Principles of Equity and Trusts Law in Hong Kong

Third Edition

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Preface to the First Edition

This is a student edition of Lawrence Ma's *Equity & Trusts Law in Hong Kong*. The chapters of this book are largely selected from the pages of its parent text and adapted to the needs of a student audience.

There is, in the authors' view, a pressing need for a student text that looks at Equity & Trusts from a Hong Kong perspective. The reasons are the same as those advanced in the preface to the first edition of *Equity & Trusts Law in Hong Kong*. UK textbooks (on which Hong Kong students have relied until now) necessarily deal with the law as it has developed there. The UK has its own legislation in this area that has no parallel in Hong Kong. Further, the CFA has developed the law of equity and trusts in Hong Kong and, thus, the Hong Kong system (although part of the common law world) requires its own special treatment. Then there is the need to consider the impact of equity on Chinese institutions and practices in Hong Kong. Finally, as *Equity & Trusts Law in Hong Kong* illustrates vividly, there is a wealth of Hong Kong cases that can be used to illustrate the practical impact of equity and trusts law in the Hong Kong context.

The topics covered in this book have been chosen to meet the needs of students of Equity and Trusts in Hong Kong. The first thirteen chapters represent the core of the book and the final chapters on undue influence and confidential information provide some further illustrations of the practical importance of equitable principles in domestic and commercial relationships.

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[1-30] In *Li Hung Chan v Wong Woon Heung*,[29] a husband had assigned property to his concubine with the aim of defeating his creditors, but also sought to retain beneficial interest in his property. This scheme had succeeded in prejudicing the husband's creditors and the husband sought a declaration that the concubine was his trustee for the assigned property. His claim was that the concubine had known of the fictitious nature of the assignment and the purpose of the scheme. The concubine denied such knowledge and claimed instead that the assignment was a gift from the husband. The concubine contended that even if the husband's claim succeeded, he should be denied equitable relief because he had committed a fraud on his creditors. Williams ACJ held that even if the concubine were a party to the fraud, it would not aid the husband. His Lordship further held that:[30]

> [The husband] has come to this Court to ask for equitable relief but, if he is to succeed, he must come with clean hands. To grant him the declaration for which he asks would be to give direct encouragement to him and to many others in Hong Kong of a like mind to defeat their creditors by adopting schemes of this nature.

[1-31] There is a danger in interpreting this maxim too widely in that 'equity does not demand that its suitors shall have led blameless lives'.[31] It is possible for the plaintiff to rectify any inequities or wrongs that may bar equitable relief before trial to regain his otherwise unblemished record. For example, the plaintiff has advanced money to the defendant for the purpose of defrauding the tax department and the tax evasion has been successfully achieved but the defendant then refuses to repay the plaintiff. There is no reason why, if the plaintiff now voluntarily discloses the tax fraud and reaches a settlement with the tax department to repay all taxes and penalties, that he should be deserted by equity.

[1-32] The misconduct must have an immediate and necessary relation to the equitable relief sought before equity denies his relief.[32] If the impropriety indirectly or remotely relates to the relief sought or there is mere general depravity, hands are then not 'unclean'.[33] To illustrate, in *Hin Fai Ltd t/a Sun Food Seafood v Longrace Development Ltd*,[34] a company director, who incorporated a new company to engage in a competing business, forged documents to deceive the government by passing off the new company as the old one so as to obtain a licence to operate. He later transferred his shares in the new company to a third party. Neither the third party nor the new company was aware or otherwise participated in the breaches. Deputy Judge Wong SC held that the claim by the

29 *Li Hung Chan v Wong Woon Heung alias Wong Yuen* (1950) 34 HKLR 213, [1950] HKCU 21.
30 *Li Hung Chan v Wong Woon Heung alias Wong Yuen* (1950) 34 HKLR 213, [1950] HKCU 21 at para 7.
31 *Li Hung Chan v Wong Woon Heung alias Wong Yuen* [1950] HKLR 213, [1950] HKCU 21.
32 *Moody v Cox* [1917] 2 Ch 71 at 87 – 88 per Scrutton LJ; *Hin Fai Ltd t/a Sun Food Seafood v Longrace Development Ltd* [2003] HKCU 1280 (unreported, HCA 1788/2003, 18 July 2003) at §§ 43 – 44; *Poon Ka Man Jason v Cheng Wai Tao* [2015] 2 HKC 143 (CA) at 159D-E.
33 *Jones v Lenthal* (1669) 1 Cas in Ch 154; *Dering v Earl of Winchelsea* [1787] 1 Cox 318, (1787) 29 ER 1184, [1775–1802] All ER 140; *Meyers v Casey* (1913) 17 CLR 90; *Dewhirt v Edwards* [1983] 1 NSWLR 34 at p 51; *Dow Securities Pty Ltd v Manufacturing Investments Ltd* (1981) 5 ACLR 501; *A-G (NZ) v Equiticorp Industries Group Ltd* [1996] 1 NZLR 528; *Glev Pty Ltd v Kentucky Fried Chicken Pty Ltd* (1994) ATPR 41–299; *Atari Games Corporation v Nintendo of America Inc* (1992) 25 IPR 646. See also, *Strong Offer Investment Ltd (In Liq) v Nyeu Ting Chuang* [2007] 3 HKC 234 (CFA) (where a money lender was allowed to enforce a loan agreement which was in breach of the documentary requirements under the Money Lenders Ordinance (Cap 163) since there was no prejudice caused to the borrower).
34 *Hin Fai Ltd t/a Sun Food Seafood v Longrace Development Ltd* [2003] HKCU 1280 (unreported, HCA 1788/2003, 18 July 2003).

new company against the old company for the delivery up of goods was not tainted by any unclean hands and accordingly granted a mandatory injunction compelling delivery up.

[1-33] Similarly, in *The Incorporated Owners of Ning Fung Court v Ho Mei Tak*[35] the DMC provided that the open space of a housing estate was to be used for recreational purposes only but the incorporated owners allowed commercial clients (including PCCW and Citibank) to use the open spaces for displaying counters so as to enable their respective marketing sales personnel to promote business sales there, in breach of the DMC. A flat owner then installed a surveillance system and a wall-lamp at the corridor outside his flat without the incorporated owners' consent, also in breach of the DMC. The incorporated owners sought to enforce the DMC by restraining the flat owner. The Lands Tribunal in granting the injunction sought held that the maxim would not operate to defeat such enforcement action if the owners' corporation's breach had no immediate and necessary relation to the flat owner's breach.

