subsequently went bankrupt and the loan was not paid back.

Twinsectra sues Leach for assisting in a breach of trust.

Held

The Court found a Quistclose trust, but on a different conceptual basis.

Judgment

The Court found that a **Quistclose trust will arise where money is paid for a particular purpose and the recipient’s freedom to use the money is limited exclusively to that purpose.**

* Here, the money was provided on the undertaking of Sims that the money would only be used to purchase property. A Quistclose trust arose, and the use of the money for other purposes was a breach.
* This is because when money is provided in such a context, it creates **fiduciary obligations** because the lender places trust and confidence in the borrower to use the money only for that purpose. Because of these fiduciary obligations, a trust is created.

The Court then went on to **consider who the beneficial owner of the money** was:

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| **The lender:**  Beneficial ownership does not leave the lender until the money reaches its intended recipient. If the purpose is frustrated, the money will go to the lender as beneficial owner. | The lender must be the beneficiary because they have the right to enforce or revoke the primary trust if the purpose is not fulfilled. The only way they could have such a right is if they retained some beneficial interest in the money.  Lord Millett found this to be the only way to rationalise a Quistclose trust under orthodox trust law, and preferable to the ‘two-trust rationale’ in *Quistclose.*   * Enables borrowing of money while protecting the lender’s property rights. People have the right to do with their property as they wish: if they want it to be used by someone else for a particular purpose, they can put a trust in place to ensure that. It doesn’t make as much sense to create an initial trust in the first place where the settlor has the power to revoke its existence simply on the basis of its purpose being defied - no trust would be created in the first place.   It is not a purely contractual measure: there are often loans without any contractual agreement in place. |
| **The borrower:**  The borrower has both legal and beneficial ownership. | The Court of Appeal:   * The lender retains a contractual right to ensure the money is not used for any other purpose (Tipping J, adopting Rob Chambers’ opinion) * If it is used for another purpose, a restrictive covenant can be used that grants the lender a proprietary interest over the money - which appears similar to a resulting trust, but is based on contract   However, the SC found that this was wrong because contractual rights do not take priority over security interests: this reasoning does not explain Quistclose. This is also inconsistent with the conceptualisation of fiduciary duties where such specific purposes exist, and gives no remedy for lenders who have no contractual agreement.  Lord Millett decided that beneficial ownership could not vest in the borrower:   * This would render the entire Quistclose trust unnecessary: it would vest full legal and beneficial ownership in the borrower. * It would be inconsistent with *Quistclose’s* precedent * There would be hardly any practical limitation on the borrower’s rights to the money |
| **The anticipated beneficiaries:**  If the purpose has been carried out, this is not at issue. | If the money is successfully used for its intended purpose, the borrower’s fiduciary obligation to the lender is fulfilled and they only owe a debt.  If it is not, however, is what we are concerned with in cases like this. Lord Millett found that *Quistclose’s* two-trusts analysis was wrong because:   * The lender (as settlor) would be unable to enforce the primary trust. Only those anticipated beneficiaries could - but if it failed, they could not. * Normal trust law would not cause a trust to result back to the settlor simply if its purpose was frustrated * There would also be difficulties if the money is loaned in the abstract, or the future beneficiaries are uncertain. No trust could arise here for lack of certainty. (*DFC)*   *Note: Lord Millett’s use of the DFC case is incorrect here.*  DFC loaned $950k to Video Workshop to purchase stationery and office equipment. It was held by VW’s solicitors on their behalf. The stationery was supplied by GC. VW went insolvent and the creditors aimed to get its money back.  The Court found a trust where GC are beneficiaries, though it’s unclear whether this is constructive or express. Based on our knowledge, no Quistclose trust existed because QC (the beneficiary of the primary trust) was permitted to have the money. If a Quistclose trust existed, DFC as lender would have the money. This is clearly decided on some sort of express trust basis (or something similar to that), NOT Quistclose. |
| **In suspense:**  A trust is created but the beneficiaries are ‘in suspense’ until its purpose is either carried out or frustrated. | A resulting trust may arise if an express trust is created, but the full beneficial interest is not exhausted (*Crampton-Smith)*. Therefore, if there is no clear intention to pass beneficial ownership of ALL of the property, the property will result back to the settlor.  Therefore, a resulting trust would arise back to the lender (which, if the purpose is unfulfilled, already the preferred approach, and if it’s not, defeats the purpose of a loan).  Property does not like to be in suspense, it needs an owner because the law favours certainty over property. |

The Court found that beneficial ownership does not leave the lender until the money reaches its intended recipient - if the purpose is frustrated, the money will go to the lender, as beneficial owner.

