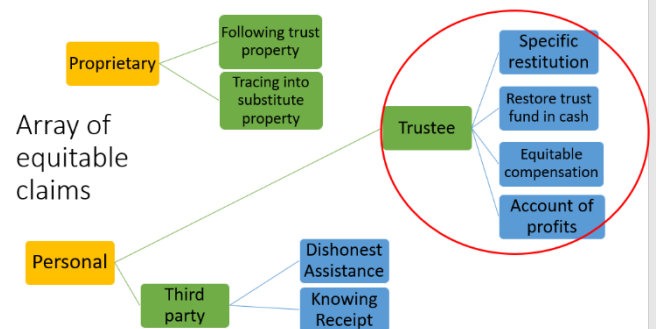


Personal claims against trustees (and fiduciaries)

- Breach of trust – can make proprietary claims on trust property
- Substitutive or tracing claims – can track where trust property ended up but cannot claim it back as now belongs to a bona fide purchaser of value without notice of the trust. Can trace for what was exchanged for trust property and claim for proceeds against trustees.
- Personal claims against 3rd parties who dishonestly assisted in breach of trust or who knowingly receive trust property



Remedies for Breach of trust

- **Specific restitution:** put trust property back if possible
- **Substitutive compensation:** pay in money to replace trust property
- **Equitable compensation:** money remedy to restore loss – back in situation if breach of trust had not occurred
- **Account of profits:** If the breach results in a profit, the beneficiary can claim this
- In context of fiduciaries, can have gain-based remedies.

Armitage v Nurse

- In what ways can a settlor in drafting the trust deed exclude personal liability
- There are certain irreducible core of obligations
- Could exclude mere or ordinary negligence – trustee is not personally liable for breach of trust except in case of wilful default or fraud
- Court: can exclude grossly negligent actions for personal liability
- If Trust Bill becomes law – s 37: cannot exclude liability for gross negligence
- Section 40 if adviser on creation of a trust, need to tell the settlor what an exclusion clause is and the extent of the exclusion clause. If have not done it, the exclusion of liability will not have an effect on the trustees.

Equitable compensation

- *Day v Mead* per Cooke P:
- Courts of equity must always have the power to compensate by awarding damages
- The main difference between an award of damages at common law and of compensation in equity lies in the way in which the appropriate sum is estimated. Equitable compensation is not fettered by the requirements of foresight and remoteness which control awards of damages at law.

Equitable compensation different from common law?

- *Re Dawson (dec'd)* [1966] 2 N.S.W.R. 21
- the inquiry in each instance would appear to be whether the loss would have happened if there had been no breach...
- Shall equity have different rules of causation than in common law – tort and contract? This would mean equitable claims an advantage
- Common law applies two basic concepts of causation
 - ‘Factual causation’ – was the breach of duty a ‘but for’ cause of the loss
 - ‘Remoteness’ – was the loss suffered reasonably foreseeable (tort) or the ordinary or stipulated (contract) consequence of the breach of duty
- So does equity have the same requirements?: ie can a defendant avoid liability for a loss if they can say
 - (i) that it would have happened even if they had not breached their duty, or
 - (ii) that it was not a reasonably foreseeable consequence of the breach of duty?
- Still controversial, but generally accepted that the three categories of breach of trust have different rules:
- For misapplication of trust property, and breach of fiduciary duty, there must be ‘factual causation’ but rules of remoteness do not apply
- For other breaches of duty, which are akin to common law breaches of duty, both factual causation and rules of remoteness of loss apply
- Have equitable compensation recognised by courts of equity giving effect to equitable remedies, but different from common law damages.
- Equitable compensation does not look to remoteness or foreseeability of loss
- Common law losses are limited by foreseeability i.e. damage was the foreseeable result of a breach or wrong.