[1-34] *Poon Ka Man Jason v Cheng Wai Tao*[36] further illustrates. In that case, Ricky, a chef of Japanese cuisine, by a company which he was the sole director, opened up and operated a well-known sushi restaurant in Hong Kong named Itamae Sushi. The company had 9 shareholders who all contributed to the funding of this sushi restaurant business and Jason is one of them. After this first Itamae Sushi, Ricky set up other Itamae restaurants (all by companies which Ricky was the sole beneficial owner). Jason, representing other shareholders of the company, commenced derivative action against Ricky for breach of fiduciary duty towards the company and sought account of profit from Ricky. One of the arguments of Ricky was that the Itamae mark was designed and owned by Ricky and that Jason had had acted in bad faith in applying for and seeking registration of the Itamae mark which belong to Ricky. The CA held that Jason's misconduct in surreptitiously registering the Itamae mark has no immediate and necessary relation to the relief sought by the company for breach of fiduciary duty on the part of Ricky; that the act of Jason cannot be attributed to that of the company which consisted of shareholders in addition to Jason; and that accordingly, the company's claim was not barred.[37]

[1-35] Where the defendant seeks to derive advantage from his dishonest conduct in so direct a manner that it is considered to be unjust to grant relief against him, equity will not play into the hands of such a defendant.[38] For example, in company matters, for a just and equitable winding up due to breakdown in mutual trust and confidence of a quasi-partnership company, unless the misconduct was causative of the breakdown in confidence on which the petition was based, it was no bar to a winding-up order.[39] That is to say that if the breakdown in the relationship was at the instigation of the petitioner, not by the other directors, then it is the petitioner's misconduct that has caused the

35 The Incorporated Owners of Ning Fung Court v Ho Mei Tak [2010] HKCU 1587 (unreported, LDBM 11-/2009, 20 July 2010) (Lands Tribunal).
36 Poon Ka Man Jason v Cheng Wai Tao [2015] 2 HKC 143 (CA).
37 Parties appealed to the CFA but the clean hand argument was not relied upon, see, *Poon Ka Man Jason v Cheng Wai Tao* [2017] 1 HKC 463, (2016) 19 HKCFAR 144 at § 132.
38 See, Ian Spry, *Principles of Equitable Remedies* (9th ed, Sydney: Thomson Reuters Australia, 2013), p 254.
39 *Ebrahimi v Westbourne Galleries* [1973] AC 360 at p 387 per Lord Cross; *Re Trocadero Ltd* [1988] 2 HKLR 443, [1988] HKCU 260; *Re Shiu Fook Co Ltd* [1989] 2 HKC 342; *Vujnovich v Vujnovich* [1990] BCLC 227 (PC); *Re Brio Technology International Ltd* [2000] 3 HKC 536. See also *Re Cirtex Co Ltd* [1987] 3 HKC 13; *Re London School of Electronics Ltd* [1986] 1 Ch 211 at 222C per Nourse J that there is no independent or overriding requirement that it should be just and equitable to grant relief or that the petitioner should come to the court with clean hands.

breakdown.[40] In *Re Brio Technology International Ltd*,[41] a company was incorporated in 1996 as a 50/50 joint venture between Lam and Yeung to provide consultancy services in information technology to clients. The two directors and shareholders of the company were Lam's mother and Yeung's father. The company was de facto managed and financed by Lam and Yeung and was operating as a quasi-partnership between Lam and Yeung who reposed trust and confidence in each other. In 1999, differences arose when Yeung discovered that Lam had misappropriated company funds to pay off his personal expenses. When asked to repay the drawings to the company, Lam refused. A deadlock resulted and since about August 1999, neither Lam nor his mother reappeared at the office. Four of the company's staff, representing 50% of its workforce, also left to join Lam's companies. Since August 1999, the company had been funded by the Yeung family alone. Eventually, a petition was presented by Yeung in October 1999 for the winding up of the company on just and equitable grounds and was opposed by Lam's mother on the basis that Yeung had diverted the company's business before filing for winding up. Le Pichon J held that the misconduct (diversion of business) was not causative of the breakdown in confidence between the parties; that the diversion of business occurred after the breakdown; and that accordingly, the absence of 'clean hands' challenge failed.

[1-36] The defence of 'clean hands' is one of general application to all types of proceedings in equity and it is not limited to any particular kind of proceedings. However, for interlocutory proceedings instead of a full trial on the merit, the court would not come to a conclusive finding of fact upon the allegation of unclean hands, unless there is cogent evidence in support.[42] For instance, *Ever Judger Holding Co Ltd v Kroman Celik Sanayii Anonim Sirketi*[43] involved a dispute between a shipowner and a Turkish buyer of a cargo of steel wire rods carried on board the ship. The buyer found that the steel rods were rusty because the Master of ship, knowing that the steel rods were scratched on the surface, still accepted and uploaded them; and allowed the steel rods to be uploaded on deck when it was raining. The buyer believed that the shipowner had colluded with the manufacturer to issue clean bills of lading, notwithstanding that the cargo was damaged, in order to ensure that the manufacturer would get paid the price under the letter of credit. The buyer issued proceedings in Turkey and had the ship arrested. The ship owner applied for an anti-suit injunction against the buyer in Hong Kong and in opposing the anti-suit injunction, the buyer alleged that the shipowner had unclean hands attributable to it the fraud perpetuated by the Master of the ship. G Lam J held that as for an interlocutory application argued on the basis of affidavit evidence, the court could not come to a finding of fraud on the basis of contested affidavit evidence; that cogent evidence was required where serious allegations of wrongdoing were involved and the materials were not sufficiently cogent to infer that the master was fraudulent in deciding to issue and sign the clean bills; that accordingly the defence of clean hands failed.

4.6 Equity assists the diligent and not the tardy

[1-37] A litigant seeking to rely on an equitable right must not delay too long before bringing his claim. Otherwise it may be defeated by the equitable defences of laches and acquiescence.

40 *Re Trocadero Ltd* [1988] 2 HKLR 443, [1988] HKCU 260; *Re Brio Technology International Ltd* [2000] 3 HKC 536.

41 *Re Brio Technology International Ltd* [2000] 3 HKC 536.

42 *Royal Bank of Scotland plc v Highland Financial Partners LP* [2013] 1 CLC 596 (anti suit injunction); *Ever Judger Holding Co Ltd v Kroman Celik Sanayii Anonim Sirketi* [2015] 3 HKC 246 at [47] (anti suit injunction).

43 *Ever Judger Holding Co Ltd v Kroman Celik Sanayii Anonim Sirketi* [2015] 3 HKC 246.

4.7 Equity is equality[44]

[1-38] Equity is equality[45] is that, in the absence of an expressed intention to the contrary, or other circumstances and reasons, parties who are entitled to properties should have the certainty and fairness of equal division.[46] This maxim is usually found in its operation in the division of matrimonial property in a marriage or in a de facto relationship situation, where parties either made advances using their own funds or funds in joint names to purchase property, without any evidence of specific intention that they would be entitled to share equally as a measure of last resort.[47]

4.8 Equity looks to the substance and not the form

[1-39] The court of equity will not allow blind adherence to the legal form of a transaction, if giving effect to the form would allow the substance to be disregarded.[48] This maxim is applied in a number of situations. Firstly, where a vendor of property fails to complete on the date of completion and is thus in breach of contract, equity will regard it as sufficient if the vendor can complete within a reasonable time after the date of completion.[49] However, equity would treat time as being of the essence when the intention of the parties, and the express terms of the agreement they previously entered into, have so stipulated.[50] Secondly, at common law, a receipt is conclusive evidence of payment of the price in full, notwithstanding that only part of the price was paid. Equity does not treat

44 From the Latin phrase *aequitas est aequalitas*. See, generally, J McGhee, *Snell's Equity* (31st Ed) (Sweet & Maxwell: London, 2005) at paras [5-20]–[5-23]; R Meagher, D Heydon, M Leeming, *Meagher Gummow & Lehane's Equity: Doctrines & Remedies* (4th Ed) (Sydney: LexisNexis Butterworths, 2002) at paras [3-145]–[3-155]; HG Hanbury and J Martin, *Modern Equity* (16th Ed) (Sweet & Maxwell: London, 2001) at p 30.

45 From the Latin phrase *Aequitas est aequalitas*. See generally, *Snell* at paras [5-012]; *MGL* at paras [3–130]–[3–140]; *H & M* at para [1-033].

