Final Equity Notes

Trustee's Powers and Duties

Trustee's Powers

- The source of the trustee's powers:
  - The trust deed
  - Trustee Act 1956 s 2(4)
  - **S 2 Interpretation and application**
    - (4) The powers conferred by this act on a trustee are in addition to the powers given by any other Act and by the instrument (if any) creating the trust, BUT the powers conferred on the trustee by this Act apply if and so far as there is no contrary intention expressed in the instrument (if any) creating the trust.
- The Trustee Act confers specific powers allowing the trustee to do certain things:
  - Powers of management (sell, lease etc)
  - Powers of investment
  - Powers of disposition (advancing or transferring property).
  - Gives further powers:
    - The power to appoint agents (s29)
    - Delegate if absent or incapacitated (s31)
    - Carry on testator's business (s32).
- All these powers can be excluded by the trust deed; however, the powers cannot be reduced too far.
- There is an 'irreducible core' beyond which the duties cannot be reduced.

Duties of the Trustee

- Trust duties are the obligations borne by trustees either under the trust instrument (if there is one) or under the general law of trusts.
- Trust law **reverses the power relationship** by putting the beneficiary in a position of strength over the trustee, by giving the beneficiary a means of enforcing the trustee's obligations to act in the beneficiary's best interests.

Sources of the Trustees' Duties

- The trust deed.
  - The paramount question is what does the trust deed say about the situation.
  - The trust deed acts as the key statement as to the intentions of the parties.
- Trustee Act 1956
- Equity case law/precedent.
  - Obligations of a trustee as a fiduciary – the key duties that exist
    - Must act honestly, in good faith.
    - Exclusively for the benefit of the beneficiaries.

Exclusion of Duties

- The trust deed is paramount, but a trust cannot exist which a court of equity will not enforce.

List of Trustee's Duties

1. Acquaint oneself with terms of the trust deed.
2. Comply with the Trust deed – 'perform the trust' – including investments; redistribute to correct beneficiaries.
3. Take possession of property and safeguard it; keep identifiable.
4. Act impartially as between beneficiaries.
5. Keep accounts provide information as required.
6. Act with a due diligence/prudence, including investing trust fund
    a. If you are in a profession that manages trust funds, then you are held to the standard of your profession (not just ordinary person standard).
7. Fiduciary duties:
    a. Loyalty – act in beneficiaries' best interest
    b. Not to profit or self-deal
    c. Not to act with improper motives
    d. Not to charge for the trustee service – act gratuitously
8. Be active, and act personally (not to delegate) and jointly (act with other trustees unanimously).

Failure to Conform to the Trustee's Duties is a Breach of Trust

- Failing to comply with the above duties may lead the court to set aside an exercise of the trustee's powers. Personal claims exist against the trustees.
    1. **Personal liability of trustee(s) to restore trust property, compensate trust fund, and remedy any consequential loses.**
        - If you've breached the trust in any way which has diminished the trust property, as a trustee you are personally liable to get the property back.
        - If you can't get it back, you must restore the trust fund with cash.
        - If there is any consequential loss, you will have to compensate the beneficiaries.
    2. **Personal claims against third parties**: Those who dishonestly assist in the breach of trust, or receive property knowing of the breach of trust.
        - There is no limitation on only suing the trustees, you can sue anyone who has assisted the breach of trust, or anyone who has at some time received that property knowing about the breach of trust.
        - Sue for the value.
    3. **Proprietary claims against third parties** who currently control the trust property or its substitute (tracing).
        - If you see the trust property in another's hand, then you can say the property they hold is the trust property, which gives you as the beneficiary a proprietary claim in it regardless of who is in control.
            - Beneficiary can sue because it's trust property, and they have a proprietary claim on the assets of the trust.
            - The person who has the property may have defences available to them (eg: Bona fide purchaser, buying without notice etc).
        - Even if you can't see the exact thing that was trust property, you can say my thing was paid away on breach of trust, and therefore claim the substitute property.

Trustee's Duties

Impartiality: Trustee must practice even-handedness, or a lack of bias in decisions that have an effect on different beneficiaries' entitlements.

- *Re Mulligan*
  - Widow was an income beneficiary, nieces and nephews were the residual (capital) beneficiary.
  - The trustees went too far in favouring one beneficiary over others.
- In the case of discretionary beneficiaries, the trustees have an obligation to consider them. They don't have to 'treat equally', but they must act in good faith. The must not consider irrelevant information, and must consider relevant information.

Information

- Court's discretion as to what information must be disclosed to which beneficiaries/objects.
- Balance between giving beneficiaries information they need to know, versus keeping confidential and commercial information safe from a possibly large class.

Due Diligence

- "The duty of a trustee is not to take such care as a prudent man would take if he had only himself to consider; the duty rather is to take such care as an ordinary prudent man would take if he were minded to make an investment for the benefit of other people for whom he felt morally bound to provide." – *Re Whiteley* [1886]
- Trustee Act 1956, ss 13B and 13C.

Investment

- Section 13E outlines certain matter which the trustee must take into account when deciding to invest.

Duty not to Charge

- Common law rule that Trustees are to act gratuitously.
- Reflected in the Trustee Act 1956 s 38(2).

Ways Trustee can avoid Liability for a Breach of Trust

Exclusion/Exemption Clauses

- A clause which purports to limit or exempt the liability of a trustee.
- Found in Trustee Act s 13D.
- Creates a tension between the understandable desire to get professionals involved, enticing them by excluding certain liabilities, while still retaining a trust.
- The clauses don't infringe on the irreducible core. The basic duty to give effect to the trust deed still fully exists. Exemptions only apply in the absence of dishonesty.

Spencer Rule

- *Spencer* had an exclusion clause which said 'no trustee shall be liable for any loss not attributable to his or her own dishonesty'.

- Dishonesty has a different meaning in case law. A person could act dishonestly for the purposes of the exemption clause, even though he genuinely believed his actions were morally justified (*Wong v Burt*).
- Test for honesty: **In light of what the trustee knew, did they act in a way that the honest person would have in the circumstances?**
    - Subjective aspect.
    - Look at what the trustee knew about the relevant breach, and what they knew about what they were doing.
- Applying this test to *Spencer*, the judge was critical of the way the trustees had conducted themselves.
    - The did not try to recollect the debt.
    - They did not collect rent from SGL.
    - They charged excessive management fees.
- In light of all these things, the court held that the trustees had not acted as an honest person would have in the circumstances.

Court's Relieve Liability: S 73 Trusts Act 1956

"If it appears to the court that a trustee, whether appointed by the court or otherwise, is or may be personally liable for any breach of trusts,… but has acted honestly and reasonably, and ought fairly to be excused for the breach of trust and for omitting to obtain the directions of the court in the matter in which he committed the breach, then the court may relieve him either wholly or partly from personal liability for the same'.

- Even if there is no exclusion clause, the defendant could still claim they acted reasonably and honestly, and therefore should not be liable.
- But if they had relied on an exclusion clause, their dishonest conduct had been established, and they lost, then they cannot rely on s 73.

Spencer v Spencer [2013] NZCA

Facts

- The Spencer Family Trust is established. All three children were to be specific beneficiaries of the trust, plus a specific payment of $200/week for Robert's maintenance (he had a disability).
- Barry Spencer (father) was one of three trustees, and also a discretionary beneficiary of the trust.
- Principal asset of the trust was a commercial building.
    - Building was managed by SGL, a company of which Barry Spencer was manager, director, and shareholder.
        - The property produced very little income.
- Weekly payments were to go first to Robert ($200), then to go to another child's education. General clause for income to go to children's needs, any excess could also be passed off to the other beneficiaries.
- Weekly payments to Robert stopped in 1995, and did not resume. It is on his behalf that this case was brought.
    - Alleging irregularities in the administration of the trust.
    - Remedy sought included an inquiry into the trust's income, and orders for restoration of losses resulting from breaches of trust.

Issue

1. Whether the trustees were in breach of trust (by failing to pay Robert) and
2. Whether (if found liable) they were protected by the trust deed (exemption clause) or s 73.

Held

Were they in breach of trust

- Trust failed to pay Robert $200/week, claiming there was no net income available to pay. But the issue lay in the reasoning behind why there was no income.
    - SGL were charging huge management fees to the trust (exorbitant).
    - There was a huge debt owed by SGL to the trust which was being offset by the management fees.
    - SGL didn't pay any rent for the space they occupied in the building.
- If the debt had been recovered, and adjustments made, they would have been able to pay Robert. They were in breach of trust.

Were they entitled to exemption?

- Under the Trust Deed?
    - Clause 10: 'No trustee shall be liable for any loss not attributable to his or her own dishonesty'.
    - Judge was critical of the way trustees had conducted themselves; trustees had not acted as honest persons would in the circumstances, even if they thought their actions were morally justified.
- Under s 73?
    - Requires a trustee to show both that they acted honestly and reasonably, and they he or she ought to reasonably be excused.
    - Previous conclusion means there were no grounds upon which this section could exclude the trustees.

Clayton v Clayton [2013] HC

Facts

- The Vaughn Road Property trust settled by Mr Clayton, he was the sole trustee. The children are the final beneficiaries.
- In the Family Court, Mrs Clayton submitted that the Trust is a sham by virtue of Mr Clayton's powers as trustee, including the power to appoint and remove trustees and beneficiaries. This was said to amount to a bundle of rights which could be classified as property in the hands of Mr Clayton.

Procedural History: Family Court

- There are two aspects to the trust deed which called into question the existence of a trust.
- The first relates to the requirement that the trustees are accountable to the beneficiaries:
    - There is an irreducible core of obligations.
    - Two provisions of the trust deed negated against the ability to call the trustee to account (clause 11: Trustee's discretions unfettered, and clause 19: Trustee's conflict of interest).
        - These provisions in conjunction negate the ability under this deed for the beneficiaries to call the trustee to account in the exercise of his discretion. The beneficiaries therefore have no rights under this deed enforceable against the trustees.

- The second is the 'power of revocation' under clause 23:
  - The principle family member is Mark Clayton, and the power to revoke the trust lies solely with him.
  - The power to revoke a trust is distinguished from the power to appoint/remove trustees. It is a dispositive power that can be exercised selfishly without regard to the interest of others.
- This trust is a convenient structure for commercial purposes, but it does not meet the basic elements of the trust.
- Held to be illusory, and invalid.

Held

- The provisions relied on by the Judge do not erode the core obligations of the trust.
  - Clause 11 allows the trustee to act without considering the interests of all beneficiaries. It does not excuse him from acting honestly and in good faith, it merely relieves him from the obligation to act impartially towards beneficiaries.
  - Clause 19 is to similar effect. It allows the trustee to act despite a conflict of interest. He still must act honestly and in good faith.
- Second matter: the revocation clause 23.
  - Judge relies on *TMSF v Merril Lynch*.
  - The power in the present case is much more limited. It does not confer on the trustee any power to deal with trust property as he pleases.
- However, there are many other provisions of the trust deed which lead irresistibly to the conclusion that Mr Clayton indeed retained powers tantamount to ownership of trust property.
- **The Vaughan Road Property trust is illusory.**
  - It is what Mr Clayton had the legal power to do which is important, and he has the power to do basically whatever he wants with the property.
  - The trust deed provides an appearance of separation, but the reality is that Clayton is able to deal with the property exactly as he would have if the trust had never been created.

Introduction to TABOLs

- Trusts arising from operation of law generally arise because of the court's interpretation of what the parties have done, regardless of whether there was actually any intention to create a trust.

Westdeutsche (Bank) v Islington London Borough Council (HoL)

Facts

- W is a German bank doing a deal with an English Council (ILBC) called an interest-rate swap. W bank pays the council £2.5m, and the council made 'interest' payments, totalling £1.4m.
- Court held that interest rate swap transactions by local authorities were ultra vires and the contracts void.
    - Following this decision, the council made no more repayments, because they no longer have any contractual burden to pay the money back.
- W can't say the money belongs to them, because legal title to the money is with the council.
    - W wants their debt (minus the repayments, about £1.145m) back.
    - Although it's no longer their property, there is a common law claim that will get them their money back.

Issue: Compound Interest

- ILBC had the benefit of the money for a certain period of time, therefore the lawyers are allowing W to claim simple interest.
- W don't want simple; they want compound interest.
- However, case and statute law don't allow compound interest on these kinds of actions in a common law claim. **But you could get compound interest under an equitable claim**.
- Therefore W argues the money as a trust. Although W gave legal title of the money to ILBC, the contract was void, so the money must be returned. During the time ILBC was holding on to the money, they were acting as a trustee for W, so now W has an equitable claim on the money, and are therefore entitled to compound interest.

Resulting/Constructive Trust

- Counsel for Westdeustche specifically disavowed any claim on a constructive trust. This is correct, because the local authority had no relevant knowledge sufficient to raise a claim for a constructive trust at any point before the money became untraceable.
- The only possible trust which could be established would be a **resulting trust** arising from the circumstances.
- Resulting trust arises in 2 sets of circumstances:
    - A: Where A pays for property that is vested and legal title is put in the name of B, there is a presumption that A did not intend to make a gift to B: **the money and title are held on trust for A**.
    - B: Where A transfers property to B on express trust, but the trust declared does not extend to the full beneficial interest.
- Both types of resulting trusts are traditionally regarding as giving effect to the common intention of the parties. A resulting trust is not imposed by law against the intentions of the trustee, but gives effect to his presumed intentions.