BNZ v NZ Guardian Trust Co Ltd

- Trust estate was charged (security interests) over assets of Comsec, and interests/rights/powers in relation to these security interests
- The loan was not fully repaid, due to a fall in the value of the assets of Comsec – market conditions due to sharemarket crash
- The breach of trust was not taking reasonable care to detect unsecured advances from Comsec to subsidiaries in breach of debenture deed
- Claimant’s argument: but for this BOT, NAB’s loss would have been avoided: NAB would have used Comsec’s breach of the debenture conditions to exit the scheme – getting all its loans back
- HC says factual causation satisfied (NAB would have exited and not had any loss, but for breach) but loss too remote from duty
- CA doubts factual causation, but agrees that the loss is too remote from the breach of duty
- CA says that causation in relation to duties of skill and care found in a trust deed should not be the same as in the case of **misapplication of the trust estate or breaches of fiduciary duty**
- The loss must not only be ‘but for’ caused by the breach, but the loss must be a reasonably foreseeable result of the breach of that particular duty

BNZ v NZ Guardian Trust

Facts:

- Banks loaned money to Comsec which speculated on property markets, with requirements on how Comsec used money and the security needed
- NZ Guardian Trust was the trustee of the deal who ensures Comsec meets its loan from the banks. Trust property were the obligations Comsec owed to all the banks under the transaction. Comsec becomes insolvent.
- Guardian had a duty to take reasonable care in auditing Comsec and ensuring Comsec only lent money if it received a security interest in return. Guardian failed to monitor what has occurred.
- NAB: sued NZ Guardian Trust for breach of trust obligations in loan debenture deed i.e. trust deed as failed to exercise due diligence and detect unsecured advances from Comsec to its subsidiaries in breach of loan agreement
- The breach must cause the loss. If the loss would have occurred even if the trust obligation was not breached, then the loss was not caused by the breach. i.e. must be a 'but for' cause of the loss.
- NAB: (but-for causation) if Guardian had fulfilled its duty and detected the breach of agreement, NAB would have exited the deal and been repaid all its money rather than only 14% of the loan
- Real cause of the bank's losses was a financial collapse which was unconnected with the breach
- NAB: suffered a loss within the scope of Guardian's duty and kind of loss the duty is supposed to protect against and therefore breach caused our loss i.e. if money given to subsidiaries disappeared, it would have caused loss within the scope of monitoring advances to subsidiaries but did not occur.
- CA: Trustee duties were directed at preserving the value of the securities and shareholder's recourse to them during the term of the loan i.e. monitoring duties

Result:

- HC: NAB would have exited and hence been repaid and not have suffered any loss. However, claim does not succeed as loss too remote from duty.
- CA: trustees' breach is a but for cause of the loss i.e. the loss would not have occurred if trustees did not breach their obligations, the connection between the loss and the breach of duty was too remote, despite doubting HC on 'but for' causation.
- Both HC and CA: in an equitable cause of action i.e. breach of trust took into account remoteness in terms of assessing loss.
- CA: lack of diligence means beneficiary may not be able to take steps it would have taken to and loss was suffered as a result. The purpose of the duty was "to notify stockholders of any breach to protect them from losses caused by that breach."
- NAB as beneficiary accepted that it did not suffer any loss from Comsec's unauthorised use of money.

Law:

- Relationship itself does not dictate how to determine issues of remoteness
- Always apply 'but for' causation test i.e. breach has to be a cause of the loss. If loss would have happened despite breach, then not a but for cause of the loss.
- Must consider the duty or obligation breached by the trustee or fiduciary.

- **Custodial stewardship duty** – preserve and protect assets of trust unless permitted to do otherwise by terms of the trust i.e. breaches leading to direct loss to trust property
 - Relief sought by beneficiary is normally restitutionary, trustee restores trust estate.
 - Apply ‘but for’ causation
 - Foreseeability or remoteness irrelevant (similar to debt)]
- **Duty of undivided duty** – prohibits the trustee from taking any advantage from his position without the fully informed consent of the beneficiary – fiduciary obligation i.e. breach from infidelity or disloyalty which engages the conscience of the fiduciary
 - Apply ‘but for’ causation
 - Foreseeability or remoteness irrelevant
- **Management stewardship duty** – duty to manage trust property with proper care i.e. breach from a lack of skill or care eg. due diligence
 - Different type of duty. Similar to common law.
 - Foreseeability or remoteness applies to potential losses liable for
 - Scope of the duty did not extend to the loss suffered