46 *Petit v Smith* (1695) 1 P Wms 7 at 9; *Re Young* (1885) 28 Ch D 705; *Re Bradberry* [1943] Ch 35 at 40; *Re Midland Express Ltd, Pearson v Midland Express Ltd* [1914] 1 Ch 41 at 48 (Eng CA); *Re Searle, Hoare & Co* [1924] 2 Ch 325; *The Tolo* [1916] P 206 at 212; *Jones v Maynard* [1951] Ch 572 at 575; *MacDonald v MacDonald* [1957] 2 All ER 690; *Diwell v Farnes* [1959] 1 WLR 624; *Gage v King* [1961] 1 QB 188.

47 *Jones v Maynard* [1951] Ch 572 at 575 per Vaisey J; *Gissing v Gissing* [1971] AC 886, [1970] 2 All ER 780; *Falconer v Falconer* [1970] 3 All ER 449, [1970] 1 WLR 1333 (Eng CA); *Hall v Hall* [1982] 3 FLR 379 (Eng CA); *Bernard v Josephs* [1982] Ch 391, [1982] 3 All ER 162 (Eng CA); *Burns v Burns* [1984] Ch 317, [1984] 1 All ER 244 (Eng CA); *B v B* [1988] 2 FLR 490; *Preston and Henderson v St Helens Metropolitan Borough Council* (1989) 58 P & CR 500; *Grant v Edwards* [1986] Ch 638, [1986] 2 All ER 426 (Eng CA); *Midland Bank plc v Dobson and Dobson* [1986] 1 FLR 171 (Eng CA); *Lloyds Bank plc v Rosset* [1991] 1 AC 107, [1990] 1 All ER 1111 (HL). In *Ho Lai Chuen v Xerox (Hong Kong) Ltd* [2002] 2 HKC 442, the court applied the maxim to determine what are the 'reasonable charges' that one party has to pay to the other for a copy of the full transcript where the first party initially paid in full – that is, equal sharing of the total transcript cost. Another Hong Kong case illustrating this rule of equal division of matrimonial property is *LKW v DD* [2010] 6 HKC 528, (2010) 13 HKCFAR 537 (CFA).

48 See, generally, J McGhee, *Snell's Equity* (31st Ed) (Sweet & Maxwell: London, 2005) at para [5-24]; R Meagher, D Heydon, M Leeming, *Meagher Gummow & Lehane's Equity: Doctrines & Remedies* (4th Ed) (Sydney: LexisNexis Butterworths, 2002) at paras [3-160]–[3-190]; HG Hanbury and J Martin, *Modern Equity* (16th Ed) (Sweet & Maxwell: London, 2001) at p 30.

49 See *Solomons v Halloran* (1906) 7 SR (NSW) 32; *Canning v Temby* (1905) 3 CLR 419.

50 See *Radcliffe v Warrington* (1806) 12 Ves 326, 33 ER 124; *Steedman v Drinkle* [1916] 1 AC 275; *Union Eagle Ltd v Golden Achievement Ltd* [1997] AC 514, [1997] 2 All ER 215;

a receipt as conclusive evidence of full payment of the price.[51] Thirdly, a party to a deed cannot deny the truth of the terms of a deed or agreement he has voluntarily executed in law, but equity would allow a mistake of facts to be raised against the operation of the estoppel by deed.[52]

4.9 Equity regards as done that which ought to be done[53]

[1-40] This maxim is mainly used in contract cases. An agreement to perform a certain act is regarded by equity as that act having been done. A classic illustration of this maxim is the case of *Walsh v Lonsdale*.[54] There, an agreement to lease was reached between a lessee and a lessor and, subsequently, the lessee went into possession. The lessee paid rent regularly, but not in advance as required by the agreement, and the lessor sought to put in a distress. The lessee sought an injunction, specific performance and damages. The English Court of Appeal held that equity regarded the agreement to lease to be as good as a formal lease itself and thus rent was to be paid in advance. Distress was granted.

[1-41] In Hong Kong, there are a few examples where this maxim finds its application. One example is where family members have contributed moneys to the construction of a property on the basis of an agreement that they would share in the ownership of the said property. In determining the rights and obligations of the parties, equity will deem the arrangement to have been given effect.[55] Upon execution of a sale and purchase contract for land, the purchaser is regarded as the owner in equity and the vendors as trustee for him, such that the purchaser has a full right in equity to dispose of the land.[56] Where a fiduciary receives a bribe in breach of his fiduciary duty, equity regards as done that which ought to be done so that the bribe must be repaid instantaneously to the principal.[57] Where a mortgagor seeks to set aside a sale by the mortgagee, the mortgagor must be ready, willing and able to redeem. If the property has been sold and the purchaser has made improvements on the land, the purchaser has to be allowed the cost of the improvements that have increased the value of the property.[58]

MLC Life Ltd v Edmund Barton Chambers (Level 43) Co-operative Ltd (1990) NSW Conv R 55-550.

51 *Wilson v Keating* (1859) 4 De G & J 588, 45 ER 228.

52 *Scholefield v Lockwood* (1863) 33 LJ Ch 106; *Brooke v Haymes* (1868) LR 6 Eq 25; *Greer v Kettle* [1938] AC 156, [1937] 4 All ER 396.

53 See, generally, J McGhee, *Snell's Equity* (31st Ed) (Sweet & Maxwell: London, 2005) at para [5-25]; R Meagher, D Heydon, M Leeming, *Meagher Gummow & Lehane's Equity: Doctrines & Remedies* (4th Ed) (Sydney: LexisNexis Butterworths, 2002) at paras [3-205]–[3-210]; HG Hanbury and J Martin, *Modern Equity* (16th Ed) (Sweet & Maxwell: London, 2001) at p 29.

54 *Walsh v Lonsdale* (1882) 21 Ch D 9.

55 *Fu Wan Sang v Fu Man Kwong* [2003] HKCU 337 (unreported, HCA 16108/1999, 31 March 2003).

56 *Lee On Construction Co Ltd v The Collector of Stamp Revenue* [1964] HKDCLR 83, [1964] HKCU 46.

57 PJ Millett, 'Bribes and Secret Commissions' [1993] *RLR* 7 at 20, cited in *A-G (HK) v Reid* [1994] 1 AC 324 at 337E–H per Lord Templeman. See also *Secretary for Justice v Hon Kam Wing* [2003] 1 HKLRD 524, [2003] HKCU 147.

58 *Hip On Insurance, Exchange and Loan Co Ltd v Li Po Yung* [1909] 4 HKLR 190, [1909] HKCU 3.

4.10 Equity imputes an intention to fulfil an obligation

[1-42] The equitable doctrine of satisfaction and ademption is derived from this maxim and its application is fairly limited in modern times.

4.11 Equity will not assist a volunteer

[1-43] A volunteer is a person who has not provided any consideration when receiving a transfer of property which he beneficially holds, in contrast with a purchaser for value. There is one important exception: equity provides assistance to beneficiaries of a trust or a deceased's estate, who are usually volunteers. This maxim is sometimes expressed differently: 'equity will not perfect an imperfect gift'.

[1-44] A Hong Kong example is found in *Wu Koon Tai v Wu Yau Loi*.[59] In that case, a father died on 7 September 1921 and his son succeeded the father's land. The son was never registered as successor to the father under section 17 of the New Territories Ordinance (Cap 97) or under any of its predecessors. The son entered into a transaction with a purchaser to sell the land for $200 and subsequently the land was transferred to the purchaser. The purchaser went into possession of the land and for many years, he and his successors occupied the land or were in receipt of rent for it. The son died some time in the 1940s. Upon the death of the son, the grandson succeeded to the estate of the son and, through the son, to the estate of the father. In 1951, the grandson was registered under section 17 of the New Territories Ordinance as successor to his grandfather. The grandson was not registered as successor to the son since the son had himself never been registered. The grandson died in 1962 and Wu Yau Loi succeeded the grandson's estate and was duly registered under section 17 as successor to the land. The purchaser died in 1991 and Wu Koon Tai succeeded to his estate. The court was then asked to decide whether the land had been validly sold and conveyed to the purchaser.