This is a different approach to the two-trust rationale in *Quistclose.* Lord Millett found that this conceptualisation was the only way to rationalise Quistclose trusts under orthodox trust law.

* It’s a practical, commercial arrangement that enables the borrower to use the lender’s money while protecting the lender’s property rights as far as possible.
* It is not a purely contractual measure because there are often loans without a contractual agreement in place.

Tipping J adopted Rob Chambers’ theory = “a resulting trust is one where the transfer of beneficial ownership has not been completed.” This conceptualisation of Quistclose trusts is consistent with this.

However, Chambers actually found that situations such as this are protected by contract - ownership is given to the intermediary, but they lender reserves the right to ‘pull’ this back.

This is obviously only of limited application: it wouldn’t be able to apply if no contract exists, or if the borrower went insolvent.

*Occam’s razor - can we just take the simplest approach with the least assumptions?*

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| Quistclose trusts under the PPSA:  Because Quistclose trusts often arise in cases of insolvency, they have sometimes been viewed as a security interest. However, it’s not meant to secure repayment of a debt - it’s actually meant to ensure that money is used for a particular purpose. If the money IS used for that purpose, it becomes a debt, subject to personal property security legislation.  Although Lord Millett does draw a parallel between Quistclose trusts and retention of title clauses. It’s possible that this could be an equitable retention of title. If this were accurate, it would be subject to the PPSA. Will turn on whether Quistclose trusts are interpreted as security interests, or as something akin to an express trust. |

*AIB v Redler*

Note: usually, duties of stewardship and loyalty result in account; and duties of management result in equitable compensation.

Facts

Solicitors were acting on behalf of Barclays Bank. BB’s clients applied for a $3.3m loan. The solicitors acted for both the clients and BB. The solicitors were under instruction NOT to pay out the loan the clients had applied for unless they were sure the clients were not subject to any other security. They made a mistake, and didn’t realise that the client’s old loan was actually still current, and had been re-negotiated. Again, because of this, they overpaid the clients by just over $300,000 (and underpaid BB that same $300,000).

The clients defaulted, and when BB sold the property, the market had fallen and they only made back $1.2m.

It was settled that the solicitors had acted in breach of trust. The real question is whether they needed to repay the full amount paid out in breach ($3.3m) or repay the money lost as a result of their breach ($300,000).

Held

Judgment

The Court found the case to be very similar to *Target Holdings*, and first discussed whether that case was correctly decided.

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| *Target Holdings*  TH gave solicitors $1.5 to loan to Crowngate for purchase of property, over which TH would have a mortgage. The solicitors were under instruction not to release the money until the mortgage was executed. Crowngate had a fraudulent plan to profit from the property, which it was purchasing for only $775,000. The solicitors actually released the money before the mortgage was complete. The sale went through (the mortgage was put in place), but the investment failed. Crowngate defaulted, and TH only recovered $500,000. They sued the solicitors and claimed they had a duty to account. The solicitors argued the loss was not caused by their breach.  *Lord Browne-Wilkinson*   * In common law, there would be no loss. But for the defendants’ actions, nothing different would have happened. * However, we do not necessarily use common law rules in equity. The first step is to **look at the nature of the equitable rules that apply, in light of their purpose, to determine what it is appropriate to consider.** We take a common sense approach about the nature of the obligation, and find a remedy relating to that.   + Trusts are created for a purpose. Once that purpose has been fulfilled, beneficiaries can seek compensation, but not reconstitution.   + Equitable compensation is designed to make good the loss that was suffered. Here, the loss that was suffered was not attributable to the solicitors. * It is true that if a trustee steals gold, they are obliged to return the gold, even if the monetary value of the gold has increased. * However, this case is different from that. This is a situation where the solicitors did what they were meant to do in substance, but breached their duties in form/procedure. This is a breach of negligence, diligence, or performance.   The solicitors were not liable to account for the money they had paid out the account. The loss was caused by Crowngate’s fraud, not the solicitors’ breach. |
| *Criticism following Target Holdings*   * It focuses on **hypothetical loss**, not actual loss. Hypothetically, TH would have still lost the money even if the breach didn’t happen. But we can’t know that, because the breach DID happen. It’s hypothetical. If we look at actual loss, the solicitors breached the trust and TH lost $1m. * Lord Browne-Wilkinson confused restitutive compensation (account) with reparative compensation. Restitutive compensation arises when a trust asset is dissipated without authority. If this is too harsh, the courts should relieve trustee liability rather than change the law. |

It is in the context of *Target Holdings* that the UK Supreme Court made their decision.