Another example of ‘but for’ causation: *AIB v Mark Redler* [2014] UKSC 58

Facts

- The claimant bank AIB agreed to loan Sondhi 3.3m pounds, secured by a mortgage over their (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 Barclays’ mortgages so that AIB would have a first mortgage
- 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

- Redlers 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 Redlers paid out the 3.3m, it was immediately required to reconstitute the trust fund. We do this by ‘falsifying’ the 3.3m payment: we say it was not trust property (belonging to AIB) 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
- Notice that this violates ‘but for’ causation: if the BOT had not occurred, then AIB would have lost 2.1m

AIB v Mark Redler

Background:

- Equity maybe different from common law due to historical origins of remedy
- Equity different with misappropriation of the trust property from applying common law 'but for' causation approach
- Academics: 'but for' causation approach is inappropriate when dealing with misappropriation of the trust property. Have to take an account.

Facts:

- Sondhi owned a house already mortgaged to BB for 1.5 million
- Sondhi wants to borrow from AIB
- AIB wants to become first mortgage holder so pays off 1.5 million owed to BB.
- AIB as beneficiary passes 3.3 million to Redler as solicitors and trustees to pay off BB and remove their security interest over house before paying Sondhi
- Redler made a mistake where Sondhis had 2 debit accounts with BB
- Redler only pays BB 1.2 million but does not pay 300,000 in other account. BB retained its first security interest over mortgage and without BB discharging its security interest it then gives the rest of the money to Sondhi.
- Upon realising the mistake, BB allows AIB to take the second security charge
- Property worth 4.25 million. House secured borrowings of 3.3 million + 300,000
- Redler breached trust as required to only hand property it held on bare trust to the borrower once it has had secured what the lender wanted by way of security. Redler did not secure what AIB wanted by way of security before it paid money to Sondhis as AIB did not receive the first mortgage but a second mortgage.
- Redler had paid 2.1 million to the Sondhis in breach of trust
- Sondhis later renege on loans. The house is later sold for 1.2 million as crash in property market and inaccurate valuation – BB receives 300,000 first as first mortgage holder followed by AIB who receives 900,000.

Claims:

- AIB: breach of trust – claimed 2.4 million (out of 3.3 million as received 900,000)
- Redler: applying 'but for causation'. Comparing reality of the loss caused from the breach i.e. receiving 900,000 back
- What would have occurred if there had been no breach i.e. AIB would have had first mortgage and Redler paid 1.5 million to BB and 1.8 million to Sondhis.
- Difference: amount AIB would receive if held a first charge worth 1.2 million instead of 900,000.
- Basis for AIB receiving more beyond 'but for' causation: Target was wrong when it applied a 'but for' causation approach to misappropriation of trust property and for breaches of the custodial obligation as it relates to taking an account. Should rectify account such that trust property 3.3 million should remain in Redler's hands.
- Trustees have to account for stewardship of trust property, hold onto it as custodians, give an account by falsifying unauthorised payments out
- Trustees can only apply trust property for certain purposes. If used for purposes not permitted under the trust then the payments are not said have existed and the amount must show that the money was there.
- Foreseeability not relevant as money should be in the account (like a debt)

Result:

- Court rejected AIB's argument and scholarship that trusts are a special kind of equitable device where 'but for' causation is not applicable and instead, apply a

remunerable procedure in the account of what the trustee must pay for misapplication of the trust property.

- Court: applied a 'but for' causation approach – trustees should not be liable for a loss which would have occurred even if they had complied with trustee obligations. Fairer approach and did not want to overturn Target as followed by lower courts
- Historical differences in holding trustees not enough to overturn Target
- Redlier only liable for lesser amount caused by breach

The UKSC's decision

- The key idea is that only the losses that are caused by the breach of trust are recoverable:
- “Where there has been a breach of [a trust] duty, the basic purpose of any remedy will be ... to put the beneficiary in the same position as if the breach had not occurred... . Placing 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 at [62] and [64].
- “The purpose of a restitutionary 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 of £2.5m by reason of the solicitors' 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.” [65].

Premium Real Estate v Stevens

What about breaches of fiduciary duty?

- Plaintiff recovers unless defendant fiduciary can show that the loss would have occurred in any event without any breach on the fiduciary's part
- Foreseeability and remoteness irrelevant
- Fiduciaries only allowed narrow escape route
- *BNZ v NZ Guardian Trust Tipping J* at 685

What is the narrow escape route?