[1-45] The District Court judge decided that the son and his successors held the land in trust for the purchaser. The Court of Appeal, by a majority (Liu JA dissenting), allowed Wu Yau Loi's appeal.[60] The majority held that since the son had never taken a grant to the father's estate or been registered as successor to the father under section 17 of the Ordinance, the land had at no time been vested in him. The title to the land had instead passed directly from the estate of the father to the grandson. Any disposition of the land by the son was ineffective. The majority further considered that the transaction in 1934 could not be enforced as an action brought on a contract for the sale of land. Wu Koon Tai appealed to the Privy Council.

[1-46] The Privy Council allowed the appeal and held that since the land had not been sold to a third party but was held by someone taking as a volunteer through the son, the purchaser's equitable right in the land was enforceable against the present owner of the title, Wu Yau Loi. Lord Browne-Wilkinson said:[61]

59 *Wu Koon Tai v Wu Yau Loi* [1997] AC 179, [1996] 3 HKC 559 (PC).

60 *Wu Koon Tai v Wu Yau Loi* [1995] 2 HKC 732 (CA).

61 *Wu Koon Tai v Wu Yau Loi* [1997] AC 179, [1996] 3 HKC 559 at 568 (PC).

> The equitable right of the purchaser in the land under the contract of sale would have been specifically enforceable against the land vested in the grandson as the personal representative of the son and against all those taking the land as successors to the son: all would be volunteers. Therefore if a grant had been taken to the son's estate, the 1934 contract would have been enforceable against [Wu Yau Loi] as successor, via the grandson, to the estate of the son.

[1-47] Note that all the successors were volunteers and the result would be different if a third party's interest was affected.

4.12 Equity acts *in personam*[62]

[1-48] Equity does not make orders that affect the property, but orders that affect the conscience of the party concerned. As equity is directed at the person but not the property, insofar as the defendant is within jurisdiction, an order can be made against him regardless of where the property is.[63] It acts in *personam* and not *in rem*.[64] In *A-G v Reid*, Lord Templeman explained that equity, which acts *in personam*, would disregard the legal estate vested on a fiduciary who obtained the benefits of a freehold property by way of bribery in breach of fiduciary duty.[65]

5. Self-Test Questions

(1) What do you understand by 'the fusion debate'?
(2) Is there a sense in which fusion has certainly occurred?
(3) What are the arguments for and against the proposition that there is (or should be) a more general fusion of equity and the common law?
(4) In *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] AC 669, [1992] 2 WLR 802 (HL), Lord Browne-Wilkinson set out (at 705) four central principles of trust law (we will return to them later). The first reads:

> (i) Equity operates on the conscience of the owner of the legal interest. In the case of a trust, the conscience of the legal owner requires him to carry out the purposes for which the property was vested in him ….

The focus on conscience means, as we will see, that equity is concerned with the state of a person's knowledge and, sometimes, their honesty. Do you think that this is likely to cause problems?

62 See, generally, J McGhee, *Snell's Equity* (31st Ed) (Sweet & Maxwell: London, 2005) at paras [5-27]–[5-28]; R Meagher, D Heydon, M Leeming, *Meagher Gummow & Lehane's Equity: Doctrines & Remedies* (4th Ed) (Sydney: LexisNexis Butterworths, 2002) at paras [3-220]–[3-260]; HG Hanbury and J Martin, *Modern Equity* (16th Ed) (Sweet & Maxwell: London, 2001) at p 31.
63 *Li Chok Hung v Li Pui Choi* (1910) 5 HKLR 121, [1910] HKCU 6.
64 *Li Chok Hung v Li Pui Choi* (1910) 5 HKLR 121, [1910] HKCU 6; *Mercedes-Benz Ag v Leiduck* [1995] 3 HKC 1 at 13–14 and 20; *Berman v SPF CDO I Ltd* [2011] 2 HKLRD 815, [2011] HKCU 522.
65 *A-G v Reid* [1994] 1 AC 324 at 331B–H. Cited in *Secretary for Justice v Hon Kam Wing* [2003] 1 HKLRD 524, [2003] HKCU 147 at para 23.

6. Further Reading

(1) Andrew Burrows, 'We Do this in Common Law but that at Equity' (2002) 22 *Oxford Journal of Legal Studies* 1
(2) S Holdsworth, 'Relation of the Equity Administered by the Common Law Judges to the Equity Administered by the Chancellor' (1916) 26 *Yale Law Journal* 1
(3) Oliver Wendell Holmes, 'Early English Equity' (1885) 1 *Law Quarterly Review* 162
(4) Jill Martin, 'Fusion, Fallacy and Confusion: A Comparative Study' [1994] *Conveyancer and Property Lawyer* 13
(5) Peter Millett, 'Equity's Place in the Law of Commerce' (1998) 114 *Law Quarterly Review* 214
(6) F Tudsbury, 'Equity and the Common Law' (1913) 29 *Law Quarterly Review* 154
(7) Sir Paul Vinogradoff, 'Reason and Conscience in Sixteenth Century Jurisprudence' (1908) 96 *Law Quarterly Review* 373

CHAPTER 2

THE TRUST

1. INTRODUCTION

[2-1] The trust is equity's most important contribution to Hong Kong's legal system. A large part of this book will be devoted to a study of the trust – it will explain the rights and duties of the parties to a trust and the proprietary (ownership) rights created by the trust. This chapter introduces the fundamentals of the trust relationship and explains the types of trust that can be created or that can arise. It also sets out some of the practical uses to which the trust can be put. The next few chapters will build on the foundations thus laid.

[2-2] The essential concept underlying the trust is that it allows a settlor (S) to transfer ownership of property to a trustee (T) on the basis of a prior understanding between them that T holds the property on behalf of someone else, ie the beneficiary (B). The trust provides a good example of the interaction between the common law and equity. The common law regards T as the owner but equity holds that it would be unconscionable for T to act in defiance of his understanding with S. Although T is the 'legal' owner, his ownership is subject to the obligations that he assumed when he agreed to act as trustee of the property.

[2-3] Why would anyone want to create a trust? If you wanted to give property to someone, why not simply give it to them? Why use the cumbersome trust as the device for making a gift? The answers to these questions should become clear as we progress through the book but we can provide an outline in this chapter. The trust is useful, for example, where a parent wants to make a gift to an infant; the trustee administers the property until the child is old enough to be trusted with the property. The trust might be used to ensure that someone gets the use of property, or the income from it, but not the property itself. So, real estate or shares, for example, could be put into a trust. The settlor could provide for one beneficiary to receive the income during his lifetime and for another to receive the capital when the first beneficiary has died. A trustee could hold money that is to be used for charitable purposes. When a couple buys property, they can agree on how the equitable interest is to be divided between them; they can hold the property on trust for themselves. We will also see that the trust has its part to play in business relationships. Solicitors, for example, hold clients' money on trust for them.