- Applying these principles, the bank's claim must fail:

  - (B) There was no transfer of money on an express trust.
  - (A) Any presumption of a resulting trust is rebutted since it is demonstrated that the bank paid and the council received upfront payment with the intention that the moneys so paid should become the absolute property of the council.
- The parties **were** under a misapprehension that the payment was made under a valid contract, but that does not alter the actual intentions of the parties at the date the payment was made.

- Lord Browne-Wilkinson states it is basically impossible for the trust to have attached to the property in this case, because at the time that it was known that the contract was void, the money had been paid out for a purpose which could not be traced.
  - Therefore, W wasn't in possession of the subject matter of the trust at the time when they're claiming the conscience of the trustee was bound.
  - W is claiming that despite their being **no intention** to create a trust, the court is saying someone is bound.
  - Lord BW is saying they can only be bound if they know about the thing which is binding their conscience.

<u>Resulting Trusts</u>

- (A) Presumed common intentions of the parties.
- (B) Trust declared do not exhaust the whole beneficial interest.

<u>Constructive Trust</u>

- Relief available when the conscience of the legal owner of the property is burdened.

In circumstances of A or B, there is a presumption of a resulting trust. If there is evidence that a trust was not intended, this presumption can be rebutted: 'No, it was just a gift from A to B'.

<u>Lord BW's Fundamental Ideas about Trusts</u>

1. Equity operates on the conscience of the owner of the legal interest.
2. A trustee cannot be a legal title holder unless the conscience of the property holder is affected.
3. In order to establish a trust, there must be identifiable trust property.
4. Once a trust is established, the beneficiary has a proprietary interest enforceable in equity against any subsequent holder of the property, other than a purchaser for value of the legal interest without notice.

<u>Lord BW's Practical/Policy Considerations for not extending RT</u>

- Despite the fact that no one expressly created a trust, in these circumstances the court should say that, because of what the party did, no trust exists.
- There could be serious negative consequences if the courts apply resulting trusts arbitrarily, although in the present case, the only issue is the personal liability of the local authority as a trustee, it is not possible to hold the local authority liable without imposing a trust which, in other cases, will create property rights effecting third parties.
  - The creation of an equitable property interest under the trust can have unfortunate consequences if the original recipient of the moneys becomes insolvent; the money and trust property is not available for the creditors to claim.

    - The proprietary interest under the unknown trust will be enforceable against any recipient of the property other than the purchaser for value of a legal interest without notice. This would cause uncertainty.

- The court is high reluctant to extend the existing categories of TABOLs because of the dangers these equitable rights impose on third parties.

Commentary

- *Westdeutsche* is a good introduction to the way in which trusts can arise in different ways from express trusts. The HoLs held that compound interest was available in equity to effect a stripping of profits from a defendant who is a trustee or otherwise in breach of fiduciary duties.
- According to Lord B-W, the bank had transferred the money outright to the Council.
- The trustee must have relevant knowledge of the binding of their conscience which is occurring, and they must be aware that a resulting trust will arise.

Resulting Trusts

Definition

- A resulting trust is not imposed by law against the intentions of the trustee in the same way as a constructive trust, instead it gives effect to the presumed intentions of the trustee.
- It connects to the basic notion of 'trust' in that the common law owner would not be entitled to assert beneficial ownership, but rather would be bound to hold that property on trust for the previous owner.
- A resulting trust can arise in one of two ways (*Westdeutsche*):

Type A/Presumed resulting trust

- When someone transfers property or pays the purchase price of property that is legally vested in another, there is a presumption that the person who paid the purchase price intended to remain the beneficial owner.
- Where the claimant has contributed to the purchase price of property, the claimant acquires an equitable interest in the property on resulting trust in proportion to the size of their contribution.

Type B/Automatic Resulting Trust

- A resulting trust will arise where a settlor has sought to transfer property or to declare a trust but has failed to make clear who is intended to take those rights, with the result that any rights left unallocated pass back to the settlor on resulting trust.
    - The RT is an automatic consequence of A's failure to dispose of what is vested in him, the resulting trust does not establish the trust but merely carries back to A the beneficial interest that has not been disposed of.
- A failure to dispose of all the beneficial interest – the person who tried to set up the trust gets the property back.

Type A

- Where A pays for property that is vested and legal title is put in the name of B, there is a presumption that A did not intend to make a gift: the money or the property is held on trust for A.
- The claimant acquires an equitable interest in the property on resulting trust in proportion to the size of their contribution to the property.
  - Historical foundations: The 'norm' of feudal land holding.
    - When it was beneficial not to hold land for yourself, but have someone else hold it on trust for you. Because it was so beneficial, everyone did it.
    - Presumed that you were simply avoiding tax, and that in equity, the person who actually owned it was the person who made the purchase price/made the transfer.

Test

1. Payment of the purchase price (or part thereof) by A in property vested in B.
2. Transfer of property by A to B.
3. Created a presumption that A did not intend to beneficially entitle B to the property; rebutted by the introduction of evidence that A did so intend.

- Without any evidence of intention to create a trust, we will presume there is an intention to create a trust over this property. This presumption can be displaced if some other intention can be proven.

Crampton-Smith v Crampton-Smith [2011]

Facts

- Brother transferred the purchase price of a property to his sister.
- She built upon the land, subdivided it, sold it. Legal property was vested in her.
- Brother claimed he was the beneficial owner.

Held

- Here, the presumption applied, that the brother was the beneficial owner.
- In the absence of any evidence, the presumption will apply.
- Here the court thought it would be ridiculous to claim this.
- The presumption is fairly easy to rebut.

Presumption of Advancement

- Exists in a parent – child or spousal relationship.
- Presumes that any transfer of property is a gift.
- Exception to the resulting trust rule.

However

- The Property (Relationships) Act 1976 s 4:
  - The presumption of advancement was used before we had relationship schemes.
  - When there is a contribution from one of the marital couples to the property, and it is vested in only one of them, the resulting trust could activate, and maintain the partner who contribute some of the purchase price to maintain an equitable interest.
  - The PRA abrogated this presumption.

        - No longer applies between married or civil union couples.
    - Still applies to parent – child.

Tinsley v Milligan

Facts

- Tinsley had legal title to a house and bank accounts belonging to her and her lover Milligan.
- Milligan had contributed to the purchase price of the house.
- Seems obvious that equity will aid her through a resulting trust.
    - Purchase price of the house paid by Milligan, so she has an equitable right in the house to the extent of the price paid.
    - Tinsley is a trustee, and has to hold the property for the benefit of Milligan to the degree that Milligan contributed.
- BUT the reason the house was in Tinsley's name is so Milligan can defraud social security. **Problem of illegality.**
    - Milligan was defrauding the authorities and receiving a benefit by claiming that she was paying rent.

Issue: Can Mulligan really claim in equity when her name wasn't on the title in order to aid in an illegal purpose?

Held

Lord Goff (Minority)

- No court will aid a person who funds their claim upon an immoral or illegal act.
    - One must come to equity with clean hands.
    - The purpose of this transaction was benefit fraud.
- This is a principle of policy, not of justice.
    - A principle within the law of equity is that a claim based on immoral or illegal grounds will not be allowed.
- Exception if the claimant has 'repented' before the illegal purpose was carried out.

Lord Browne-Wilkinson (majority) – Allowed the claim

- Doesn't disagree with Lord Goff that there exists this doctrine of legal purpose, but because Milligan didn't base her claim off the illegal act, Lord BW allows her to make it.
- At common law, property can pass on an illegal contract, and the claimant can rely on those property rights so long as she does not need to rely on the illegal contract except for evidencing their property rights (ie Rather than enforcing the K).
    - Milligan based her claim on the fact that she had contributed half the money to buy the property. She did not have to plead illegal action to make her claim.
    - Once she has contributed some of the purchase price, the presumption of the resulting trust kicks in.
- The reasoning behind her actions in contributing half the purchase price are irrelevant, it doesn't matter that she only did it to commit a fraudulent act. All she needs to show is that she contributed half the purchase price, and did so legally.
- "On the presumption (of a resulting trust) (and on the contrary presumption of advancement) hinges the answer to the crucial questions 'does a plaintiff claiming under a resulting trust have to rely on the underlying illegality?' Where the presumption of a resulting trust applies, the plaintiff does not have to rely on the illegality. If he proves the property is vested in the

defendant along but that the plaintiff provided part of the purchase money, or voluntarily transferred the property to the defendant, the plaintiff establishes his claim under a resulting trust unless either the contrary presumption of advancement displaces the presumption of resulting trust, or the defendant leads evidence to rebut the presumption of resulting trust. Therefore, in cases where the presumption of advancement does not apply, a plaintiff can establish his equitable interest in the property without replying in any way on the underlying illegal transaction."

Type B: 'Automatic' (Failure to dispose) Resulting Trusts

- An RT will arise where A transfers property to B on express trust, but the trusts declared do not exhaust the whole beneficial interest.
    - Centred around the idea of 'jumping back'.
- Contrary to the name, this kind of trust does not occur regardless of the intentions of the parties.
- The presumption that the property is to go back to the settlor when he/she fails to dispose of the property can be rebutted by contrary evidence of intention.
    - If the settlor never meant the property to come back to them, there is no resulting trust.
- These are the kinds of trusts in *McPhail v Doulton, Morice v Bishop of Durham*, and *Choithram*.

Re Vandervell (No 2) [1974]

- Type A 'presumed' trust. 'The presumption thus establishes both that B is to take on trust and what that trust is'.
- Type B or 'automatic': 'The resulting trust here does not depend on any intentions or presumptions, but is the automatic consequence of A's failure to dispose of what is vested in him… the resulting trust does not establish the trust but merely carries back to A beneficial interest that has not been disposed of."
- Actually could be about intentions, if the settlor never actually thought they'd get the property back.
- Presumption that intention could affect these trusts. (*Westdeutsche*)

In Re the Trusts of the Abbott Fund [1990]

Facts

- Trust established for the benefit of the two Abbott daughters who couldn't provide for themselves, and whose father couldn't either.
- A fund was set up, and subscribers donated money according to a circular soliciting donations.
- Arrangement was found to be a discretionary trust.
- After the death of the beneficiaries, a surplus remained. Question over to where that money goes.
    - It can no longer be used for the benefit of the sisters, and there was no intention to provide the money to the sisters absolutely.

Held

- Resulting trust in favour of those who donated money.

- The court held that the money goes back to the settlors.
    - There's a surplus, there are no more beneficiaries under this DT, no provision telling us what to do with the property, so it goes back to the subscribers.

Re Gillingham Bus Disaster Fund [1858]

Facts

- Fund established to help victims of an accident.
- Due to the success of common law actions, the fund could not be exhausted.

Held

- Surplus held on resulting trust for the contributors.
- The other options were:
    - *Cy Pres* doctrine could apply.
    - Bona vacantia for the Crown if there is no other owner.
- But in this case, the court held there was a resulting trust.

Air Jamaica v Charlton [1999]

Facts

- Pension scheme for employees of Air Jamaica was discontinued when the Airline privatised (they made everyone redundant then hired back those who they wanted).
- The defined benefits were paid out, a surplus of $400m remained.
- The company claimed the surplus, as did the employees as contributors, and the Crown claimed as well.
    - Employees had been paid their entitlements, and the trust deed prevented the company from benefitting, therefore the Crown claimed bona vacantia.

Held

- This is a complicated situation.
- Eventually held that there is a resulting trust in favour of the contributors of the trust (50% to the workers, 50% to the company).
- Despite the fact that the employees were paid what they were owed, and despite the trust deed preventing the trustees from benefiting. **The court was just returning the money to where it came from.**
- Automatic: There was a trust, there was a surplus, there's a beneficial interest that wasn't disposed of – give it back to the people where the property came from.

Property is to be held on resulting trust for the settlor, unless the court can find a contrary intention.

- What would a contrary intention look like?
    - Could be the person or purpose should be absolutely benefitted, so if there is a surplus, then according to that absolute benefit purpose, the surplus should be used to benefit them.

- If the purpose has been completely abandoned, the Crown could claim (rare).
    - In some cases (*Re Bucks*) the surplus could be distributed to the members according to the terms of the contract, or in equal shares.
- How do we find contrary intention?
    - Look at the circumstances.
    - It only requires ordinary intention.

‘Quistclose’ Trusts

- Trusts are often used to take security in commercial transactions, due to the huge advantage they offer in an insolvency.
- Usual course of events when a creditor loans money to a debtor:
    - Unless the creditor has proprietary rights in the money, then they lose their money. Absolute ownership goes to the debtors.
- Then when the debtor goes insolvent, **why doesn’t the money come back?**
    - The money goes into the pool of debt for all creditors.

The *Quistclose* Trust

- One of the most significant forms of trust used in banking transactions, they provide a lender of money with a proprietary interest in the loan moneys in the event the borrow goes insolvent.
- When a debtor hold money for a creditor on trust, typically:
    - In a trust relationship, the trust ‘belongs’ in equity to the beneficiary, so that it cannot be used to pay debtor’s creditors, even in debtor’s insolvency.
        - The creditor who made the loan has property rights in that money.
    - If the debtor breaches the trust, the creditor can follow and claim the trust property.
        - Equitable remedies are available in the event of a breach.
    - Even if the trust property cannot be found, the creditor will have personal claims against third parties (as well as the debtor) if they have assisted in, or received property knowing of, the breach of trust.

Barclays Bank v Quistclose Investments Ltd

Facts

- A loan contract was formed in which Quistclose lent money to Rolls Razor solely for the purpose of paying dividends to its shareholders.
- That money was held in a share dividend bank account, separate from all other moneys.
- Rolls Razor went into insolvency before the dividends were paid.
- RR owe the bank around $400K, and this account with the money from Quistclose is in surplus around $200K.
    - The bank decides to cancel the accounts and try to use the surplus to set off the overdraft.
- Quistclose contended that the money in the share dividend account is held on trust for Quistclose itself. Barclays say it is not a trust, it’s a loan giving rise to a debt.