- “I did not cause the loss”. It would have occurred anyway. My breach was not a but for cause of the loss
- Eg in the context of fiduciaries: I did not inform my principal of my conflict of interest or a material fact about the transaction, but they would have gone ahead with the transaction anyway
- *Brickenden v London Loan* [1934] 3 DLR 465 is a Canadian Privy Council decision saying that the breaching fiduciary could not make this argument

Reasons for *Brickenden*

- Equity is special: where there is a breach of fiduciary duty, equity will presume that any loss was caused by the breach. It will not allow evidence presented to deny 'but for' causation.
- This adds to the prophylactic, discouraging of breaches of fiduciary duty. It does so in conjunction with the denial that remoteness principles limit liability for the loss caused
- Remoteness irrelevant when there is a fiduciary breach

- Fiduciaries normally argue loss would have happened even if there was no breach
Eg. fiduciaries who breach duty of loyalty through non-disclosure of information to principal. Fiduciary may argue principal would have undertaken transaction even if they knew about the information i.e. ‘but for’ causation.
- Principal generally has to prove their loss and what they would have done i.e. would not have suffered a loss from transaction if knew about information
- Equity imposes special rule on fiduciaries who cannot challenge principal/claimant’s claim that they would have done something different eg. if they had received the information they would not have engaged in the transaction.
- Relieves the principal from the burden of showing that the loss was caused by the breach
- In NZ, SC: onus shifts onto fiduciary to show that the loss would have occurred regardless of the breach. The courts will assume the principal would have acted differently if they had received information from the fiduciary, however fiduciary can present evidence to prove that the principal would have acted the same even if they had been told the information. Does not apply strict rule.

Retreat from *Brickenden: Premium Real Estate v Stevens*

- [85] It was once the strict rule that when a fiduciary committed a breach of duty by non-disclosure of material facts which the party to whom the duty was owed was entitled to know in connection with the transaction, the fiduciary could not be heard to maintain that the disclosure would not have altered the decision to proceed with the transaction; once the court had determined that the undisclosed facts were material, speculation as to what course the beneficiary, on disclosure, would have taken was not regarded as relevant.
- [85] ... The strict rule could sometimes lead to unfair results and has been modified in this country by an approach which affords the fiduciary a limited opportunity of showing that all or some of the loss would have occurred even if disclosure had been made.

Premium Real Estate v Stevens
<p>Facts:</p> <ul style="list-style-type: none"> • Stevens selling house – thought its worth 3 million, made counter-offer at 2.8 million in earlier negotiations but later unhappily sold it at 2.6 million to Larsen. • PRE was real estate agent and a fiduciary for Stevens who did not disclose information they had about Larsen that he was an investor who purchased and sold houses for a profit. PRE suggested to Stevens that Larsen wanted to live in the house, which was information relevant to Steven’s decision in selling the house to Larsen • Larsen later sells the house for 3.6 million.
<p>Result:</p> <ul style="list-style-type: none"> • SC: breach of fiduciary duty of loyalty and lack of disclosure of info • Applies ‘but for’ causation and modified Brikenden approach • <i>Elias CJ (Minority)</i>: Brikenden concerns whether the principal would have proceeded with the transaction in any case. • Onus on the fiduciary to prove that the principal would have engaged in the transaction regardless. Otherwise equity assumes transaction would not have occurred if there was no breach i.e. information was provided • Difficult for PRE to prove Stevens would have made the same transaction in any event. • ‘But for’ causation of loss made out i.e. Stevens would not have engaged in the transaction if they knew about the information