[2-4] The trustee is under a duty to comply with the settlor's directions given at the time of setting up the trust. If a formal written instrument was drawn up to govern the trust, then the trustee's primary duty is to comply with the settlor's wishes as expressed in the trust instrument. Equity imposes further important duties on the trustee; a trustee must act in the best interest of the beneficiaries, he must not allow his interests to come in conflict with those of the other beneficiaries and he must not allow himself to profit from the trust property without the other beneficiaries' informed consent, save for proper remuneration received for management of the trust in his role as a trustee. The trustee owes his duties to the beneficiaries. It is the beneficiaries who have the right to approach the court to complain of a trustee's breach of duty. In other words, the beneficiaries have personal rights as against the trustees. If the beneficiaries suffer a loss because of a trustee's breach of trust, then the beneficiaries can seek compensation from them.

[2-5] However, in addition to the above, the beneficiaries have a proprietary (ownership) interest in the trust property itself. Although the legal title is vested in the trustees, the equitable or beneficial ownership is vested in the beneficiaries. If a trustee transfers property to a third party in breach of trust, he transfers the legal title subject to the equitable interest of the beneficiaries. The person who acquired the property from the trustees steps, in a limited sense, into the shoes of the trustees. He is not subject to the full range of duties of the original trustee but he does hold the trust property on behalf of the beneficiaries. Thus, if a trustee disposes of property in breach of trust and this causes harm to the interest of the beneficiaries, there are two ways of attempting to remedy the situation. The first is to call on the trustees themselves to make good the loss (the personal remedy). The second is to try to recover the property itself.

[2-6] This is potentially unfair; the person who took the property from the trustee might be innocent, unaware of the existence of the trust. He may have bought the property at an arm's length transaction. This potential unfairness is mitigated, but not entirely removed, by the rule that a bona fide (good faith) purchaser of the property who has no notice of the beneficial interest takes free of that interest. The beneficiary will then have only his right to make a claim against the wrongdoing trustees.

2. History of the Trust

[2-7] The trust has its origin in medieval times. Usually, a landowner would employ a trusted agent, the *feoffee to uses*, to hold his land for the benefit of the landowner and his heirs. The landowner was known as the *feoffer to uses* and the beneficiary as the *cestui que use*. Once the land was conveyed by the *feoffer* to the *feoffee* (the trustee), the law regarded the *feoffee* as having the full legal title to the land to the exclusion of the *feoffer*. The *cestui que use* neither had rights at law to compel the *feoffee* to apply the property for their benefit nor any legal claim or title to the land. That is, the common law offered no protection to the *feoffer* nor to the *cestui que use*. Equity intervened to compel the *feoffee* to hold the land for the exclusive use of the *cestui que use*. Equity's protection was not limited to an *in personam* action against any wrongdoing by the *feoffee* but extended to any other person who took the land from the *feoffee*. It did not, however, allow the *cestui que use* to claim against a *bona fide* purchaser of the use for value without notice. Gradually, it was recognised that the *feoffee to uses* was the owner in law of the land and the *cestui que use* was the owner in equity.[1]

[2-8] Uses were common and widely adopted to manage people's affairs and there was an obvious need for it: a man going on a crusade for his country needed a trusted agent to manage his estates, say to receive rent and dues for support of his family; or an indicted felon may fear a conviction which might result in the loss of his land.[2] The widespread deployment of uses had a negative impact on the royal revenue, and finally, Henry VIII sought in the 1530s to abolish uses but failed. Following a compromise with the House

1 See HG Hanbury and J Martin, *Modern Equity* (16th Ed) (Sweet & Maxwell: London, 2001) at pp 8 et seq.

2 *Davies v Otty (No 2)* (1865) 35 Beav 208.

of Commons, the Statute of Uses 1535 (27 Hen VIII c 10) was enacted. It did not totally abolish uses but had a draconian effect on them. Not only did it re-impose all feudal taxes, it restricted conveyance of land to heirs only and prevented the conveyance of land to any third party, who would otherwise stand as a *feoffee*. However, it had a short life, and soon the Statute of Wills (32 Hen VIII c 1) was enacted in 1540 to remove its most controversial effects.[3] The Statute of Uses 1535 remained in force until 1925. Despite the Statute of Uses 1535, the law of trusts continued to develop in the Court of Chancery into its modern form.

[2-9] The modern law of trusts was adopted in Hong Kong through the enactment of the Application of English Law Ordinance (Cap 88) in 1966. Despite its repeal upon the return of Hong Kong to the People's Republic of China on 1 July 1997, the law of trusts, part of the rules of equity, continues to apply in Hong Kong.[4]

3. Types of Trust

[2-10] The rest of this chapter introduces some of the most fundamental distinctions between different categories of trust. First, it explains the distinction between express trusts (those that are deliberately created and accepted), resulting and constructive trusts. Second, it explains the distinction between fixed and discretionary trusts. A fixed trust is one where it is possible, from the outset, to list the beneficiaries and to calculate the proportion of the trust fund that each will receive. By contrast, in the case of a discretionary trust, the trustees are given instructions as to the class of potential beneficiaries but are given a discretion as to which members of the class are to benefit or as to the extent of their entitlement or both. An express trust could be either a fixed trust or a discretionary trust. The chapter includes a discussion of Chinese customary trusts and their relationship with the law of equity and trusts. Finally, there is an account of two very specialised trust relationships, the *Quistclose* trust and the *Romalpa* clause.

3.1 Express, resulting and constructive trusts

[2-11] Trusts can be divided into express, resulting and constructive trusts. An express trust is one that has been deliberately established and accepted. The simplest example is where the settlor expressly declares a trust of property. Such a trust might be inferred or implied from the words or actions of the settlor.

[2-12] Resulting trusts are commonly divided into two sub-categories – the presumed resulting trust and the automatic resulting trust. The presumed resulting trust itself covers two situations. In the first, there has been a voluntary transfer of property from A to B. Equity's starting point is to presume an intention that B holds on trust for A. In the second situation, B pays for some property (or contributes to the price) but it is transferred to A's name alone. Equity presumes that A holds on trust for B; the size of B's equitable interest is calculated by looking at the proportion of the purchase price contributed by B.

[2-13] Whether automatic resulting trusts also depend on intention is controversial. Some explanations of automatic resulting trusts see them as arising in cases where there

3 See DB Parker and AR Mellows, *The Modern Law of Trusts* (8th Ed) (Thomson Sweet & Maxwell: London, 2003) at pp 4 et seq.

4 See above, Chapter 1.

is a transfer but no intention to benefit the recipient. It may be that automatic trusts arise to fill 'gaps' where there is no clear indication as to who has the beneficial ownership. Or, again, it may be that intention is irrelevant to automatic resulting trusts and that they arise by operation of law when the transferor has failed to dispose of the beneficial interest despite an intention to do so. The effect of an automatic resulting trust is that the beneficial interest in the property reverts to the original owner. They have been used to deal with the question of who owns money donated to help people in need after that need has been remedied and the donors' money has not been exhausted. In some cases, the courts have held that the surplus is held on automatic resulting trust for the original donors.

[2-14] The institutional constructive trust (the only kind recognised in Hong Kong) has been explained in the following terms:[5]

> A constructive trust arises by operation of law whenever the circumstances of the case are such that it would be unconscionable for the owner of the property … to assert his own beneficial interest in the property and deny the beneficial interest of another … the constructive trustee really is a trustee. He does not receive the trust property in his own right but by a transaction by which both parties intend to create a trust from the outset and which is not impugned by the plaintiff. His possession of the property is coloured from the first by the trust and confidence by means of which he has obtained it, and his subsequent appropriation of the property to his own use is a breach of that trust.

[2-15] Institutional constructive trusts are trusts that arise by operation of law but that exist independently of any judicial pronouncement; the court's role is not to create them but merely to declare their existence. The boundaries between express trusts and constructive trusts are not always clear. The use of the constructive trusts to decide on how the equitable interest in family homes is to be allocated as between spouses or co-habiting couples will be examined elsewhere in this text.