Held

Lord Wilberforce

- Upheld the finding of a resulting trust, based on it being an implied term of the loan contract that the money be returned to Quistclose in the event it was not used for the purpose for which it was lent.
    - The mutual intention of the parties was that the money be used to pay dividends, never that it should become part of the general assets of Rolls Razor. It was to be used exclusively for the payment of a particular class of creditors (those entitled to the dividends).

    - A necessary consequence therefore was that if the dividend could not be paid, it should be returned to the respondents.
    - Based off the word 'only' in the loan agreement.
- There were 2 trusts:
    - 1. Primary trust: Empowered RR to use the money to pay the dividend, AND
    - 2. A secondary trust: Required RR to return the money to the bank if it was not used to pay to dividend.
- '… arrangements of this character for the payment of a person's creditors by a third person, **give rise to a relationship of a fiduciary character or trust, in favour, as a primary trust, of the creditors,** and secondarily, if the primary trust fails, of the third person…'

How can a loan sit alongside a trust obligation?

- The bank argued no trust. It's a loan, giving rise to a debt. There cannot be a loan with debt obligations, and a trust with trust obligations.
- Lord Wilberforce rejects this argument; it means the law does not allow an arrangement to be made by which one person agrees to advance money to another, on terms that the money is to be used exclusively to pay debts of that latter, and if not, rather than becoming a general asset, is to be returned to the lender.
    - 'I'd be surprised if an argument of this kind has never been accepted.'
- When money is lent for a particular purpose, the borrower has an obligation to only use that money for the particular purpose, if not, then the loan must be returned.
- A loan contract can create both equitable and personal obligations.

Twinsectra Ltd v Yardley [2002]

Facts

- Twinsectra lent money was to Yardley for the purchase of property.
- T sought a personal undertaking from Y's solicitor Leech that the money would be used only for a designated purpose.
- Leech refused to give the undertaking, but it was provided by another solicitor (Sims, who was indebted to Yardley). Twinsectra relied on this undertaking.
- Yardley transferred the money to Sims. Sims simply passed the money in to Leech, who in turn passed it on to Yardley.
- Not all the money spent on property.

Held

Lord Hoffman (Majority)

- Held that this is a Quistclose trust, and that such a trust is an express trust.
- The money was held on express terms through the loan agreement. (Mark disagrees, you should agree with the CA):
    - Sims (a solicitor) held the money for Twinsectra in trust, but subject to the power to apply it by way of loan to Mr Yardley in accordance with the undertaking.
- The contract included a provision that the money was to only be used for certain purposes, therefore the money is held on trust for those purposes. The borrower is a trustee; using the money for any other purpose is in violation of the trustee's duties, and therefore void. This trust is created as soon as the contract is agreed, with the normal requirement for it to be validly created.

Lord Millet (Dissenting)

- He finds a Quistclose Trust is a resulting trust.
- Lord Wilberforce's speech suggests there are 2 trusts, a primary trust where the money goes from lender to borrower, and a secondary trust which reverses the interest.
    - Difficulties with this. What if the primary trust is not for an identifiable person, but is indeed for an abstract purpose?
    - Where is the beneficial interest?
- Wilberforce got it wrong; a Quistclose trust is a resulting trust. The beneficial interest remains with the lender, subject to a specified power that the borrower may use the fund according to the stipulation of the purpose.
    - Lender retains the interest throughout the transaction.
- More akin to a retention of title by the lender.
    - However this is confusing, because it says the money was held on resulting trust, and that the money should be returned.
    - More like the borrower is holding the money for the lender's benefit, and must either return it to them, or use it for the specifically designated purpose.

What is a Quistclose Trust?

Resulting Trust

- Lord Wilberforce (*Quistclose*)
- A QT is a resulting trust, there are two trusts, a primary and a secondary.
- Minority in *Twinsectra*
- It's a resulting trust, but disagrees with Lord Wilberforces 'dual trust' model.
- Argues that the lender retains equitable title of the property throughout the transaction.

Problems

- If the resulting trust only comes into existence after the misuse of the loan, it may be too late. If the money is not available because of the misuse, there is no remedy.
- It doesn't actually look like a resulting trust at all.
    - No intention to create a trust which failed.
    - This situation was intended from the start.
    - Property was held for the lender's benefit until it was used for the designated purpose.

Express Trust

- Majority in *Twinsectra.*
- A QT is an express trust; the money is paid to someone, but held subject to a trust, enforceable by the lender that they can only use for a particular purpose.

Problems

- Not upheld by the English Courts.
- Courts would require explicit terms to be a part of the contract.
- Doesn't satisfy the certainties required by an express trust.
- Arises because of intention: was there an intention for a trust to be made?

Best Argument

- Better argument is that a Quistclose trust is a resulting trust – the trust property goes back to the lender (secondary trust) when the purpose of giving the trust property (primary trust) has failed.

- This is why it's seen as a resulting trust – the equitable interest jumps back to the lender, even though they have transformed away the legal interest. The property goes back to where it came from, because of some unforeseen circumstance (how RT's arise).

Conceptual Basis for Quistclose Trusts

- A relationship of a fiduciary character or trust, in favour, as a primary trust of the creditors.
- Any analysis of the Quistclose trust must be able to accommodate gifts and loans for abstract purposes.
- The beneficiary must be the lender of the property, not an abstract purpose.
- The borrower can't have the beneficial title, the money can't just hang in suspense or have no owner.

Ultimately, Sims found liable for breaching the trust, Twinsectra got their money back.

Constructive Trusts

- The law relating to constructive trusts is complex, and oftentimes, elusive.
- An express trust is created when a settlor exercises her powers of ownership to create it.
- Resulting trusts are based on presumptions about a settlor's intention to create a trust.
- In contrast, that law itself imposes constructive trusts in circumstances where it would be unconscionable for the owner of property not to recognise someone else's right to the property.

What is a Constructive Trust?

- It arises in circumstances when the defendant knows that they are acting in an unconscionable manner (*Westdeutsche*)
  - It's not about the settlor's intention. D must hold it for the benefit of another person because it would be unconscionable not to do so.
- More of an imposition. It's preventing the person holding the property from doing with it what they will.
  - Any profits gained from the use of the property does not belong to the trustee.

What actions will result in a constructive trust?

- There is no set list, the boundaries are left deliberately vague so the court will not be restricted.
- Standard of whether or not it would be unconscionable for the person who has legal title **not** to hold the property on trust for someone else.
- Unconscionability is the key test.

Difficulties in this Area

- The duties of the trustee are unknown.
  - The duties are not clearly specified in the trust deed, because there is no trust deed.
  - There is doubtfulness, these trusts are often said to be bare trusts – trusts where the only obligation is to hand over the property when asked, and not to use it for own purposes.
- When can a court find a constructive trust? There is no hard test of 'unconscionability'.
- Remedial Constructive Trust

    - A CT which the court creates at the time of judgement as a discretionary remedy for unconscionable conduct.
    - Their basis is very uncertain.
- A remedial constructive trust is distinct from:
    - Institutional constructive trust which arises not at the time of judgement as a remedy, but at the time when a particular thing happened.
    - Important to distinguish when the CT came into existence when there is an insolvency.
- Equitable Claims: Proprietary claims to trust property, personal claims under third party liability, dishonest assistance and knowing receipt.
    - Ambiguous as to whether there is a constructive trustee over the person or a personal loss.
    - Different from the usual idea of being a constructive trustee, the property must be held for their benefit.
    - Third parties have a personal duty to account for any loss caused as a result of their actions.

We've seen CTs before

- *Goldcorp*: They were a beneficiary because of something they did.
- *Re Rose, Choithram*: The transfers were invalid at law, but still created a trust.
- *Page*: Secret trusts.
- *Westdeutsche*: High level principles of knowledge and conscience, applied to mistaken payments.
    - You've done something that means your conscience is bound to use the property for the benefit of another person, but you must have knowledge of the material facts.
    - This might apply to mistaken payments and theft.

When else may a CT arise?

1. Defendant unconscientiously asserts legal ownership of property to which another has contributed (*Lankow v Rose*)
2. Fiduciary improperly profits from his or her fiduciary position (*Keech, Regal, Sanford, Chinside, Reid*).
3. Property has been obtained by fraud/ultra vires action. (*Westdeutsche*).
    - Unconscionable for someone to hold onto that property if someone deliberately used a statutory formality to defeat another's proprietary rights.

Defendant unconscionably asserts legal title of property to which another has contributed

- Where one person makes contributions to property owned by another person, and there is no binding legal contract, the contribution must be the kind of contribution that would give rise to a resulting trust.
- Now covered by a statutory regime which excludes the use of a constructive trust.

Lankow v Rose [1995]

Facts

- Ms Rose and Mr Lankow lived together in a de facto relationship for 10 years. When the relationship came to an end, her assets were work around $30K, his worth around $625K.
    - Statutory regulation of **relationship property** replaces these rules for separations after 1976 (marriage) and 2002 (de facto).

- Legal title belongs to Lankow, who seeks to retain not only the legal title, but the whole beneficial interest. Rose seeks a beneficial interest in the property in recognition of her work done in the relationship.
- Ms Rose's contributions:
    - Unremunerated work for Mr Lankow's company.
    - Assisted with the administration of tenancies.
    - Contributed in a direct financial way to the building of the house.
- No express trust, because no intention.
- No resulting trust because Lankow paid the purchase price of the land.

Held

- Courts of equity have found another way of dealing with the inequality where someone has contributed to property owned by another:
    - You are conscience bound to use a part of this property for the benefit of another person. If you don't do this, a court of equity will step in and control your unconscionable conduct.
- Different approaches of overseas jurisdictions:
    - Canada: Unjust enrichment.
    - Australia: Unconscionability.
    - England: Focus on common intention in the relationship. Made it a reasonable person test.
    - NZ: Trusts.

Tipping J's Test

- To establish a constructive trust and be awarded a beneficial interest in the property owned in law by the defendant, the claimant must show:
    1. Contributions, direct or indirect, to the property in question.
    2. That he/she expected an interest in the property.
    3. The his/her expectation of an interest was reasonable in the circumstances.
    4. That the defendant should reasonable expect to have to yield an interest to the claimant.

If a claimant can demonstrate each of these four points, equity will regard the defendant's denial of the claimant's interest as unconscionable and will therefore impose a constructive trust.

1. Contributions

- Financial/formal work, or domestic work.
- Causal relationship must be shown (direct or indirect) to the value of the defendant's assets.
- 'I would allow as a contribution any payment or service by the claimant which either: (1) of itself has assisted the acquisition or increased the value of the property, or (2) by its provision helps the other party acquire, improve, or maintain the property or its value.
- Contributions made should exceed the benefits gained, so as to enrich the defendant (Hardie Boys J)
- Mere unequal sharing of household expenditure is not sufficient (*Nuthal v Heslop*).

2. Reasonable Expectation in the Property

- Claimant must subjectively have an interest in the property.
- Objective element – what would the reasonable claimant expect.

3. Defendant should reasonably expect to yield an interest

- Objective – was it reasonable in the circumstances? If it was made clear throughout that the defendant was not recognising any right on the part of the claimant, despite the work done, there would be no reasonable expectation.
- Just because there was no actual expectation does not necessarily bar equitable recognition of an objectively reasonable expectation (*Wilson v Webster*).

Quantum

- There was no equal sharing starting point in the statutory regime.
    - o If you are married, relationship property is assumed to be split 50/50.
    - o This is not the case, in 1995, the same rules did not apply to de facto couples.
    - o The claimant starts with getting nothing, they must show that they deserve everything they claim.
- "The Court must assess as closely as reasonably possible what weight the claimant's contributions have had against the contributions of the defendant in the acquisition, improvement, or maintenance of the property or its value."
- "The Court must, however, do its best to reflect in the assessed shares the value of the claimant's contributions. That value will represent, if uncompensated, the amount of the unjust enrichment accruing to the defendant which in turn is the amount of the claimant's sacrifice."
- Can be a relatively complicated tracing exercise of where does this value go.
- Work done for the company benefit Lankow, which he used to buy more property etc.

Harvey v Beveridge [2014]

Facts

- Dr Bird owned a unit.
- Mr Beveridge is recently released from jail, and is allowed to live in the unit.
- Dr Bird says 'it's yours', Mr Beveridge pays no rent, is responsible for the upkeep of the unit, and treats it as his own.
- BUT: No gift, no transfer of property. Can't be an incomplete gifts, no steps at all were taken to give it.
- Dr Bird dies, his testatrix attempts to take back the unit, Beveridge claims it is his through a constructive trust.

Held

- Beveridge had not contributed to the unit. He would have to prove he contributed 100% of the value of the property, which he cannot do.
- Based against the benefit of living rent free, he gave no benefit at all.
- Court says that Beveridge could have a claim based solely on the English model of intention, by claiming the Dr Bird intended to give him the unit.
- None of Tipping J's elements are met, Beveridge cannot have the unit.

Fiduciary Duties

- A fiduciary is not entitled to take an unauthorised profit from a trust.
- Any profit made by the trust will be held as part of the trust property on constructive trust.
- It is advantageous to a claimant to demonstrate that the defendant is a fiduciary, because that person is consequently prevented from making unauthorised profits from the relationship, from acting otherwise than in the beneficiary's best interests, and from permitting any conflict of interest.