It is accepted that at common law in negligence, the solicitors will at least be liable for the $300,000 loss caused to AIB. However, if AIB wishes to have the full amount loaned returned, there needs to be a successful case that account is the appropriate remedy for their unauthorised use of trust property.

Importance of account vs compensation

The distinction between the two is usually not as important as in this context. If trustee who breached goes insolvent, you want to claim that your interest is proprietary. This gives you the ability to **trace** the money you’ve lost, because you can’t get it from that trustee. It also means you can follow it if it moves into a different form (ie: cash assets into real property).

If your interest is only personal (compensation), the trustee must pay you that money. But if they’re insolvent, they can’t - and you’ll just lose it. On the other hand, there are times when this is preferable. If the value of the converted property is less than it used to be (due to devaluation or currency exchange), you might prefer a personal right to repay the value at the time it was taken.

The real issue is, when there is a duty to restore the trust fund, should it be restored completely? If yes, then *Target Holdings* was wrongly decided.

Distinction between management duties and custodial duties

In *Guardian Trust,* GT was supervising another company on behalf of BNZ. They failed to tell the banks about breaches and were sued in negligence. GT argued they were acting as managers of the investment, not custodians. As managers, common law causation should apply.

* The justification of such an argument is that due administration of trust funds can be enforced by duties of due care as a professional. Duties of loyalty, however, are core to the fiduciary relationship, and should be enforced by account.

However, the UKSC decided this **distinction is of no assistance in this case.** The trustees paid out funds - this sounds custodial by nature, but because they should only do it at the instruction of their principal, it could also be conceptualised as management.

The Court **adopted the approach in Target Holdings: each trust should be examined in practice to determine the nature of its obligations. The appropriate remedy follows from this.**

* Look to the reality of the obligation, its breach, and the loss.
* Here, have you actually breached the trust, or fulfilled what you were supposed to do?

Here, the solicitors fulfilled their duties substantively, and only breached the trust in form. $300,000 loss flowed from that, and they are required to compensate AIB for that loss. If they hadn’t breached the trust, that $300,000 would not have been lost, but the remaining money would have been because the property market would have crashed regardless.

While it is not appropriate to always use common law rules, sometimes an equitable analysis may be guided by them.

* Because of the nature of fiduciary obligations, tort or contract measures are of no assistance. Foreseeability is not a requirement, because a breach is wrong despite this.
* Because a breach of trust is wrong, the aim is to **put the principal in the position they would have been in if the obligations had been duly performed.** It aims to provide the **monetary equivalent of performance.**
* If the nature of the obligation is strict, the full amount must be repaid.
* If nature of the obligation can be flexible according to circumstances, the amount compensated will depend on the effect of T’s act upon the fund.

*Critique*:

Charles Rickett & Jessica Palmer

This is crossover between the two doctrines. Should you borrow from one, or limit yourself simply because of the form the claim comes in, sticking with the traditional divide?

* Concurrence = take the rule that suits the most: equity or common law
* Concordance = approach Lord Reed took. Look at the nature of the obligation, and the rules that should be imposed.

If equity and common law are separate (as Lord Reed acknowledges) then we should stick with concurrence, not concordance.

Sarah Worthington

The outcome is correct, but the way the Court arrives there is wrong.

The relevant duties and remedies:

* There is a duty to perform the trust (primary)

The remedy is specific performance.

* There is a duty to compensate for losses or faults arising from non-performance (secondary)  
  The remedy is an order of repair or damages.
* There is a fiduciary obligation not to compete, and not to put your interests above your principal’s (fiduciary)  
  The remedy is proprietary disgorgement.

The Court wrongly considered this under the duty to compensate for losses or faults arising from non-performance. However, the same decision (solicitors winning) can be reached under an alternative head, analysing breach of the primary duty.

Primary duty

The primary duty of the solicitors is not to pay an agreed sum or to hold a specific fund. It’s to go through a series of steps to meet a particular end result. In addition, the object of trustee obligations is to ensure custody and management of the trust assets, to ensure the trust ‘pot’ is kept in the state it ought to be in, or returned to the state it should be in if there’s any ‘slippage’.