[2-16] The institutional constructive trust is also used in another category of cases where someone implicated in a fraud receives trust property as a result of the fraudulent action. Trustees who make off with trust property, as well as those who receive trust property knowing that their receipt amounts to a breach of trust, fall into this category. This type of liability even extends to people who dishonestly assist a breach of trust even though they never actually receive trust property themselves.

[2-17] Some jurisdictions recognise another category of constructive trust, which is known as the remedial constructive trust. The remedial constructive trust has been described by Lord Browne-Wilkinson as a 'judicial remedy giving rise to an enforceable obligation: the extent to which it operates retrospectively to the prejudice of third parties lies in the discretion of the court'.[6]

[2-18] Here the court does not discover a pre-existing constructive trust but, rather, creates the constructive trust as a way of doing justice between the parties. The orthodox view is that the remedial constructive trust is not a part of Hong Kong's law of equity.

3.2 Chinese customary trusts

[2-19] There exists in Hong Kong a type of Chinese customary trust known as the ancestral worship trust or the ancestral land trust. Basically, ancestral land is set aside

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5 *Selangor United Rubber Estates Ltd v Cradock (No 3)* [1968] 2 All ER 1555 at 1582.
6 *Westdeutsche Landesbank Girozentrale v Islington Borough Council* [1996] AC 669 at 714 (HL).

and designated for the purpose of ancestral worship. Rents of this land go towards the maintenance of the ancestral temple, to provide financial assistance to clan members in need, and to fund education of members of the clan. The land is held in the name of the ancestor and cannot be transferred or conveyed without the consent of the representatives of the clan. Chinese customary law governs the inheritance of such land.[7] Chinese customary law does not recognise testamentary disposition and all disposition has to be *inter vivo*.[8] Under Chinese customary law, land can be held on one of three types of trusts for beneficial interests: the *tsos*, the *tongs*, and the *wuis*, which are all species of clans. A *tso* is managed by registered managers who are trustees within the meaning of the Trustee Ordinance (Cap 29).[9] The members of a *tso* are the living male descendants from time to time of the focal ancestor.[10] The managers cannot dispose of *tso* property against the wishes of the members, and in the absence of a distribution, each member only has a life interest.[11] Membership of a *tso* is a birthright. It stems from descent instead of by an admission process and there is no need for any formal or informal process of admission.[12] Whenever a new member of the *tso* is born, a new equitable interest in the *tso* land is created for that new member.[13] Existing members of a *tso* have no right to exclude a male descendant from the *tso* in the absence of specific provision to such effect when the *tso* was established.[14]

[2-20] English trust law does not apply to Chinese customary trusts. In *Tang Kai-chung v Tang Chik-shang*,[15] land was divided into nine groups by a common ancestor who had six sons. Descendants of each son formed a separate *tong*, and six of the nine groups were formed to correspond with the number of *tongs*. The number of members in each *tong* varied and so did their individual entitlement. The registered managers of the two smaller groups proposed that the six groups be portioned into six groups of equal value so as to avoid pressure by the larger groups on the smaller groups. The court dismissed the action, recognising that a grant of partition would be destructive of the social structure of the clan. Further, the court held that section 13 of the New Territories Ordinance (Cap 97) recognised Chinese law and custom as mandatory and thus any aspect of English law affecting customs or trusts must be disregarded. Ordinances of general application such

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7 New Territories Ordinance (Cap 97), section 13(1). The New Territories covers areas from the north of Boundary Street to the Shum Chun River, together with some 235 islands.
8 *Re Estate of Lau Wai Chau* [2000] 1 HKC 681, (2000) 3 HKCFAR 98 at 103D - F, [2000] 1 HKLRD 924; followed in *Tang Tak Sum v Tang Kai Fong* [2013] 4 HKLRD 16, [2013] HKCU 1689 at [54] per DHCJ Chan SC.
9 *Tang Kai-Chung v Tang Chik-Shang* [1970] HKLR 276 at 304 per Mills-Owens J; *Wong Shing Chan v To Kwok Keung* [2008] 5 HKC 372 (CA); *Million Way v To Shing Wo* [2011] 2 HKLRD 1017, [2011] HKCU 766 (CA) (the trust relationship is not altered and converted into one of principal and agent, even the members of the Wui authorised the manager to enter into commercial arrangements with third parties).
10 *Tang Yau Yi Tong v Tang Mou Shau Tso* [1995] 2 HKC 245, [1994–95] CPR 236; *Tang Yau Yi Tong v Tang Mou Shau Tso* [1996] 2 HKC 471, [1996] 2 HKLR 212 (CA).
11 *Chu Tak Hing v Chu Chan Cheung Kiu* [1968] HKLR 542, [1968] HKCU 71; *Tang Kai Chung v Tang Chik Shang* [1970] HKLR 276; *Kan Fat Tat v Kan Yin Tat* [1987] 4 HKLR 516, [1987] HKCU 258; *Tang Yau Yi Tong v Tang Mou Shau Tso* [1995] 2 HKC 245, [1996] 2 HKLR 212; *Leung Kuen Fai v Tang Kwong Yu Tong* [2002] 2 HKLRD 705, [2002] HKCU 745; *Tang Woung Shiu v Tang Kun Yueng* [2003] 1 HKC 195.
12 *Tang Chun Kit (A Minor) v Tang Lo Ping* [2004] 4 HKC 492.
13 *Wong Shing Chan v To Kwok Keung* [2007] 4 HKLRD 232, [2007] HKCU 1049 (DC); [2008] 5 HKC 372 (CA); *Tang Man Kit v Chong Kee Ting Vicwood* [2011] HKCU 1339 (unreported, HCA 1222/2010, 14 July 2011) at para [17].
14 *Tang Chun Kit (A Minor) v Tang Lo Ping* [2004] 4 HKC 492.
15 *Tang Kai-chung v Tang Chik-shang* [1970] HKLR 276.

as the Intestates' Estates Ordinance (Cap 73), the Inheritance (Provision for Family and Dependants) Ordinance (Cap 481) and the Probate and Administration Ordinance (Cap 10) do not apply to proceedings in relation to New Territories land, which are specifically governed by the New Territories Ordinance (Cap 97). Should the land cease to be subject to the New Territories Ordinance, the aforesaid Ordinances of general application will resume their governance.[16]

The Trustee Ordinance (Cap 29) applies to clans.[17] The registered managers are trustees within the meaning of the Trustee Ordinance, notwithstanding that their powers as such are to be found in section 15 of the New Territories Ordinance (Cap 97) and not the Trustee Ordinance.

3.3 Ancestral worship trust

[2-21] To create to ancestral worship trust over the land, a t'ong or a t'so would have to be set up, and the land would need to be registered in the name of such t'ong or t'so.[18] A testator, who sought to create an ancestral worship trust over the land he owned, even by writing, was held to be insufficient in *Tang Tak Sum v Tang Kai Fong*.[19] There, an indigenous grandfather who died in 1965, had four sons who had their own families (房 fongs) and grandchildren. Defendant's father was the head of the first fong, while claimants' father was the head of the third fong. In 1939, the grandfather divided his houses and land amongst the four fongs and designated the rest of his land for ancestral worship by a Division of Family document (分家文書). In 1999, the Division of Family document was registered at the New Territories Registry and was given legal effect. Under the Division of Family document, the son of the first fong (and subsequently the Defendant) received all income generated by the land. Since the 1990s, the Defendant had rented out the Land as a public car park. Upon the Planning Department's notice banning the public car park as an unauthorised development, the claimants claimed that the Defendant had mismanaged the Land and demanded for the first time in July 2009 an account from the Defendant of all his dealings with the Land and pleaded that by the Division of Family document, the ancestral worship trust came into existence from 1939 and the Defendant should be bound to account. Chan SC DHCJ held, inter alia, that the Division of Family could not by itself create an ancestral worship trust over the land; that the creation of such a trust required positive steps to be taken by either the deceased in his lifetime or his descendants after his death, ie setting up a t'ong or t'so and registering the land in the name of the t'ong or t'so; and that accordingly, no ancestral worship trust was created over the land, whether during the grandfather's lifetime or on his death.