Established Categories of Fiduciary

1. Relationships of Trust and Confidence
    - One party undertakes to act in the interests of another, or where she places herself in a position in which she is obliged to act in the interests of another.
    - Key obligation: Loyalty.

2. Relationships of Vulnerability
    - One person exercises power over another, so that person is vulnerable when that power is not used in their best interests.
    - Key obligation: Not to exploit the fiduciary's influence he may have over another for his or her own benefit.
        - Cannot use a fiduciary power for own benefit.

3. Relationships involving Confidentiality
    - Can arise in a variety of contexts.
    - Key obligation: Not to use information for own benefit.

Trustee/Beneficiary

- Paradigmatic fiduciary relationship.
- Duties of loyalty and impartiality.
- Prohibition on conflicts of interest.
- Prohibition on unauthorised gain or profit.

List of Fiduciary Duties:

1. Loyalty – Act in beneficiaries own best interests.
2. Not to profit or self-deal.
3. Not to act with improper motives.
4. Not to charge for their services.

Many relationships can give rise to a fiduciary duty.

Keech v Sanford [1976]

Facts

- Trustee (Sanford) held a lease for an infant. He was entrusted to look after this property until the child matured. But before that happened, the lease expired.
- The landlord had told the trustee that he did not want the child to have the new lease, because he couldn't put the lease in the name of a child.

- So Sanford purported to put the new lease in his own name.
- Keech, now an adult, sued Sanford for the profit he had been making.

Held

- Sanford holds the new lease on constructive trust for Keech.
- Even though there was no suggestion the trustee acted wrongly (no fraud, he genuinely tried to get the lease renewed etc), there was no possibility that the trustee has taken a benefit from his fiduciary office.
- May seem harsh that the trustee is the only person who cannot have the lease, but there is strict policy for doing so.
  - Without this rule, it would encourage trustees to search for loopholes to exploit their duty.
  - Removes the incentive for trustees to act dishonestly.
  - Therefore the rule must be strict.
- When people are a fiduciary, they must not act with their own self-interest.

Bray v Ford [1896]

- It is an inflexible rule that a person in a fiduciary position is not entitled to make a profit, this rule is not founded upon principles of morality. It is **based on the consideration that, human nature being what it is, there is a danger of the person holding a fiduciary position being swayed by interest rather than by duty**, and thus prejudicing those whom he was bound to protect.
- It's not about morality, it's a rule based on the flawed nature of man.

Regal (Hastings) v Gulliver [1942]

Facts

- Regal Ltd owned cinemas; wanted to purchase the lease on two other cinemas.
- Regal formed a subsidiary (Amalgamated [AM]) but the subsidiary was under capitalised (Regal could only find 2/5ths of the necessary capital).
- Owners of the leases in the two cinemas became concerned that Regal might not be able to continue paying the rent; required the capital to be paid up front OR have the directors personally guarantee the rent until the share capital was paid up.
- Instead of providing the personal guarantee, the directors purchased the remaining shares in AM for themselves.
- AM was subsequently sold at a profit. Regal was also sold.
- Regal came under the management of a new board of directors, who initiate proceedings against the former board.

Issue: Did the old directors owe a fiduciary obligation to the company?

- New Regal is arguing there is a breach, as the old directors made a profit from their actions.
- The old directors claimed they acted in good faith, the deal was always planned, they were seeking to make the best possible deal for their shareholders.
  - There was insufficient capital, so the directors acted to make up that difference.
  - The claim the profit was incidental.

Procedural History

- In the lower courts, the liability theory advanced focused on the idea that the directors had acted in bad faith or against Regal's interests – they had intended all along to take the profit for themselves.
  - It was held that bad faith was a necessary element, that they were depriving their company of an opportunity.
- Therefore there was a focus on good faith and pursuit of Regal's interests.
- They were thereby depriving the company of an opportunity and a profit which should have been secured to it.
  - There had to be a duty to take the opportunity to buy the property. If they didn't have that duty, then they could profit.
  - A much more lenient rule, but it's not correct. Fiduciary duties are strict.

<u>Held</u>

- Proceeded on the basis that the directors acted in good faith, intending to act in the interests of Regal. But, as fiduciaries, the former directors were required to disgorge their profits.
  - Court affirms that the case law holds there is a fiduciary duty.
  - They weren't being dishonest, or acting contrary to the interests of the company. The directors were acting in good faith, but they made a profit, and have to be accountable.
- The transaction only could have gone ahead with the cash put in by the directors.

<u>Lord Macmillan</u>

- The question to be asked is did you make a profit, and was that profit made in the course of your acting in the role of a fiduciary?
- The question of whether or not they acted fraudulently has no relevance to this question. Once the profit has been made, they have breached their fiduciary duties.
  - What the directors did was so related to the affairs of the company that it can properly be said to have been done in the course of their management and in utilisation of their opportunities and special knowledge as directors.
  - That what they did resulted in a profit to themselves.

<u>Reason for the strictness of the duties</u>

- It encourages the single-minded loyalty of the fiduciary.
- Deterrent aspect: there is no possibility of getting around it.
  - Protects the beneficiary, and the fiduciary from abusing their position.
- Avoids issues with proving relevant facts and intentions, simpler approach.

<u>'Fact Based' Fiduciaries</u>

- Established on the facts rather than inherent in the category.
- Joint venture partners ('strong case') are a good example.
  - Business partners trigger a fiduciary duty.
  - A joint venture is a partnership over a single issue, it probably does trigger a duty.
- Key indicators:
  - Power/vulnerability.
  - Confidentiality
  - Trust/confidence.
  - Property held for the principal.

Chirnside v Fay [2006] NZSC

Facts

- Chirnside and Fay collaborated on a site development project.
- Chirnside loses confidence in Fay, and decides to exclude him from the venture. The development proceeded to completion.
- Fay wants his share of the profits: claimed that Chirnside owed Fay fiduciary obligations which he breached by excluding him, and he owed him the profits that he made.
- Chirnside argued he and Fay had no legal partnership of any kind.

Procedural History

- In the HC and CA, it was held that Fay and Chirnside were parties to a joint venture in the development.
- Appeal against the determination that Chirnside owed fiduciary duties.

Issue: Do joint venture partners owe each other fiduciary duties?

Held

- Fay does not have a common law claim, but because Chrinside owed him fiduciary duties in equity, which he then breached, Chirnside must account for the profit.
- Although there was no legal partnership, they were in a joint venture, acting together to pursue a particular project.
  - They were going to have to share profits etc.
  - SC analogised it to a business partnership over a single issue.
    - 'We cannot accept Mr Whiteside's submission that the parties had not reached sufficient agreement or understanding on key issues to move this transaction from one of antagonism to one of collaboration'.
  - It was a different kind of joint venture, but it's fallacious to think unless a contract sets out every requirement, no joint venture can be agreed to.
- The courts below were correct in finding their relationship was such that Chirnside owed Fay fiduciary duties which he breached when he unilaterally excluded him from the venture.

What on the facts showed a fiduciary relationship?

- Joint venture was analogous to a partnership. It did not matter that they had not formalised their agreement.

Fiduciary Factors:

1. Worked together on feasibility calculations, with architects, council, and others.
2. Joint negotiations to purchase Speight's Building.
3. Not antagonistic.
4. Mr Fay liaises with Harvey Norman.
5. Mr Chirnside introduced Mr Fay as a principal in the development.

Leaving a joint venture

- Appropriate notice.
- Release of the parties from their duties of loyalty to each other.
- Possibility that duties of confidentiality will remain after the termination of the joint venture.
- Need to agree as to how assets are to be shared.
- Equitable obligations continue through the 'winding up' period.

Amaltal Corp Ltd v Maruha Corporation [2006]

Facts

- Commercial fishing 'joint venture' set up under a joint company.
- Amaltal through its accountant conceals tax deduction, to its benefit (gets a higher payment from Maruha).

Held

- Court held that when you look at what has been set up, determine whether it is one where fiduciary duties apply.
- The general relationship in this case was not fiduciary; former partnership was replaced with company.
- But, Amaltal was a fiduciary for Maruha in respect of accounting and tax returns, which it had undertaken for the joint company.
    - Look at the commercial agreement, it is no just about what it is called, it's about **what the company actually did**.
- There may be aspects were something that you are doing creates a fiduciary duty. That particular aspect means that one of the parties can impose trust and confidence.
- Therefore, there are 2 possible situations:
    - 1. Is it a general set of categories where FD arises, then:
    - 2. Commercial relationships that don't fall into a fiduciary duty
        - **But** it can be assumed that because they're acting on behalf of the other party, in that particular course of action, they are acting as a fiduciary.

- *Amaltal*: It is 'well settled that, even in a commercial relationship of generally non-fiduciary kind, there may be aspects which engage fiduciary obligations of loyalty. That is because in the nature of the particular aspect of the relationship, one party is entitled to rely upon the other, not just for adherence to contractual arrangements between them, but also for loyal performance of some function which the latter has either agreed to perform for the other or for both or has, perhaps less formally, even by conduct, assumed.'

Paper Reclaim Ltd v Aoteraroa International Ltd [2007]

Tipping J: Is this the kind of situation where one of the parties should be entitled to impose trust and confidence on the other? Was there anything in particular about their relationship?

- This test focuses on the intentions of that parties.
- Question is:
    - What did the parties intend, and how can we give effect to that?
- 'To style a contractual relationship as a joint venture may be apt to distract. It is a term to be applied with caution.'
    - When parties have formed a contract, the correct approach is first to decide exactly what they have agreed upon.
    - Only then should the court consider whether any aspect of their agreement gives rise to a relationship which can properly be characterised as fiduciary, imposing an obligation of loyalty on one or both parties, which supplements the express or implied contractual terms.
    - A fiduciary relationship will be found when one party is entitled to repose and does repose trust and confidence in another.

- "The existence of an agreement, express or implied, to act on behalf of another and thus to put the interests of the other before one's own is a frequent manifestation of a situation in which fiduciary obligations are owed."

Distinction between CL approach to relationships and the fiduciary approach

- Fiduciary Principles: Fiduciary must subjugate his/her personal autonomy to the interests of others.
    - You're supposed to be acting for the benefit of another person and you cannot act in your own interest.
- Common law: Personal freedom stops where harm to others starts.
    - Can act for your own benefit up to the point where you harm others.

Breach of Fiduciary Duty

What happens when a fiduciary fails?

- Personal remedies: compensation, account of profit etc.
- Proprietary rights: Held on constructive trust.
- Basic distinction: Have a personal right against this person vs being able to say that you have a proprietary right in the particular asset. Whether you have a personal or proprietary claim depends on the type of breach of the duty.

Advantages of Proprietary Remedies

1. Insolvency: If you have a proprietary claim to assets in the insolvency pool, you have a full claim on those assets, dollar for dollar.
2. Tracing – Following the property into the hands of the third party recipients.

Categories for Breach of Fiduciary Duties

1. When a breach of duty involves actually using trust property to make unauthorised gains.
2. Where a breach of fiduciary duty involves using opportunities arising out of the fiduciary position (*Keech v Sanford, Regal, Boardman*).
    - Orthodoxy is that if you use a principal's property or your own position, then both personal and proprietary remedies will be available.
3. Where breach of the FD does not involve using trust property or involve opportunities;
    - Fraud, bribery, other kinds of secret profits.
    - This category is much less clear.
    - A number of cases hold that there is only personal liability. The controversial question is whether a bribe imports a collective trust, due to its illegal nature.

Profits from Bribery

- The law is undecided on this point.

Attorney General for Hong Kong v Reid [1994]

Facts

- The former Director of Public Prosecutions for Hong Kong had accepted bribes not to prosecute certain individuals accused of having committed crimes within his jurisdiction.
- The bribes he had received had been profitably invested.

Procedural History

- High Court and Court of Appeal both held that Reid has only a personal duty to account for the bribes.
- Why is the case held in NZ?
    - Reid used the bribed to invest in a property in Tauranga.
    - AG claims he is owed the value of the bribes.
    - Hong Kong has a proprietary claim to the bribes, traced to Tauranga houses. AG can sustain a caveat.
    - Caveat was lodged to prevent Reid selling the houses and running.

Held

Lord Templeman

- Because in good conscience Reid ought to have given up the bribe when it was received, a constructive trust should have been deemed to come into existence automatically, and
- Because equity looks upon 'as done that which ought to have been done', the bribe would be deemed to have belonged to the claimant from the moment it was received, therefore anything bought with the bribe would be considered the property of the claimant.
- The device for effecting this transfer of ownership to the claimant was by means of a constructive trust.
- Therefore the houses were held on constructive trust.

Why was there a property right?

- Clear breach of fiduciary duty: Occurs while Reid is acting as a fiduciary of the government.
- In account of profits, you just have to account for the initial value of the money, but this value may have increased through investment.
    - If there is an increase, the fiduciary pockets the increase.
- Bribery is an evil practice, should not allow an errant fiduciary to profit from their bribery.

Policy Implications

- If the fiduciary becomes bankrupt, the bribe would be taken from their assets.
- The fiduciary has to account for the original amount, and all their profits made by using it. Privy Council supports this.

Ratio: Every kind of profit made by a fiduciary is held on trust, giving rise to a proprietary claim.

Sinclair Investments (UK) Ltd v Versailles Training Ltd [2011]

Facts

- Ponzi scheme makes businesses seem more valuable than they are, and shares are sold for huge profit.

- Principal claims proprietary rights in proceeds of the share sale, as profits were gained in breach of the fiduciary duty.