* If specific performance were ordered, they would need to take all the steps required by instruction - not merely one or two. However, ordering damages for breach on the basis of *one* of those steps is doing exactly that; preventing the solicitors from completing their obligation.
* The court should assess what state the trust assets ought to be in at that date, considering the trustees’ ongoing duties, up until the date of assessment. This includes consideration of all elements (including the market).

**Succession**

People make wills to ensure that their property is dealt with as intended after they pass away. The starting point of testamentary wishes is always freedom of K and autonomy over your property. However, there are a number of limitations on the ability to enforce wills.

* Testamentary Promises Act ensures that people who make contributions with the expectation of property will receive it
* Relationship Property Act ensures that spouses and de facto partners are not cut out of wills
* Family Protection Act ensures that children are not forgotten or left out
* The executor of the estate also has certain freedoms.

Sometimes it can be easier to ‘get around’ all of these limitations and ensure your intention is carried out by creating a trust with reliable trustees to ensure it is effected. Many people create trusts to avoid succession laws.

In contrast, the civil law system has a system of forced heirships. It requires certain proportions of the estate to go to certain people. Foreigners often used NZ trusts to escape forced heirship. Arguably, these limitations indicate a move towards this approach (though to a far lesser extent).

Jurisdiction over succession law lies concurrently with the High Court and Family Court.

If the deceased has over $15,000 worth of property, executors must apply to the High Court for **probate**.

**Validity of wills**

**Making a will - section 11 Wills Act**

* Name
* Revocation of previous wills
* Appointment of executors
* Bequeathing of property
  + Including any instructions for residual property
* Signature
* In writing
* Permanence
* Witnessed and signed by two non-benefitting people

Interesting is **Section 14 - High Court may declare a will valid.** This is used as a last resort, and is only really exercise where there appears to be a will, it just hasn’t fulfilled formality requirements.

* Potential issue of access to justice? HC only located in main centres.

This has been used in cases where the deceased was unable to complete their updated will:

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| --- | --- |
| Brundell | Middle aged woman with a valid will. It’s clear she’s drafting a new will and negotiating with her solicitor. They discussed it over the phone, and a draft was prepared and sent to her. She passed away before it was signed and witnessed.  S 14 allowed the Court to decide this was a valid will because:   * Substantial evidence expressing Deceased’s intentions * Death intervened. But for this, the will would have been executed   However, the old law would have been stuck on formalities. |
| McNeil | Suicide note left by deceased: leaves possessions to whoever wants them. She only asks that people listen to her Dixie Chicks CD in the stereo.  The family did not contest the existence of the will. The Court was satisfied that this laid out testamentary intent.   * The difficulty with this is that there are often uncontested cases. In cases such as this, the court may be more flexible, but this may not be an accurate reflection of the law. * Shows the breadth of s 14 discretion. |

If a person makes a will, it will be voided upon marriage or civil union unless there’s evidence that it was made in contemplation of marriage, shown by express words or implication of circumstances (**s 18**).

**Burial decisions**

Another limitation is that the default position in NZ is that **the executor decides what happens with the deceased’s body - it is not determined by the deceased’s testamentary wishes**. While the deceased can express burial wishes, the decision is ultimately the executor’s.

This was discussed in *Takamore v Clarke:*

* After Takamore, of the Tuhoi hapu, passed away unexpectedly, his family travelled to Christchurch to discuss burying his body in a pa according to tikanga. When no agreement was reached, the family members took the body and buried it in the Bay of Plenty. His long term partner, Ms Clarke, was executor of his estate and requested the body back.
* The Supreme Court applied the executor rule, despite considerations of tikanga.
* Elias CJ applied a ‘significance in the deceased’s life’ test.

The Law Commission proposed repealing the executor rule in favour of a focus on the individual decision of the deceased, starting from a presumption of autonomy. If they want tikanga, the law should facilitate it. However, no change was made (apart from allowing Maori access rights to the coronial body).

There has been speculation around whether this issue could be dealt with on a case-by-case basis by the Maori Land Court.

* The old government’s view was that MLC is not a tikanga court, but a land court. They do not simply have tikanga expertise to be used in all scenarios.
* MOJ’s concern is that if procedures for succession disputes are created, people will use them, which can increase administration costs and backlogging of the courts, OR that there wouldn’t be enough disputes to justify the creation of such procedures.