[2-22] An ancestral worship trust is of indefinite duration and cannot exist in Hong Kong except in the New Territories, where certain land can be held on Chinese customary trusts for ancestral worship.[20] In *Re Estate of Lau Wai Chau*,[21] the ancestor, Lau Wai Chau, was a successful businessman born in 1864, who had land in Guangdong Province and in the

16 New Territories Land (Exemption) Ordinance (Cap 452), section 3.
17 *Lau Leung Shi v Lau Po Tsun* [1911-1925] HKC 15, (1911) 6 HKLR 149 (FC); *Ip Cheung-kwok v Ip Siu-bun* [1988] HKC 437, [1988] 2 HKLR 247.
18 *Tang Tak Sum v Tang Kai Fong* [2013] 4 HKLRD 16, [2013] HKCU 1689 at [57] per DHCJ Chan SC.
19 *Tang Tak Sum v Tang Kai Fong* [2013] 4 HKLRD 16, [2013] HKCU 1689.
20 *Re Estate of Lau Wai Chau* [2000] 1 HKC 681 (CFA). See T Tyler, 'Never the Twain' (1998) 7 *Hong Kong Lawyer* 14.
21 *Re Estate of Lau Wai Chau* (2000) 3 HKCFAR 98, [2000] 1 HKC 681 (CFA).

New Territories. He also had five wives and eight sons. His eldest son predeceased him and a son of the second son was adopted to continue the line of the eldest son. The eight sons each had their own families (the *fongs*) but only the eighth son had survived. The ancestor made an English will in 1930 appointing his second, third (Lau Leung Chau) and fourth sons as his executors. Between 1932 and 1933, the ancestor divided some of his New Territories properties into nine parts. One part was given to each of the sons and a ninth part given to his second, third and fourth sons expressly on trust for himself. In 1932, the ancestor made a codicil in Chinese to his English will, which provided, inter alia, that the remaining unallocated properties, including fish ponds and paddy fields, were to be kept and managed for payment of expenses designated by the ancestor while alive, and after his death, to be held for the purpose of offering sacrifices to ancestors or gods. After the ancestor's passing in 1933, his properties were managed by the second, third and fourth sons. During the Second World War, the second son collected all the rental income and refused to share it with the other families, other than that of the deceased elder son. This resulted in a family disagreement and, in 1946, the ancestor's remaining properties were divided amongst the eight families (*fongs*) in equal shares. The ancestral hall and ancestral graves were regarded as common property and retained for ancestral worship. The method of allocation of remaining properties was by random drawing of lots. Having made the greatest contribution to the family by being the active manager of the properties, the second son had the privilege to draw first. The allocation was recorded in a document in Chinese titled 'Deed of Confirmation of Division of Assets for Descendants of Ancestor Lau Wai Chau', made up of eight signed duplicates, which was later confirmed by a Deed of Family Arrangement (DFA) in English, properly prepared by solicitors. Shortly thereafter, the eight *fongs* took possession of their respective properties. Between 1980 and 1995, various parts of the properties were resumed. The plaintiff, a son and the executor of the fourth son who had obtained letters of administration with the will of the estate of the ancestor annexed, negotiated with the government over the compensation for the resumptions payable to several of the *fongs*. Before the government would pay the compensation, it insisted that he obtain vesting orders in respect of those lands. In 1995, he was obliged to commence proceedings for vesting orders. These were obtained and the compensation paid. No agreement, however, was reached on the allocation of the compensation (in excess of HK$8 million). Proceedings were commenced in 1996 to determine the validity of the DFA. At trial, Cheung J held that the DFA was valid and binding.[22] Appeals to both the Court of Appeal[23] and the Court of Final Appeal were dismissed. The Court of Final Appeal held that:

(1) An ancestral worship trust existing under Chinese law and custom took the form of an endowment in perpetuity of property for the purpose of ancestral worship. Such endowments were to be made either by steps taken by someone in his lifetime to carry out his own wishes or by steps taken by heirs in their lifetime to carry out the wishes of a deceased ancestor. In other words, it has to be settled *inter vivos* by deed and not by will.[24]

(2) Under Chinese law and custom, no ancestral worship trust could be created by will for the simple reason that Chinese law and custom did not recognise testamentary dispositions. The testamentary capacity of the ancestor under Hong Kong law could not be relied upon to create, purportedly by way of an express

22 *Lau Yue Kui v Estate of Lau Leung Chau* [1998] 3 HKC 562, [1998] 1 HKLRD 579 (CFI).
23 *Re Estate of Lau Wai Chau* [1999] 2 HKC 63 (CA).
24 *Lau Yue Kui v Estate of Lau Leung Chau* [1998] 3 HKC 562, [1998] 1 HKLRD 579 at 688C–E (CFI).

direction in a will, an ancestral worship trust over New Territories land for the purposes of Hong Kong law.[25]

[2-23] It is a common Chinese tradition that a man devises land he owns to his descendants in his family and wishes that his children and grandchildren benefit from his gifts. Descendants sometimes regard this devise of real property as a kind of 'family property' and that it is expected that all the descendants share in the use and ownership of the land and not divide or sell their respective shares without the consent of all others. This concept of 'family property' is not part of the law of Hong Kong. Descendants hold their respective interests in the 'family property' as tenants in common. Chinese customary law has no application in this respect because Chinese customary law does not state that a son has no identifiable interest in his father's estate, or that such interest cannot be disposed of by him without the consent of his brothers. Rather, under Chinese customary law, the sale or disposition of a son's share could be effective.[26]

3.4 *Quistclose* trust

[2-24] If money is lent for a mutually agreed sole purpose, then that money becomes the subject matter of a trust. If the purpose of the loan cannot be fulfilled for some reason, then the putative borrower will be bound to return the money to the lender and is forbidden to use it for another purpose. This type of arrangement is known as a *Quistclose* trust.[27] If the loan monies cannot be used for their agreed purpose, then they are held on trust for the lender. The practical significance of this is that the funds are then not available to meet the claims of other creditors of the borrower. The *Quistclose* trust makes it possible to provide short-term finance to a borrower who may be in financial difficulties while protecting them from the borrower's creditors. The precise analysis of the *Quistclose* trust has been the subject of both judicial and academic debate.

[2-25] To establish a *Quistclose* trust, it is necessary for the provider of the money or the lender to have an intention to create a trust. In *Twinsectra Ltd v Yardley*, Lord Millett stated that:[28]

> ... [a] *Quistclose* trust does not necessarily arise merely because money is paid for a particular purpose. A lender will often inquire into the purpose for which a loan is sought in order to decide whether he would be justified in making it. He may be said to lend the money for the purpose in question, but this is not enough to create a trust; once lent the money is at the free disposal of the borrower.

[2-26] There, a lender was only prepared to make a loan to a company for the purpose of purchasing property if repayment of the loan was secured by a solicitors' personal undertaking to repay it. The company's own solicitor was unwilling to give such an

25 *Lau Yue Kui v Estate of Lau Leung Chau* [1998] 3 HKC 562, [1998] 1 HKLRD 579 at 688F–G (CFI).