Held

- EWCA reviews the authority and principle, concluding that there is no proprietary right to assets obtained in breach of fiduciary duty unless:
    - 1. They are obtained through funds previously owned by the principal; or
    - 2. Derived from opportunities of the principal.
- The EWCA sided with academics.
    - Why should the principal be favoured over other creditors?
    - The principal cannot have been benefitted by a bribe.

FHR v Cedar Capital

- Agent for the purchaser takes secret/undisclosed commission from vendor.
- Possible rules: See arguments 10 – 11, 30 – 31, big academic debate at [29].
- Precedent is divided, argument against proprietary remedy is not well founded.
- There is no right answer.
- Strict conflict of interest principle applies to such cases.
- The constructive trust rule is good as a matter of principle – bribery is bad.
    - Principal may have been disadvantaged, allows tracing, fiduciary must disgorge the 'whole benefit'.
    - Simplicity vs uncertainty, harmonising the common law in different jurisdictions.

Tracing

Introduction

- The law of trusts will always try to come to the aid of the beneficiary.
- There are three ways for beneficiaries to recover any lost property.

1. Personal liability of trustees for the breach of trust
    - Specific restitution – restore the specific property.
    - Restore funds in cash.
    - Equitable compensation
    - Account of profits.

2. Personal claims against third party strangers for their involvement in a breach of trust.
    - Whether because they assisted that breach of trust dishonestly or
    - Because they received property from a breach of trust unconscionably.

3. Proprietary claims against third parties
    - Tracing property that was originally held on trust or
    - Was used as a substitute for that trust property.

Proprietary claims against third parties

- Tracing is an attempt by a claimant to establish a proprietary claim to a specific piece of property by racing a pre-existing piece of property into it.
- "Tracing properly so-called… is neither a claim not a remedy but a process. Moreover, it is not confined to the case where the plaintiff seeks a proprietary remedy; it is equally necessary where he seeks a personal remedy against the knowing recipient or knowing assistant. It is the process by which the plaintiff traces what has happened to his property, identifies the persons who have handled or received it, and justifies his claim that the money which they handled or received (and if necessary which they still retain) can properly be regarded as representing his property. He needs to do this because his claim is based on the retention by him of a beneficial interest in the property which the defendant handled or received'

Following vs Tracing

Following: Simply identifying where one's property has gone, and pointing to it in the hands of whoever has it, it focuses on the original property. **Involves following the same asset as it moves from hand to hand.**

Tracing: Still about property, but it looks to what a particular person has done with your property, as they substitute your original asset for various substitutes in the course of their dealings. **Involves identifying a new asset as a substitute for the old.**
The process can include both where one asset is exchanged for the other, the plaintiff can elect to follow the asset into the hands of the new owner, or find its value in the new asset in the hands of the same owner.

Rationale behind tracing

- The law allows the claimants to make their claim against substitute property. Essentially the claimant is identifying property that they never had any right in and saying it is theirs.

- The traced property represents the value/proceeds of the original property, so it belongs to the claimant (*Foskett*)
- The rationale is based in property rights. You own the original property, so if you can identify the substitute, you can claim it as belonging to you in place of the original property.

Common Law Tracing

- One is asserting their common law title, there is no need for a fiduciary relationship.
- The common law claim is 'that's my asset over there, unless you have a defence third party, you must give it to me'.
- Common defences:
    - Property purchased in good faith, with the purchaser ignorant of the trust obligation.
    - '**Equity's Darling**' – A good faith purchaser for value without notice of the equitable interest takes the interest free from anyone else's title.
- Common law is not adept at tracing into mixtures, only available through equity.

When is tracing useful?

- When a claimant's personal claims are not promising.
- When the original trust property cannot be found, but a substitute property can be.
    - Not possible to make a following claim, third party may be equity's darling.
- When the substitute property is worth more than the original property.
- Increasing instances of increasingly sophisticated fraud.
- Claimant's asking for relief where (for example) their funds have been misappropriated and passed through various bank accounts.

Process of Tracing

1. Trust or fiduciary relationship.
2. Breach of the obligation arising in equity.
3. Point to the original property (must be particular property).
4. Tracing or following the asset/value
    a. Evidential process.
    b. The rules exist to figure out where the money has gone.
5. Are there any defences?
    a. The purchaser was equities darling.
    b. Change of position in response to gaining this property.
6. What is the remedy?
    a. Constructive trust
    b. Equitable charge
    c. Lien
    d. Subrogation.

- Extremely complication process.
- Lord Millet noted no one agrees exactly on how the process works.
- There is added complexity because the common law and equity do not agree on exactly the same approach to this issue.

Banque Belge v Hambrouck

Facts

- Cheque that has been paid, misappropriated by H from his employer.
- Presented to Banque Belge who pays out cash money to Hambrouck.
- H then deposits the cash into his own bank account.
- Then he withdraws the money and gives it to his mistress who places it in her bank account.

Issue: The property has change form: from cheque to chose in action, to currency. Controversy over whether the judges used common law or equitable tracing.

Held

- The facts remove any difficulty in the way of the Bank recovering without having recourse to equity – so whilst equity has a better sense of tracing into mixtures, this is not what has occurred on the facts.
- Banks LJ holds that the claim is made in common law tracing.
- We don't need to use equity: it's not the same asset, the form it has taken has changed a number of times before it ended up in the bank account of the mistress, but it has not been mixed.
- Common law tracing works as long as the asset has not been mixed.

Agip (Africa) Ltd v Jackson

- 'The common law has always been able to follow a physical asset from one recipient to another. Its ability to follow an asset in the same hands into a changed form was established in *Taylor v Plumer*.'
- 'Money can be followed at common law into and out of a bank account and into the hands of a subsequent transferee, provided that it does not cease to be identifiable by being mixed with other money in the bank account derived from some other source':
  - We can trace money in and out of bank accounts as long as there is no mixture.

Problem with common law tracing

- Very rarely going to have no mixtures: historically it was common to not have any money in your bank accounts, but nowadays virtually everyone does. If you can't trace into mixtures, that creates a big problem.
- As soon as there's a mixture, you cannot trace in common law. The question changes to whether or not you have a claim in equity.

Tracing in Equity

- It is a pre requisite of an equitable tracing claim that the claimant had some equitable interest in the original property, or that the person who transferred the property away had a fiduciary relationship to the claimant, such as being a trustee.
- Requirement of a pre-existing equitable interest or fiduciary relationship (*Foskett*).
  - Historical roots in equity as a separate court of law.
  - Now outdated, but still used.
- Once a pre-existing equitable interest is demonstrated, the claimant is able to trace their property into the most complex of mixtures.

Example

- At law, money paid into a bank account becomes property of the bank. The account owner has a thing in action to the extent of the deposit.
  - Not stored somewhere in the bank, it's just noted that you have paid off some of the debt or the bank owes you more.

What can the claimant get?

- This will depend on the initial equitable property right.
- He will normally be able to maintain the same claim to the substituted asset as he could have maintained to the original asset. You can claim whether you equitable right was previously:
  1. An equitable ownership interest – **constructive trust** over the traced asset, or over proportion of mixed fund.
  2. An **equitable lien** or charge.
     - Enforcing repayment of the misapplied property: allows you to say that the property belongs to me for the purposes of paying back the debt owed to me.
     - Binding on third parties.
     - These are proprietary rights.
       - Protected in an insolvency.
       - You can claim an increase in value/secondary profits.
- Asserting a lien only entitles the claimant to the value they lost.
- Claiming a constructive trust (co-ownership) entitles the claimant to any profits which they may have gained.
- If the asset has increased in value, better to claim co-ownership.
- However, if the asset has decreased, it would make much more sense to assert a lien.

Loss of the right to trace

- If the particular traced property is destroyed, made into a different asset (fixtures/accession), or can no longer be found, then the proprietary right is lost.
- If the traced property is in the hand of a bona fide purchaser for value without notice, they take the property free from any other claim, the proprietary interest is also lost.
- It would be necessary to track backwards through the tracing process until you arrive at a point which allows a claim to be made against some piece of property.

Equitable Tracing: Tracing into Mixtures

- Equity has evidential rules, presumptions, and ideas about where the trust property has gone in the event of a mixture. We can figure out who has rights in the mixture when it is not possible to identify whose property is whose.

Tracing in Equity

- Requirement of a pre-existing equitable interest or fiduciary relationship: classic example is a trust.
- Requirement of an equitable base being required **is doubted by commentators and in obiter** due to tracing being an evidential process, rather than an equitable claim.

No Mixture

- Just as with CL tracing, equitable tracing allows someone to make equitable proprietary claims to money in a bank account or assets purchased with money that is exclusively derived from the original trust property.
  - If there is no mixture, the common law and equity are on par regarding sorting that out.
- *Foskett v McKeown*: The simplest case – where a trustee wrongfully misappropriates trust property and uses it exclusively to acquire other property for his own benefit.
  - In such a case, the beneficiary is entitled to at his choice either:
    - Assert his personal ownership of the proceeds OR
    - Bring a personal claim against the trustee for the breach of trust and enforce an equitable lien on the proceeds.
  - He will usually exercise the option most beneficial to himself.
    - If the traceable proceeds have increased in value, he will assert beneficial ownership.
    - If they are worth less, he will claim a lien and take the whole of the proceeds.
- As the beneficiary takes the whole asset, it generally is irrelevant as to whether there is a constructive trust or a lien.

Mixtures: Basic Ideas

- Where the trustee takes money that is supposed to be held on trust, sells it, gets traceable proceeds, but then combines that in his or her bank account. It becomes impossible to know whose money is who's in a single bank account (fungible assets issue).
- Equity gives rules allowing us to deduce which property belongs to which person.

1. Mixture of 2 Trust Funds or with Innocent Volunteer's Money

- Concerns the situation where trust property is misapplied such that the trust property is mixed with property belonging to an innocent third party: it is necessary to decide how property belonging to innocent parties should be allocated between them.
  - The entitlement of the beneficiary to the mixed fund should rank proportionately with the rights of the innocent volunteer.
  - As between beneficiaries or other innocent contributors – proportionate shares (neutrality) – we don't want to penalise innocent contributors.

- More difficult when the fund containing the mixed property is used in chunks to acquire separate property – which innocent contributor to the fund ought to take which right in which piece of property? There are 2 approaches:
  1. Orthodox Rule: *Claytons Case* held the appropriate principle is first in, first out – the money first deposited is used first in the property acquired.
  2. Alternative approach: To decide that each contributor should take proportionate shares in all of the property acquired with the proceeds of the mixed fund.
- Current preference is for a proportionate share approach, but only where the application of the orthodox approach would produce an approach that is irrational and arbitrary.

The court's purpose when dealing with mixtures of the property of two innocent people is to achieve justice between them if there is no obvious fault on the part of one party or the other.

2. Mixture of Trust Money with Trustee's Own Money

- In deciding whether the property used was taken from the trust or the wrongdoer's own money, the courts will select the approach that achieves the most desirable result for the beneficiaries.
- Between the wrongdoer (trustee) and the beneficiary, the former's rights are 'subordinated' to the beneficiary's rights.
  - *Re Hallet's Estate* [1880]: We presume the wrongdoer as acted as she should have (ie: Any issue with the money must have been the wrongdoer's fault).
    - Where the trustee has money in a personal bank account to which trust money is added, the trustee is acting honestly when paying money out of that bank account. Hence it's assumed that the trustee is paying out her own money on investments that lose money, not the trust's money.
- Remaining money belongs to the beneficiary.
  - But the plaintiff's claim cannot be greater than the **lowest intermediate balance**; overdrawn accounts contain none of the plaintiff's money in them, and money subsequently put in is not the plaintiff's (unless the defendant intended to restore the plaintiff's money).
- *Re Outway*: B's are entitled to elect either that the property be subject to a charge as security for amounts owed to them by the trustee, or that the unauthorised investments are adopted as part of the trust fund.

Courts are prepared to protect the beneficiary at all costs from the misfeasance of the trustee.

Foskett v McKeown [2001]

Facts

- Mr Murphy, a trustee for the plaintiff's trust, had committed a breach by taking money held on trust to pay two out of five premiums (value of $20k) on a life insurance policy that he had taken out over his own life in favour of his children.
- Murphy commits suicide and insurance payment of $1m is paid to the children.
- Murphy's breach of trust identified, and most of the money cannot be traced. There is a shortfall in Murphy's estate property, and compensation is required.
- Beneficiaries of the trust claim a proportionate share of the premium (20%/$200k) but children, and CA say only the premium amount is repayable (the 20k).

Held

Lord Millet

Tracing Rules

- When a trustee wrongfully uses trust money to provide part of the cost of acquiring an asset, the beneficiary is entitled at his option either to claim a proportionate share of the asset, or to enforce a lien upon it to secure his personal claim against the trustee for the amount of misapplied money. He will normally exercise the option in the way most advantageous to himself.
- Tracing is part of the law of property's purpose of vindicating the property rights of the original equitable owner. The beneficiaries should be entitled to trace their money from the trust into the premium payments and then into a proportionate share of the limp-sum payout after the trustee's death.