**Using the legislation to determine distribution of property**

|  |  |
| --- | --- |
| **Estates Act**  If there is no will, the estate is in testacy and the Estates Act applies. |  |
| **Administration Act** |  |
| **Testamentary Promises Act**  Deals with situations where Deceased made promises in exchange for services but never followed through. | Consideration is not required. |
| **Family Protection Act**  Creates a moral duty to support children. Their need for support (being a dependent) does not preclude a claim from succeeding. Shows some shift from financial support to emotional support. | Based on the idea that family members intend to care for each other/moral familial duties.  If you would like your estate to be divided according to need, you may be better creating a discretionary family trust rather than a will, which will usually be treated by succession law as a breach of your familial duty. |
| **Relationship Property Act** |  |

**Welch** is an example of **intestacy**. The spouse and children are set to inherit under the Administration Act. Stepchildren are not included unless they are dependants. However, the step-son had carried out considerable work helping his deceased stepfather, and provided evidence of a promise that he would be included in the will.

* An example of the pragmatic, discretionary approach usually taken to intestacy.

**Aucutt** is an example of the **Family Protection Act.** Mrs Henderson’s will declared an intention to make a greater provision for her daughter Christine than her daughter Susan in order to recognise their differing financial positions (Christine was far worse off). The total estate amounted to $920,000, and Susan received assets worth $50,000 (approximately 5%), though the estate was worth far more than Mrs Henderson realised.

It was agreed that both daughters rendered services in different ways, yet Christine was closer because she supported her mother’s wish to live in her home together. Susan’s claim is that she deserved a greater provision to recognise her position in the family and life of her mother.

The High Court granted an order for greater provision due to breach of moral duty in the failure to recognise Susan’s position and contribution to the overall life of her mother and awarded 25% of the estate. This was appealed by Christine.

* The Court found that 5% was not adequate provision for support and maintenance because it did not consider moral support - financial stability is not determinative.
* If the mother had been aware of the value of her estate, a different allocation would have occurred
* The Court’s analysis under s 4 FPA should be on whether adequate provision for maintenance and support has been made, not whether the difference between beneficiaries is appropriate or just

This shows a **clear moral duty** on parents to provide for their children, even when they do not support them and their children are not dependents.

**Testamentary capacity and undue influence**

*Green*

Facts

Had a valid will that he wished to change. A short time before his death, Mr Green changed his will so that his daughter was excluded from the management of the family business and trust, despite being the only child involved throughout his life.

The reason for the change was that, as he neared the end of his life, he desired the rest of his family to become involved and help out with the business. When he mentioned this to his daughter, she refused to permit it. His son advised him, and he wrote her out of his will out of frustration.

The daughter argued that his will was invalid due to undue influence.

Held

This is a case of undue influence - not because of any spiteful intention, but because the testator’s will was overborne, guided or influenced.

Judgment

There is no need to establish an evil, spiteful or wrongful intention to find undue influence. The real question is **whether the testator is exercising their own judgement, or whether it has been overborne, established on the balance of probabilities in the circumstances as a whole.**

An indicator of this may be the presence or absence of independent legal advice

* Here, Green had advice from an interested and unknown lawyer and had documented full reasons for his change in will

*Loosely*

Facts

Aunt lives abroad but maintains a close relationship with her family in NZ. Her existing, valid will includes a number of bequests, and a provision that the residue be divided equally among her nieces and nephews. On her deathbed, she changed her will to exclude one set of nieces and nephews.

There was an issue around her testamentary capacity to revoke her previous will and enact a new one.

Held

Not enough evidence to find testamentary capacity.

Judgment

She was in the last stages of life, on morphine, and there is no evidence to explain why she had made the change. There was evidence of ‘nonsensical musings’ in a notebook.

However, there was also evidence that she went through stages in her life where she favoured different groups in the family over others.

The Court summarised the test for capacity from *Banks v Goodfellow*

1. Intellectual and moral faculties common to human nature
   1. Focus on soundness to the mind, not bodily capability
   2. Is not a sound and disposing mind and memory in the highest degree - too high a threshold
2. Understands the nature of the act and effects
3. Understands the claims people may have against it
4. Is free of any disorder of the mind
5. Evidence of previous wills may make a stronger case than someone writing a first will
6. **Overall, just be able to clearly understand and make a sound assessment of those things to enter into a rational, fair and just testament**

The Court finds that, without any justification for WHY, at the end of her life, after treating her family members equally she decided to favour one over the other, they cannot determine capacity. Consequently, the first will is not revoked.

**To what extent do we reflect testator’s will in NZ?**