26 *Re Tse Lai Chu (decd)* [1946-1972] HKC 160, [1969] HKLR 159; *Wu Koon Tai v Wu Yau Loi* [1996] 3 HKC 559; *Yau Kwai v Yau Kar Siu* [2004] 4 HKC 141.

27 *Toovey v Milne* (1819) 2 B & Ald 683, 106 ER 514; *Edwards v Glyn* (1859) 2 El & El 29, 121 ER 12; *Re Vautin* [1990] 2 QB 325; *Barclays Bank Ltd v Quistclose Investments Ltd* [1970] AC 567; *Carreras Rothmans Ltd v Freeman Mathews Treasure Ltd* [1985] 1 Ch 207; *Twinsectra Ltd v Yardley* [2002] 2 AC 164. See, generally, William Swadling (ed), *The Quistclose Trust: Critical Essays* (Hart Publishing Ltd: Oxford, 2004) and Jonathan Edwards, 'Quistclose Trusts: was Lord Wilberforce right after all?' (2013) 19(2) *Trusts & Trustees* 176–189.

28 *Twinsectra Ltd v Yardley* [2002] 2 AC 164 at para 73.

undertaking, and a second solicitor was approached who received the loan proceeds after giving an undertaking, which was in the following terms:

> (1) The loan moneys will be retained by us until such time as they are applied in the acquisition of property on behalf of our client.
>
> (2) The loan moneys will be utilised solely for the acquisition of property on behalf of our client and for no other purposes.
>
> (3) We will repay to you the said sum of £1 million together with interest.

[2-27] On receipt of the loan proceeds, the second solicitor released the money to the first solicitor, in accordance with the company's instructions. The money was then applied substantially for purposes other than the acquisition of property, the loan was not repaid, and the second solicitor's undertaking proved worthless, he having gone bankrupt. The lender brought a claim against (among others) the first solicitor, on the basis that the arrangement created a trust in respect of the loan proceeds in the hands of the second solicitor, which had been breached with the alleged dishonest assistance of the first solicitor. The first solicitor was ultimately successful in contending that he had not been guilty of any dishonest assistance, but the House of Lords unanimously agreed that the arrangement did give rise to a *Quistclose* trust.

3.5 *Romalpa* clauses

[2-28] A *Romalpa* (or retention of title) clause is, in essence, an agreement between a supplier and a purchaser that the title to the goods supplied will not pass to the purchaser until full payment has been made for all of the goods or, alternatively, until the latter has paid for all debts due to the supplier regardless of the cause of incurrence and not limited to the price of the supplied goods.[29] It gives suppliers an extra weapon to make sure that they are paid for the goods that they have supplied. The idea is that title in the goods will not pass until they have been paid for. If the buyer does not pay, the seller has the right to reclaim the goods since he would never have parted with ownership

[2-29] The term '*Romalpa* clause' is derived from the English Court of Appeal decision of *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd*.[30] In this case, the aluminium supplier sold aluminium foil to a purchaser on the basis that the title of the aluminium foil would remain with the supplier until full payment was made, at which point the title would be vested in the purchaser. Upon appointment of a receiver to the purchaser, there was a competing claim between the supplier and the receiver as to the entitlement to the unsold goods in possession and the separately identifiable proceeds of sale from a portion of the supplied aluminium. The parties agreed that the contract conferred implied power to sell the goods. At trial, Mocatta J found for the supplier and held that the supplier was entitled to both the goods and proceeds. On appeal, the critical question before the Court

29 See *Hong Kong Hua Guang Industrial Co v Midway International Ltd* [2000] 2 HKC 348 (CA). See also Sally A Jones, 'Retention of Title Clauses Ten Years From *Romalpa*' (1986) 7(6) *Comp Law* 233; Roger Gregory, '*Romalpa* Clauses as Unregistered Charges – A Fundamental Shift' (1990) 106 *LQR* 550; John De Lacy, 'When is a *Romalpa* Clause Not a *Romalpa* Clause? When It is a Charge on Book Debts' (1992) 13(9) *Comp Law* 164; '*Romalpa* Clauses' (1992) 4 *BondLR* 186; '*Romalpa* Clauses and Equitable Liens' (1993) 23 *QLSJ* 379; '*Romalpa* Clauses' [1997] '*Romalpa* Clauses: The Fundamental Flaw' (1994) 68 *ALJ* 404; '*Romalpa* Clauses Revisited – Transactions' [2000] *NZLJ* 247. *NZLJ* 391; Jane Anderson, '*Romalpa* Clauses Revisited – Transactions' [2000] *NZLJ* 247.

30 *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd* [1976] 1 WLR 676.

of Appeal was whether the implied contractual right allowed the purchaser to sub-sell the goods merely as the supplier's agent or to sell it for its own account.[31] The Court of Appeal held that the purchaser had sold the goods merely for the supplier's account.[32] The supplier was entitled to trace into the proceeds in accordance with the principle in *Re Hallett's Estate*.[33]

4. Self-Test Questions

(1) Who owns the property that has been put into a trust?

(2) What remedies are available to beneficiaries if the trustee sells the trust property and keeps the proceeds of sale for himself?

(3) What are the essential differences between fixed and discretionary trusts?

31 *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd* [1976] 1 WLR 676 at 689, 691, and 693–694.

32 *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd* [1976] 1 WLR 676 at 690, 693, and 694.

33 *Re Hallett's Estate* (1880) 13 Ch D 696.

CHAPTER 3

Express Trusts (Part 1): The Three Certainties

1. Introduction

[3-1] This chapter begins the task of explaining the fundamental requirements to be observed in setting up an express trust. There are no formalities to be observed; for example, there is no need for the trust to be in writing (except in the case of trusts of land). It is enough that the settlor clearly expresses his intention to establish the trust relationship and that the requirements set out below are observed.

[3-2] This chapter discusses the need for the three certainties to be present. These are the certainties of intention (or words), subject matter and objects. The first refers to the requirement that the settlor should have clearly expressed his intention to create a trust rather than, for example, to make a gift to the putative trustee. Certainty of subject matter refers to the requirement that it should be possible to identify the trust property and the extent of any beneficiary's interest in that property. Certainty of objects refers to the requirement that one should be able to say who the beneficiaries for the class of trust or gift in question are with the degree of certainty required by equity.

[3-3] There are other requirements for the creation of an express trust and these will be considered in subsequent chapters. The trust has to be constituted, that is to say ownership of the trust property must be transferred to the trustee (if the settlor and trustee are not the same person). This takes care of itself when the settlor declares himself as trustee. When the settlor and the trustee are different people, however, the trust is not constituted until the necessary transfer of ownership to the trustee has taken place. Until that has happened, the trust is not constituted. Unless the settlor is under a contractual obligation to the beneficiary to establish the trust, the settlor remains free to change his mind until the trust has been constituted.

[3-4] A later chapter will explain the law concerning secret trusts. Here, on the face of it, the settlor (S) has bequeathed property to the trustee (T) in a will. Off the face of the will, however, S and T have agreed that T will, in fact, hold the property on trusts indicated by S to T. The will does not tell the whole story. The chapter will discuss the requirements for there to be an effective secret trust and its nature. It will also explain the distinction between secret and half-secret trusts.

[3-5] Express trusts have to comply with the law concerning perpetuities, accumulations and maintenance. These rules, together with the law concerning sham and unlawful trusts, will also be discussed and explained in a subsequent chapter.