Tracing Process

- 1. The plaintiffs were beneficially entitled under an express trust to a sum held by Mr Murphy (the original trust property).
- 2. The money is moved in and out of various bank accounts until it is mixed into Mr Murphy's personal bank account with his own money in breach of trust. The plaintiff's money formed an indistinguishable part of the balance of his account, which represents a debt due from the bank to Mr Murphy (a thing in action).
    - When the substitute piece of property is transferred to a different b/a in a different bank, it disappears and you replace it with what it was exchanged for: the new substitute property.
    - When the money reaches Mr Murphy's account, the traced property has gone through a few substitutes already, but it is now a claim against the bank to pay back what it owes to Mr Murphy: **property is a thing in action.**
- 3. Then the plaintiff's money was represented by a different thing in action, the debt due from an insurance company to its policyholders.
    - In return for the property, the policy holder got a bundle of rights, mainly a return for the premiums.
- 4. Finally it formed an indistinguishable part of the balance of standing to the credit of the respondent trustees (Mr Murphy's children).
- The plaintiffs do not trace the premiums paid directly into the insurance money paid out to Murphy's children.
    - They trace them first into the policy and then into the proceeds of the policy.
    - The debt they allege they have is the rights Murphy received under the policy.
    - It follows that if a claimant can show the premiums were paid with his money, he can claim a proportionate share of the policy.

Reasoning of the CA

- The majority held that the plaintiffs could trace their money into the premiums but not into the policy, and were accordingly not entitled to a proportionate share.
- Sir Richard Schott VC: the use of the plaintiff's money gave a lien on the proceeds of the policy for the return of having the premiums paid, but could not divest the children of their existing interest.
    - It has never been suggested that the beneficiary is confined to his lien for repayment of the premiums because the policy was taken out by the trustee. The ownership of

the policy defends on the identity of the party or parties whose money was used to pay the premiums.
    - Claimant should be entitled to a proportionate share of the proceeds, regardless of whether some of the premiums were paid by the claimants and others with Mr Murphy's money.
    - No reason to differentiate between the first premium and later premiums. Such a distinction would lead to capricious results.

Hobhouse LJ

- The payment of the fourth and fifth premiums of the plaintiff's money made no difference to the amount of the death benefit. Once the third premium had been paid, there was sufficient value in the policy.
- This argument is based on causation, but the question to be asked is attribution; whether the death benefit is attributable to all the premiums or only to some of them? The answer is that it's attributable to all because it represents the proceeds of realising the policy, and the policy in turn represents the product of all the premiums.sation
- It is not correct to say the last 2 premiums contributed nothing. It was true that they were not needed to provide the death benefit, but Mr Murphy could not see the future. He did pay the last 2 premiums with the plaintiff's money, and they were applied by the insurer towards the payment of internal premiums needed to find the death benefit.
- His approach also introduced unacceptable and capricious results. Why should it be necessary to identify which specific payment prevented the policy from lapsing?

Complications in *Foskett v McKeown*

- Lord Millett's problem with Hobhouse's LJ's view in the CA:
    - Hobhouse essentially argued that the final payments were not causally responsible for the payout because after the first three payments, the insurance policy wouldn't have lapsed by the time Murphy committed suicide.
    - Essentially argued that these payments weren't necessary, therefore can you really argue they were a contribution to that final payment?
    - Argument revolved around the intricacies of the contract.
- Millet disagrees: This is not how it works. The insurance policy is a contract, and consideration is all of the premium payments. As soon as you proportionally contribute to premiums going in, you've contributed to that deal, and therefore your property is traceable to rights and obligations under that deal.
    - Beneficiaries provided 2/5ths of the consideration paid, therefore they should get that proportion of the payout. Beneficiaries can make a claim in proportion, but they don't get a claim over all of it.
    - All of the money paid to the insurance company was part of a mixed fund that paid off the units. The money going in was clearly something which contributed to the final payout.
- Sir Richard Scott claimed that the plaintiffs could get their money back, but not a share of the profits.
    - Problem with this view is that it says that a lien existed over the proceeds of the policy for the return of the premiums paid with their money. This is a proprietary claim.
    - Millet says if there is a proprietary claim available, there is no reason it can't be a constructive trust. The usual rule would be applied in a tracing process (two innocent volunteers), which is proportionate shares.

Backwards Tracing

- What happens when the property is destroyed or dissipated (spent on a dinner etc?)
- Tracing in equity is not possible, the tracing claim runs out.
- Tracing is a proprietary claim (a claim for a particular asset). If that particular asset cannot be identified, because it no longer exists, the claimant will have to rely on a personal claim if one is even possible.
- Equitable tracing presupposes the existence of the property.

Key Limitation: Money paid into an overdrawn bank account

- The overdrawn bank account is a debt owed to the bank. When the money is paid into it, it is paying of that debt.
- Therefore the property disappears. It goes from being a debt owed by the bank to the defendant to property having being used to pay off a debt.
    - You can only claim what is in credit.
- Personal claims for the breach of trust are still possible but are 'unsecured'.

The use of trust property to repay a debt

- The payment of a debt discharges an obligation. What property would the beneficiary be claiming?
    - One potential way around this issue: Make a claim over the property which was purchased causing the debt to exist. Eg: If the property is used to pay off a mortgage, make a claim to the house.
- This is backwards tracing.
    - Orthodox theory: B's money did not pay for T's asset. Therefore there is no claim.
    - Usually backwards tracing is not seen as possible. The fact that the overdraft occurred in order to buy an asset doesn't change the fact that it's not your asset. It was T's property, and your payment extinguished the debt rather than paid for the asset.
- Privy Council has recently stated that such claims may be allowed:

Brazil v Durant International [2015]

- 'The claimant has to establish a coordination between the depletion of the trust fund and the acquisition of the asset which is the subject of the tracing claim, looking at the whole transaction, such as to warrant the court attributing the value of the interest acquired to the misuse of the trust fund.'

Money used to improve the property

- If an errant trustee used money taken to improve their property, the beneficiary would be able to claim a constructive trust or a lien over the property. No problem.
- Issue when an innocent volunteer uses trust property to improve their property.
    - No new asset purchased, nor a mixture of trust property – the improvement or maintenance of something that belongs to the innocent volunteer.
        - 'The questions whether tracing is possible, and if so to what extent, and also the question with an effective remedy by way of a declaration of a charge can be granted consistently with an equitable treatment of the innocent volunteer, present quite different problems' *Re Diplock*
- If the improvements do not increase the value of V's property, should equity step in and say some of the property belongs to the beneficiary? No, because there is nothing to which B's property can be traced (*Diplock*).

    - The trust money cannot be traced and extracted from the altered asset, because the trust money didn't leave any value behind, there is nothing into which it can be traced.
- There can be a lien, however much value was put it, the innocent volunteer may have to pay that back to the beneficiary.
- But, unless the person improving their asset is the errant trustee, the beneficiary will not have a proportionate claim over the asset of the innocent volunteer.
- In many situations it would be too difficult (too inequitable) to untangle B's property from the 'improved' property.
    - Eg a charity used the money, it may be impossible to give a remedy which isn't equitable.

<u>Money in current bank accounts</u>

- If an errant trustee mixes the beneficiaries money in a mixed fund:
    - T's claims are subordinated to B's (*Foskett v McKeown*)
    - Property left in the fund is B's (*Re Hallet's Estate*)
    - T is assumed to spend T's own money first.
    - Unless *Re Oatways* applied; B can claim their money was used for valuable investments.
    - The beneficiary can choose whether they claim a CT or a lien (*Foskett*)
    - In *Re Oatway*:
        - If the first payment was some asset that depreciated in value, and the second payment dissipated, then you're allowing the beneficiary to choose.
        - They can decide that their money was spent on the thing most beneficial to their claim.

Personal Claims Against Trustees (and Fiduciaries)

Array of claims which can be brought

1. Proprietary claims: trust property
    - Proprietary claim can be against the trustee, or it could be against a third party with no defence.
    - Claim used where there is property to follow or trace. If there is no property, the beneficiary must rely on personal claims.
- In addition to any proprietary claim you might have, you can also say that the trustee has to remedy the situation in their personal capacity – must make good the loss caused by the breach of trust.
2. Personal claims: Against the trustee
    - The trustee as a person has breached the trust and will be liable to pay for the beneficiary's loss.
3. Personal claims: Against third party stranger
    - Personal claims can be made against third party strangers without defence.

When will there be liability for breach of trust?

- Trustees are liable for any loss **caused** by a breach of trust (*Target Holdings*). There are different kinds of breaches which may cause your loss.
    - Loss/devaluation of assets in the trust fund (B can only sue when there is a loss).
    - Any breach of any of the duties of the trustees.
    - A breach of any term in a trust instrument/deed.
    - Any kind of statutory duty placed on trustee.
    - Breach of duty of prudent investment, and general prudence and diligence in conducting trust business.
    - Breach of fiduciary duties (not acting impartially, allowing a conflict of interest, profiting etc).
- Even if there is a breach, consider that the court may exclude liability and relief:
    - S 73 Trustees Act – if the person acted honestly and reasonably
    - Exclusion clauses.

Remedies for Breach of Trust

1. Specific restitution
    - Obligation to put the misused trust property back if possible.
    - Restore any property transferred away in breach of trust.
2. Restore trust fund in cash
    - If the original property cannot be recovered, then the trustee bears a personal obligation to restore the trust fund in cash terms.
3. Equitable compensation:
    - If it's impossible to put back the trust property, might be asked to pay financial remedy out of the trustee's pocket to restore the loss.
4. Account of profits
    - If the breach results in a profit, the beneficiary can claim this amount of profits.
    - This will kick in not only when you're talking about a trustee, but whenever there is anyone breaching his or her fiduciary obligations.

Where a profit is made (*Chirnside v Fay*)

- A trustee or fiduciary will be liable in a situation where a profit is made.
- The remedy is to strip the profit from the trustee or fiduciary and give it to the beneficiary. To ensure fairness, there are 3 steps in this process:
    1. Define the net profit/gain properly
    2. Apportionment (not going to give away profit that came from source/s other than the breach of fiduciary duty – not all profits can be attributed to original breach of FD.
    3. Allowance for skill, effort, enterprise.
        - If the trustee's conduct was an act of skill, effort, or enterprise, and if you allow the beneficiary to take that value, this could be unjust.

1. Net Profits/Gain

- Ordinary definition of profit: sale price X units sold – the cost of manufacturing = profit.
- Distinction between the entrepreneurial element involved in a business, and the costs incurred in carrying it out.

2. Apportionment (attribution)

- What was gained/lost as a result of the breach of fiduciary obligation?
    - Basic causation test – the calculation of profits is essentially an exercise in causation.
- General idea: Some of the business opportunity was only existent through a breach of fiduciary duty.
    - However, businesses also require an application of the fiduciaries skill and effort. This should be recognised.
- **Accountability is confined to gains attributable to the breach**. A fiduciary is not accountable for profits irrespective of their source. (*Adlam v Savage*)
    - What was gained by a result of the breach of fiduciary duty?
    - *Chirnside v Fay*: Half the profits of the joint venture belonged to Mr Fay.
    - *Warman v Dwyer*: The agency agreement; staff; accompanying losses of peripheral businesses associated with assembly; business opportunity.

- What was gained, by not resulting from a breach of fiduciary duty?
    - The fiduciary may make profits unrelated to their fiduciary duties, so we can't say all existing profits are attributable to the breach.
    - *Warman v Dwyer*: Necessary to distinguish between the loss of agency and Bonfiglioli's own product goodwill. So Dwyer's business was built on the beneficiary's agency, plus the property that Bonfiglioli itself owned.
- This goes into the mix of where to draw the line. The more gained by the breach, the longer time period it is deemed that the profits were caused by the breach.
    - Aspects that go into the mix:
        - Agency relationship
        - Persuasive of employees to leave.
        - Entitlement to assemble products locally.
        - Associated distributorship.
        - Goodwill associated with *Warman's* business.

- Key question: **What portion of the defendant's profits are attributable to the breach.**

    - *Warman*: Profits derived from misappropriation of business and goodwill limited to two years net profits. After two years, none of the profits were caused by the breach.
        - Courts have to have a cut off point; the business has been set up, it's running, and eventually it will need to be allowed to stand alone, or commercial activity will be discouraged.
    - *Chirnside*: Defendant was entitled to retain a half share of net profits from the development, because under the joint venture these were legitimately his. The other half represented unauthorised gains.

<u>3. Allowance for skill, effort, and enterprise</u>

- "There is **room for the Court to exercise its discretion to allow the fiduciary some allowance for effort, skill, and enterprise in making those profits,** if it would be unjust not to do so. All the relevant circumstances must be taken into account. The more reprehensible the fiduciary's conduct, the less inclined the Court may be to make any allowances. The essence of the exercise is to define fairly the profit for which the fiduciary is required to account" *Chirnside*.
- The profits were made because of a breach of fiduciary duty, but there should nevertheless be a payment retained as an allowance to the fiduciary/trustee, because they have expended some kind of skill, effort, or enterprise.
    - The Court needs to adequately and fairly define the profit for which the fiduciary is required to account. The fiduciary's conduct was an act of skill, effort, or enterprise, and if you allow the principle beneficiary to take that value, then that would be an unjust enrichment.
        - Unjust not to make allowance for those activities.
        - Profits are being apportioned between the parties, but there is also argument to make that the efforts the fiduciary put in should be recognised.
    - 'The fiduciary must not be robbed.

- Onus is on the defendant to establish an allowance should be made.
    - *Boardman v Phipps*: Allowances for fiduciary's own efforts could be made if it was not unjust to do so.
    - *Warman v Dwyer*: Fact specific inquiry. Taken to an extreme, no allowance would qualify as a windfall for the plaintiff.
    - *Chirnside v Fay*: Leading NZ authority on availability of allowances.
        - Tipping J: "The essence of the exercise is to define fairly the profit for which the fiduciary is required to account."
        - Majority thinks they should calculate the effort and work expended by Chirnside. How many hours has he worked, and what should he be paid?