- Differs from majority – cannot determine loss by reference to an assumed normal transaction which would have occurred.
- Brikenden limited to onus on fiduciary to show the transaction would have occurred anyway. If the fiduciary cannot reverse the onus, the principal must still prove the loss through evidence of what transaction would have actually occurred and that they would have acted differently.
- Elias CJ: in terms of loss, the most likely eventuality is if the principal was given the information they would have sold the house at 2.8 million, which is the highest price they would have sold for. Rejects notion of a normal measure of damages
- *Majority*: reverse onus not merely about whether the principal would have undertaken the same transaction but also affects the measure of loss i.e. what would have and what actually occurred
- Onus on the fiduciary to prove that the principal would have engaged in the transaction regardless. Otherwise equity assumes transaction would not have occurred if there was no breach i.e. information was provided
- If fiduciary cannot establish that, the fiduciary also have the burden to argue against the normal and natural measure of loss i.e. ‘but for’ the breach, the loss caused is not the natural measure of loss.
- The normal and natural measure of loss when a fiduciary breach affects the price a property is sold is the difference between the sale price and market value. Policy dictates that the onus is on the fiduciary to prove the plaintiff’s loss was less.
- Natural measure of loss: actual transaction: 2.6 million
- Unless the fiduciary can prove what the loss would have been but for their breach i.e. house sold at 2.8 million and loss is 200,000, then the court applies the natural measure
- Brikenden – special rule in equity which presumes the principal would have sold at a certain price i.e. market value which defines the loss.
- Fiduciary did not provide enough evidence to displace the normal measure.
- PRE had to return commission and market price – actual price

Commission:

- Both majority and minority agree commission can be returned to principal
- Lower court: double dipping and inconsistent remedy.
- Tipping J: principal paid commission to the fiduciary. If the fiduciary breached the trust, the fiduciary does not deserve it so returns to principal. Not inconsistent remedy as restitution of principal’s property in circumstances where fiduciary cannot keep it
- An account of profits focussing on the gains made and equitable compensation will be inconsistent as compensation for gains to the principal will cancel out losses made.

What is the loss in *Premium Real Estate v Stevens*?

- Ie what do we compare the actual price achieved by the Stevens (\$2.6m) with?
- \$3.3m market price at date of sale given by valuer
- \$2.8m price Stevens had indicated that they were prepared to accept from another prospective purchaser.
- \$3.6m price achieved by Larsen

Elias CJ:

- Compensation for fiduciary duties makes good losses from a breach, otherwise it's a penalty. Compensation must be causally connected with breach
- Brickenden should not be extended to the quantification of loss
- Quantification of loss for the plaintiff to show it was causally linked to the wrong
- Additional benefit the principal may obtain is not properly attributable to breach
- Best evidence of the higher price which principal would have sold was \$2.8 million
- The question is the higher price which would have been realised if disclosure had been made
- Reverse of onus onto the defendant to assert that the loss would have occurred anyway does not affect the needs for the plaintiff to prove loss was caused by the breach. Evidential rule as proof is difficult and meets justice of the case.
- One circumstance for shifting the onus is if there was non-disclosure by a fiduciary of information material to the transaction undertaken by the principal. Once materiality shown, for defendant to show transaction would have been entered nonetheless for a different reason
- Lower courts right did not accept that principals would have entered into the transaction if it had the information.
- Principals lost the opportunity, if in possession of the material information, to obtain a higher price.
- Loss is measured by the lost opportunity to sell at a higher price – the price likely to have been achieved depends critically on evidence of vendor, purchaser attitudes' & the objective indications of the price the market was willing to pay.
- Vendor attitudes untainted by the breach indicated a preparedness to sell at \$2.8 million – highest point of any loss. Supported by hindsight escalation of property prices and later sale price.

Blanchard J:

- Once plaintiff shown a loss from breach which was material, they can recover unless defendant fiduciary, who bears the onus, can show that the loss would have occurred in any event.
- Policy dictates fiduciaries are allowed only a narrow escape route.
- Same approach to quantum of loss. Same policy applies to both, which was designed to deter fiduciary breaches by limiting circumstances in which fiduciaries can escape their liability.
- Artificial/inconsistent with that policy to distinguish between causation and quantum
- Fiduciary must show the normal and natural measure of loss does not apply
- Property = difference between the sale price and market value
- CA in reaching decision principal would have sold at 2.8 million overlooked principal's belief that their property was worth \$3 million. Principals would have reconsidered the situation if had the information that Larsen was a speculator. They likely would have sought valuation advice, extended the sale period and would have likely achieved the current market value of \$3.25 million
- Adopting the CA's \$2.8 million too easily permits the errant fiduciary to find the "narrow escape route" and fiduciary's own mistaken assessment of market value.