The Courts are not dividing up the profits, nor saying that they weren't caused by a breach of fiduciary duty (because they were). Instead they are saying the trustee has done some kind of work, and they should be rewarded for that.

<u>**Test for Breach of Trust**</u>

- "Where a breach of duty by a trustee has directly caused loss or damage to the trust property… **the relief sought by the beneficiary is usually… of a restitutionary kind.** The trustee is asked to restore the trust estate, either in specie or by value. The policy of the law in these circumstances is generally to hold the trustee responsible if, but for the breach, the loss

or damage would not have occurred… **Questions of foreseeability and remoteness do not come into it**." – Tipping J *BNZ v NZ Guardian Trust*.

- No remoteness or foreseeability questions.
- The loss must still be caused by the breach of the trust.
- A simple 'but for' test for causation: The trustee is responsible, if but for their actions, the loss would not have occurred.
    - 1. Is there a breach?
    - 2. Is so, is there some kind of loss that would not have occurred but for the breach?

BNZ v NZ Guardian Trust Co Ltd [1999]

Facts

- NZ Guardian Trust Co Ltd (Guardian) was trustee under a debenture deed, securing advances to a property investment company, Comsec, by various banks, including Bank of New Zealand (BNZ) and another bank, National Australia Bank (NAB).
- Obligations under the trust included that the trustee has to exercise reasonable diligence to figure out whether a particular condition on which Comsec could do with the money had been breached.
    - Guardian failed in its duty under the deed **to use reasonable diligence to detect breaches of the deed made by Comsec** by not detecting from the July 1987 accounts that Comsex had made advances to its subsidiaries.
- Comsec, after a fall in the property market, went into receivership. The banks eventually recovered 14% of their advances.
- BNZ (acquired assets of NAB and suing for NAB) alleged Guardian was negligent in carrying out its duties as trustee by failing to detect Comsec's breach in July 1987.
    - BNZ are claiming but for the breach of trust by Guardian (ie if they had complied with their obligations), the NAB would have been informed of the breach, could have got out of the loan agreement, and exited the venture earlier, receiving all of their money back (as opposed to only 14%).

Procedural History: High Court

- Guardian was negligent in not detecting the non-charging advances but was not liable for NAB's loss, because the substantial cause of Comsec's failure was not the non-charging advances, but external economic factors.
- NAB's lack of chance to exit the facility was an opportunity for, but did not directly create, the loss.
- BNZ appealed.

Held

- Guardian breached its trust obligation to BNZ and NAB.
- NAB has suffered a loss that would not have occurred but for that breach. Therefore, Guardian has to pay them back, even though this loss wasn't foreseeable/caused by Guardian's particular breach of duty.
    - Guardian cannot argue the loss is too remote, because that is not a part of the test in equity.
- The CA holds that it doesn't work like that. Causation in relation to a particular duty of skill and care found in a trust deed **should not** be the same as in the case of losses from the trust estate or breaches of the fiduciary duty.

    - The loss must not only have been caused by the breach, but the loss must be a reasonably foreseeable result of the breach of that particular duty.
- Applying the **but for and the reasonable foreseeability test**: The loss was caused by the share market crash, and the fall in the market – not by Guardian's failure to detect and report the illegitimate loans to subsidiaries. BNZ is trying to seize on a coincidence.
    - Was the loss foreseeable? No. The loss was caused by market downturn.
- Appeal dismissed.

When does the reasonable foreseeability test apply?

- The unsecured loans that caused the breach were paid back, so there was no loss to the trust estate. If they hadn't been paid back, then there would have been a loss, and we would only have to apply 'but for' causation.
- But there is a rule where there are particular duties that look like **skill and care, and in these cases, we use reasonable foreseeability tests**.
- In a situation where a trustee is required to use some sort of reasonable skill and care (eg: a duty to undertake due diligence) they will only be liable if the loss is 'but for' and reasonably foreseeable consequence.
- It does not apply:
    - To a breach of fiduciary duty.
    - Where there is a loss caused to the trust estate.
    - To a situation where the breach is of an absolute duty (eg: conflict of interest). It must be a situation where the trustee is required to use some sort of reasonable skill and care.

AIB v Mark Redler [2014]

Facts

- The claimant bank AIB agreed to loan Sondhi £3.3m pounds, secured by a mortgage over Sondhi's property.
- The property was already subject to two mortgages to Barclays, and it was a condition of the loan that some of the 3.3m be used to pay off Barclay's mortgages so that AIB would have the priority claim.
- Redler, the defendant, was the solicitor for Sondhi, and failed to notice that one of the mortgages, securing £270k, had not been paid off before the rest of the money was advanced to Sondhi (breach of trust).
- Thus Barclay's retained a higher priority mortgage for £270k, and AIB subsequently gained a second mortgage.
- The security was enforced after the property market had fallen, and the property sold for around 1.2m. After Barclays had taken their £270k, AIB received only £870k.

AIB's Claim

- Redler paid out the 3.3m in breach of trust: the money was a trust fund in the custody of the trustee, and only to be paid out to Sodhi if a first mortgage was secured.
- At the point that Redler paid out the 3.3m, it was immediately required to reconstitute the trust fund.
    - This is done by 'falsifying' the 3.3m payment, we say it was not trust property, but Redlers' own money.

- Thus Redler's misapplication of trust property is treated as not having occurred, so that the accounts must show the 3.3m trust fund still in place, and Redler must ensure that the funds are put back.
- There is academic support for this approach.

Held

- This is a case for 'but for' causation.
- The key idea is that only the losses that are caused by the breach of trust are recoverable.
    - "It would not in my opinion be right to impose or maintain a rule that gives redress to a beneficiary for loss which would have been suffered if the trustee had property performed its duties… Where there has been a breach of duty, the basic purpose of any remedy will be… to put the beneficiary in the same position as he would have been in but for the breach may involve restoring the value of something lost by the breach or making good financial damage caused by the breach. But a monetary award which reflected neither loss caused nor profit gained by the wrongdoer would be penal" – Lord Toulson.
- 'The purpose of a restitution order is to replace a loss to the trust fund which the trustee has brought about. To say that there has been a loss to the trust fund in the present case by £2.5m by reason of the solicitor's conduct, when most of that sum would have been lost if the solicitors had applied the trust fund in the way that the bank had instructed them to do, is to adopt an artificial and unrealistic view of the facts'.

Liability of Third Parties

Nature of Third Party Liability

- A third party stranger must account for losses caused by a breach of trust as a trustee would, but not as a constructive trustee over any particular 'trust property': this is **not a proprietary claim**. They are liable to account personally as if they were a trustee: a **personal claim**.
  - o Someone who has dishonestly assisted a breach of trust 'is traditionally described as a "constructive trustee" and is said to be "liable to account as a constructive trustee". But in fact, he is not a trustee at all.
  - o Third parties are personally accountable in equity, just as a trustee is personally liable.
  - o "He is not in fact a trustee at all, even though he may be liable to account as if he were… there is no real trust and usually no chance of a proprietary remedy." – Lord Millet *Dubai Aluminium Ltd v Salaam*.

When are they liable?

- 'That responsibility may no doubt be extended in equity to others who are not properly trustees, if they are found either making themselves **trustees de son tort**, or actually participating in any fraudulent conduct of the trustee to the injury of the cestui que trust.' *Barnes v Abby*
- The third party will be liable to account for losses if they take on the responsibilities of the trustee, act as if they were a trustee, and cause a loss.
  - o Essentially when people start controlling the trust property.
- Strangers aren't made to be constructive trustees unless they:
  - o 1. Knowingly receive trust property OR
  - o 2. Dishonestly assist in the breach of trust.

1. 'Knowing Receipt' of the trust fund

- It's not a proprietary claim. The claim is that you have had the trust property, you lost it, and now you are liable for those loses.

- Factors:
  1. Breach of trust/fiduciary duty.
  2. Receipt of trust property/traceable to the third party (they have to receive the property).
  3. Knowledge of the breach of trust/fiduciary duty.
     - ▪ Have to receive the property with knowledge of the breach of trust.
     - ▪ The recipient's state of knowledge should be such to make it unconscionable for him to retain the benefit of the receipt.

- Receipt 'available only where the defendant received or applied the money in breach of trust for his own use and benefit' (*Twinsectra v Yardley*)
  - o No 'receipt' for these purposes if the recipient is not holding the property beneficially – ie if they are holding it for another as their agent.
  - o Issue for banks: If they receive trust money in the bank account, does this make them liable for knowing receipt? **Only if they are taking that money beneficially** (eg: If

the money is being used to pay off a debt, or bring an account out of overdraft, then the bank is receiving the benefit of the money).

- Recipient is not an innocent volunteer, but a constructive trustee. Therefore they must reconstitute the trust fund.
    - If they're still holding the property, there is a proprietary claim.
    - Fund/property may be 'traceable proceeds'.
- Controversy about the standard of knowledge required.

<u>What standard of Knowledge is Required?</u>

1. Actual knowledge.
2. Knowledge which is obtainable but for shutting one's eyes to the obvious.
    - You knew this was a breach of trust, but you deliberately chose to ignore the obvious.
3. Knowledge which is obtainable but for wilfully and recklessly failing to make such inquiries as an honest and reasonable person would make. F
    - Failing to make inquiries as an honest person would.
    - If you had made these inquiries, you would have had actual knowledge of the breach of trust.

These first three categories are well accepted as constituting sufficient knowledge.

4. Knowledge of circumstances which would indicate the facts to an honest and reasonable person.
    - The defendant knows of circumstances that would add up to the situation being a breach of trust, but is careless in seeking out the trust.
5. Knowledge obtained from inquiries which the honest and reasonable person would feel obliged to make, being put on inquiry as a result of his or her knowledge of suspicious circumstances.
    - You should have known, or there were circumstances that should have aroused your suspicions. An honest and reasonable person would have felt compelled to make inquiries.

In New Zealand, all categories are sufficient knowledge for liability (*Westpac Banking v Savin*). If you fall into any of these categories, that is sufficient.

- Idea is that you should be able to catch people who have come into contact with the trust property. We want to be able to say that they have knowledge of the breach.
- 'Given what you knew, ought you to have been suspicious?' Even though you didn't actually know, you will be regarded by the court as knowing enough to be personally liable to the beneficiary.

<u>*Marr v Parkin* [2015]</u>

- 'The most difficult challenge with the law of knowing receipt is establishing the degree of knowledge or notice required before the recipient of the property in question will be held accountable. Part of this challenge arises from the different approaches that have been taken to assessing the degree of knowledge or notice required to establish liability.'
    - One school of thought looks at any of the 5 categories as sufficient.
    - Another focuses on whether the conscience of the recipient is affected.
- Ultimately, it's determined on the factual nexus.
- Largely a reasonable person test, but can incorporate some subjective elements.

2. Dishonest (Knowing) Assistance with Breach of Trust

- The third party was not the recipient of the trust property, but has done something to assist someone who is in breach of their trust obligations.
    1. Trust or fiduciary duty that is breached by the trustee/fiduciary [need not be dishonest].
        - Did the third party do something which aided the breach of trust?
    2. Assistance by third party in the breach
        - Did the third party facilitate/make the breach possible to occur?
    3. Dishonesty on the part of the third party given their knowledge of the relevant facts. does it mean to be dishonest?
        - Does there have to be a dishonest state of mind, or only a dishonest action?

Is Dishonesty subjective or objective?

- The test for dishonesty is contested.
- In New Zealand, the approach is akin to Lord Millet's in *Twinsectra v Yardley*.
    - Objective test. Dishonesty means not acting as an honesty person would have in the circumstances given their knowledge.
    - Ordinary standards of honest people.
- There is some argument against this approach, regarding dishonesty being a state of mind, therefore requiring a subjective test.

Westpac New Zealand Ltd v Map & Associates Ltd [2011]

- Leading NZ case which affirms Lord Millet's test.
- In *Barlow Clowes*, Lord Hoffman summarised the major difference between *Twinsectra* and *Barlow*. In *Barlow*, their Lordships recognise that:
    - "Although a dishonest state of mind is a subjective mental state, the standard by which the law determines whether it is dishonest is objective. If by ordinary standards a defendant's mental state would be described as dishonest, it is irrelevant that the defendant has different standards and does not appreciate that his conduct, by ordinary standards, would be regarded as dishonest."
- Judges agreed with Lord Millet.

- This test takes the subjective circumstances of the person into account. There is a subjective element as to what X's knowledge of the circumstances were.
    - Subjective speaks to what kind of person the third party was in terms of their abilities/expertise. What knowledge could they be assumed to have?
    - It is a reasonable person in the position of the defendant, incorporating their knowledge and expertise.
    - It doesn't matter that they don't know the usual standards of honesty. Did they act as an honest person would have in the circumstances?

- 'Although a dishonest state of mind is a subjective mental state, the standard by which the law determines whether it is dishonest is objective. If by ordinary standards a defendant's mental state would be described as dishonest, it is irrelevant that the defendant has different standards and does not appreciate that his conduct, by ordinary standards, would be regarded as dishonest.'

- ‘The key ingredient in the cause of action for dishonest assistance is the need for a **dishonest state of mind** on the part of the person who assists in the breach of trust. We agree... that such a state of mind may consist in **actual knowledge that the transaction is one in which the assistor cannot honestly participate**. But it may also consist in what we would describe as **a sufficiently strong suspicion of a breach of trust**, coupled with a deliberate decision not to make inquiry lest the inquiry result in actual knowledge… This state of mind, which equity equates with actual knowledge, is usually referred to as wilful blindness.’

Succession

- Under English law, the traditional concept is that of 'testamentary freedom'. The testator/trix can do whatever they want with their property when they die. 5

Upon Death

- If there is a will, there will be an executor appointed under that will. The executor, immediately upon the passing of the deceased, steps into their shoes.
- They are responsible for:
  - The funeral arrangements.
  - Probate: If the estate is worth more than $15k, the executor must apply to the High Court for probate over the estate, essentially validates their management of it.
  - Collect debts owed to the deceased/pay debts owed by the deceased.
  - After this is done, the executor becomes the trustee of the sum remaining on behalf of those designated under the will.
- If there is no will, the Administration Act 1969 comes in.
  - A close friend/relative will apply to the court for letters of administration.
  - They do the same stuff. '

Administration Act 1969

- Comes into effect if the deceased is intestate, or part of the estate is left in intestacy.

Section 2 – Interpretation

- De facto relationship: Meaning taken from the Property (Relationships) Act 1976.
  - No romantic/intimate relationship is required.
- Personal Chattels means anything apart from land, tools of the trade, or money.

Section 77 – Succession to real and personal estate on intestacy

- Outlines to whom and how much of the property is to go where.
- If there is a surviving partner, they get all the personal chattels, and $155,000. The rest is split one third to the surviving partner, and the remaining two thirds on trust for the descendants.
- If there are no children, but some parents survive, the property is split, after the chattels, 2/3rds for the partner, 1/3rd for the parents.
- After about 6 degrees of separation, the property is deemed to be held by the Crown, with the Crown having discretion to allocate property as it sees fit.
- The property will be held on statutory trust either by the administrator, or the Crown.

Section 77B – Restrictions on succession on intestacy by certain de facto partners

- If the de facto relationship is longer than 3 years, the de facto partner is treated as a spouse.
- If not, they have no claim unless:
  - There is a child of the de facto relationship.
  - Or the partner made a substantial contribution to the relationship, and the court would find it constitutes a serious injustice to the partner to leave them out.

Section 77C – Multiple surviving partners

- The $155k and all the personal chattels are split equally between the partners.

Section 78 – Statutory trusts in favour of issue and other classes of relatives of intestate

- Per capita and per stirpes.

The Wills Act 2007

- Purpose is to make it as simply as possible for a testator's wishes to be put into effect.

De Facto Relationships

- As defined in the Interpretation Act
    - A relationship akin to marriage is required.

Section 9 – Persons who may make, change, revoke, and revive wills

- You must be over 18 or
- Be under 18 if they're married/de facto/ cu, or have been in any of those.

Section 11 – Requirements for validity of wills

1. Writing (document is defined incredibly broadly).
2. Signed and witnessed in accordance to ss (3) and (4).
3. Will maker must
    a. Sign the document or
    b. Direct another to sign on his behalf.
4. At least 2 witnesses must
    a. Be together in the will maker's presence
    b. Each sign the document in the will maker's presence.

- The witnesses don't have to know that you're signing your will, but they have to be there, and witness the signing.
- The signature can be anywhere on the document.

Re Colling

- In hospital, old man signing his will, one of the nurses went away.
- While she was a away, Mr Colling signed his will.
- The will was held to be invalid, as it was improperly witnessed.
- However s 14 often dismisses issues with formalities such as this.

Section 13 – Witnesses affected by dispositions made to them

- Witnesses cannot receive anything under the will which they witness.
- Purpose it to prevent witnesses 'twisting the arm' of the deceased.
- Wills which do bequeath to witnesses are often not void, but the gift to the witness will be made void.
- Gifts to spouses of the witnesses are also void.
- This rule has resulted in some unjust results, there are ways around it.
    - S 14
    - If you can prove the will maker knew and approved of the disposition, and made it voluntarily, it will be valid (s 13(2)(d)).

    - Or if there are 2 other witnesses, who validly witnessed the will.

Section 14 – High Court may declare will valid

- The High Court has the power to validate wills which do not follow the formalities.
- This section has almost wiped out the impact of the formalities.
- The s 14 test is subjective, depends on the particular case.

Re Brundall (deceased) [2011]

- One of the earlier cases. Woman wanted to change a valid will, the lawyer received instructions and drafted the will in accordance. There was agreement about what the document was meant to be, but she died before it could be executed.
- In the circumstances, there was no doubt the solicitor has fairly represented the testator's wishes.
- No one was disadvantaged by accepting the later document, so it was accepted as valid and admitted to probate.
- Proof of intention is the critical element.

Section 15 – Changes

- A will may be changed, but only by one of the following means:
  (a) If the change is
    - Written on the will; and
    - Signed and witnessed in accordance with section 11(3) and (4); or
  (b) The change is described in a note
    - Written on the will; and
    - Signed and witnessed as described in section 11(3) and (4); or
  (c) The change is the obliteration of words in the will in such a way as to prevent their effect being apparent; or
  (d) The change is declared valid under s 14; or
  (e) The change is done under s 34(2).
- If you make lots of wills, the last valid will is the one that counts.
- A will is only effective after death.

Section 18 – Effect on will of will-maker marrying or entering into civil union

- This will typically invalidate the will.
- Does not apply if
    - The will explicitly says the will was made in contemplation of this happening, or it is clear from the circumstances and
    - The marriage/civil union was a contemplated one.

Section 19 – Effect on will of will-maker's marriage or civil union ending

- Unless there is some provision saying 'even in a divorce, this provision stands', then the divorce terminates the interest of that person in the estate.

Property (Relationships) Act 1976

- 'Relationship property' is defined as anything used in the relationship. The only way for something not to be deemed relationship property is for it to have been kept completely isolated.

Section 61 – Surviving spouse of partner may choose option

Option A

- Surviving spouse elects to apply for a division of relationship property under the Act.
    - Couple's assets are divided in much the same way as on separation.
    - Proceeds as if it was a divorce.
    - But in consequence, you are deemed as having predeceased the partner, and am no longer a part of the succession chain.
        - Exclude yourself from the succession rules.
        - Surviving spouse forfeits any inheritance available under the deceased's will, or the intestacy wills, and the estate is distributed as if the surviving spouse had died before the deceased.

Option B

- Surviving partner elects not to proceed under the Act, but to retain his or her own assets, take non-probate assets by survivorship, and inherit such provision as is available under the deceased spouse's will or the intestacy rules.
    - Accept the death and follow the normal rules.

Section 62 – Time limit on making the choice

- The choice between the two options is a formal process, it must be made by written notice within 6 months of death, or the grant of administration, whichever is later.
- If election is not made, the spouse will be deemed to have elected option B.
- If option A is chosen, it is dealt with as a priority.

Section 81 – Presumption that the property of the deceased spouse or partner is relationship property

- All property that was owned by the deceased spouse or partner as his or her death is presumed, in the absence of evidence to the contrary, to be relationship property.
- A person who asserts that any property to which the presumption in ss(1) applies is not relationship property has the burden of proving that assertion.

- People sometimes presume a joint tenancy is a way to skirt succession rules, the survivor takes the property under joint tenancy, therefore it does not come under the estate.
- But for the PRA, the survivorship doesn't operate automatically, because the house will be presumed to be relationship property.

Section 85 – De facto relationships of a short time

- If the relationship is less than 3 years, the court cannot make an order for the division of property unless:
    - The court is satisfied there is a child of the relationship; or
    - The surviving partner has made a substantial contribution to that relationship; and
    - The court is satisfied that failure to make the order would result in serious injustice.

How can the PRA be avoided?

- S 21: Spouses or partners may formally contract out of the PRA, but that's so hinged with conditions that it's not guaranteed.
- S 57: Regardless of the PRA, you can always make a claim under the Family Protection Act, or Law Reform Testamentary Promises Act 1949.

Process

1. Is there a surviving partner?
    a. If yes, deal with PRA first.
    b. If no, go to children, parents etc, but don't deal with the RPA.
2. Surviving partner must choose between A and B.
3. Is there a will?
    a. If yes, proceed under the Wills Act
    b. If no, proceed under the Administration Act.

Family Protection Act 1955

Adoption Act 1955

- An adopted child is a child for the purposes of succession law.

Status of Children Act 1969

- Until the 1st of January 1970, there were legitimate and illegitimate children.
- Now NZ does not tolerate any distinction to be made between children born after 1970.

The Act

- Concern is for maintenance and support. Maintenance is a practical consideration, but support is moral.

Section 3 – Persons entitled to claim under Act

- A spouse or civil union partner.
- A de facto partner (definition under the PRA)
- The children
- The grandchildren
- Stepchildren
- Parents
    - The possibility of parents and grandchildren to make claims are hedged by conditions.
    - Parents: A claim can only be maintained if the parent was being wholly or partly maintained, or was entitled to such maintenance, by the deceased, immediately before his or her death.
    - Or: If the partner, and children of the deceased are all dead.
    - Grandchildren: Provisions made for the parents of the grandchildren must be taken into account.

Section 4: Claims against the estate of deceased person for maintenance

- Will or not is irrelevant.
- Criteria are whether the deceased has left sufficient provision for the proper maintenance and support of the person making the claim.
- Any claim must be made within 12 months.
- One claim opens all provisions to scrutiny (eg if one child claims, the provisions made to the other 2 children are examined.

Williams v Aucutt [2000]

Facts

- Mrs Henderson died leaving an estate worth $1m. The will distributed 95% of her property to her daughter Christine, Susan got the remainder.
    - The distribution was carefully considered.
    - Christine had low worth, and did not have particularly good family circumstances.
    - Susan was worth at least $1m, and had very favourable circumstances.
    - The testator explained the division in detail.
- She chose items of significant sentimental value to go to Susan, Christine got assets to provide for herself.
- Both daughters were dutiful and caring for their mother. Susan makes a claim under the Family Protection Act because she believes the moral duty owed by her mother has been breached.
    - She claims one third of the property.

Procedural History

- Of the view that there is a breach of moral duty in this case. Both daughters brought great joy to their mother. It is inappropriate only a small number of assets are the final reward to Susan.
- The testator was in breach of her moral duty to recognise Susan's contributions.
- Judge ordered that Susan get 25% of the estate.

Held

Richardson J

- The Aucutt Test
    - The test is for whether adequate provision has been made for the proper maintenance and support of the claimant.
        - Support is an additional and wider term than maintenance.
        - Support is determined based on the factual nexus.
        - It means providing comfort.
    - The testator did not fail to recognise Susan, the question is whether the amount given to her constituted proper support.
    - The court found that 5% was too little.
        - Deceased probably didn't know the value of her estate.
        - Daughters could not be distinguished in terms of dutifulness. They were very different in their manner, but both were dutiful.
- The High Court's award was excessive.
- Awarded 10% of the estate.
- Tried to balance testamentary freedom with rights under the act.

Blanchard J

- The statute does not give the court the power to rewrite the will.
- It is for a claimant to establish why the amount given to them is inadequate.
- It is certainly not for the court to be generous with distributing the testator's property in the interest of repairing a moral wrong.
    - Before death, the testator had the right to do whatever he wants with his property, it should be similar after death.
- Looks for whether a need for support is made out in the circumstances.
- 10% is about the most a child can expect in a support claim.

Reasoning

- Four principles in assessing the needs of the applicant:
    1. The merits of the claim having regard to the applicant's circumstances as at the date and death of the testator.
    2. Relations between the testator and the applicant in the past.
    3. Extent of his estate.
    4. Strength of other claims.

Law Reform (Testamentary Promises) Act 1949

- Purpose of the act is to enforce unfulfilled promises to reward services or work performed for the deceased during his or her lifetime.

Section 3 – Definition of what the act is for

- Has to have been work done, and a promise (explicit or implied) that the work would be rewarded.

- The act is quasi-contractual in nature, and it could be seen as a means of enforcing a debt rather than a limit on testamentary freedom.
- Similar to the FPA in that the court has a very wide discretion.
- Overrides the formalities required in the PLA 2007.
- Not subject to the Homicide Act, someone may get their debt even if they killed the testator.

Re Welch [1990]

Facts

- Claimant is the step son of the deceased.
- His mother dies, leaving a will. Very shortly afterwards, the step-father dies intestate.
- In the absence of the will, the step father left 8 brothers and sisters. They stand to gain the $310k estate.
- Stewart (claimant) had a close relationship with both his parents, who had no other children. Mr Welch treated him as his son, just as Stewart treated Welch as his father.

- Welch indicated to Stewart and others that he had a will/intended to make one whereby Stewart would ultimately inherit at least most of the property of Mr and Mrs Welch.
- Stewart initiated 2 proceedings:
    - 1. Application made by him as executor of his mother's estate, seeking an order under the RPA.
    - 2. Application under the LR(TP)A that there has been a failure to recognise what he is promised from his stepfather's estate personally.

Procedural History

High Court – Gave him half the deceased assets.

CA – Reduced the award to half of the assets for his mother, and 20K extra.

PC appeal dismissed.

Held

- The focus in this case was on the promise to give the stepson property, and whether that was a promise to reward him for work he had done for his stepfather.
- Privy Council said no, it is reasonable to expect a son to act in the ordinary course of familial duties for his stepfather. Love and affection is not work.
- There is also a bar in the TPA for double awards to be made.
- 'There should be no injustice to other meritorious claims'. The court doesn't want to prejudice the claims of the brothers and sisters.
- There would be no claim under the Family Protection Act 1955, stepchildren have to have been maintained by the deceased immediately before the deceased death, this was not the case.

The Test

1. Was there a promise?
2. If there was, has there been a breach?
3. Is there a provision for the person under the will/ is the deceased intestate?
    a. This necessitates a claim under the act.