

CREATING AN EXPRESS TRUST

5.1 HOW IS AN EXPRESS TRUST CREATED?

A valid and enforceable express trust is created when a settlor makes a valid declaration of trust and the trust property is transferred to the trustee. The transfer of legal title to the trust property to the trustee is referred to as the constitution of the trust. The trustee must have legal title to the trust property for a trust to come into being. Different types of property require different methods of transfer, for example land must be conveyed to the trustee and shares must be transferred according to the restrictions placed on share transfer. Generally personal property is transferred by delivering the property to the trustee, for example a trust of \$1,000 could be constituted by delivery of bank notes to the value of \$1,000 to the trustee.¹

Declaration and constitution of the trust may occur at the same time or declaration may precede constitution. Thus a settlor may hand over \$1,000 to a friend whilst at the same time telling that friend that they are to hold the property on trust. The settlor may also tell his friend that he will be giving him \$1,000 in the future and that when he receives it the friend is to hold it on trust. The trust is only constituted and so valid when the property is transferred to the friend/trustee. Until the trust is constituted the settlor can change his mind and decide not to create the trust.² A settlor may also transfer property to a friend and subsequently inform the friend that the property is to be held on trust; however, this method of formation of a trust may cause evidential problems as the friend may have believed the initial transfer was a gift. Thus the transferee must know he is not receiving the property as a gift. If there is evidence that the property has been transferred as a gift then any subsequent attempt to declare a trust over the property by the transferor will fail as the gift to the transferee takes effect immediately upon transfer with intent to create the gift—the common law does not acknowledge “a gift for second”, a gift is a gift.³ A settlor may also declare himself trustee of his own property, in which case he does not have to transfer the property as he already has legal title. For example, “I now hold this \$1,000 on trust for Sarah.”

The declaration of trust can also be in a will and the constitution of the trust occurs when the executors transfer the property to the trustee as they administer the will—“I am leaving Michael my copy of Maitland’s *Equity*, Michael will hold it on trust for my nephew until he is a qualified lawyer.” When the executors of my estate pass the copy of the book to Michael then the trust is constituted and Michael will hold the book on trust for my nephew

¹ Methods of transferring property to constitute a trust and perfect a gift will be considered in the subsequent chapter on constitution of trusts.

² This is because generally the beneficiary and trustee are volunteers, they have not provided valuable consideration for the creation of the trust and, as equity will not assist a volunteer, they cannot enforce the trust until it is constituted. If consideration has been given, so there is a contract to create the trust then it may be possible to force the settlor to create the trust. These issues are considered in the chapter on constitution.

³ If there is no evidence of the intention of a transferor of property, then equity presumes that they would wish their property returned to them at some point and so presumes a resulting trust—the transferee holds the property on trust for the transferor. See chapters on resulting trusts.

to receive when he is a qualified lawyer. Later chapters will explain what happens if Michael refuses to take the book or my nephew does not become a lawyer.

The process of creating a trust thus seems quite straightforward: to create an express trust there must be:

- (1) a valid declaration of trust; and
- (2) valid constitution of the trust.

However, because the settlor should lose all interest in the trust property when the trust is constituted, and the trust obligation is such an onerous burden for the trustee, and the rights of a beneficiary of a trust may be so powerful, equity will only recognise and enforce an express trust if the declaration of trust contains certain elements and the trust has been completely constituted. Thus a more detailed explanation of what equity requires for a valid and enforceable express declaration of trust would be: A valid and enforceable express trust is created when a *capable settlor* makes a *declaration of trust*, complying with any required *formalities* and the *law*, imposing a *certain trust obligation* on a *capable trustee* to hold legal title to *certain property* for the benefit of *certain beneficiaries and potential objects, constituted by the transfer of legal title* of the certain property to the trustee.

Thus the elements of a valid and enforceable express trust are:

- (1) declaration;
- (2) formalities;
- (3) legality;
- (4) capacity;
- (5) certainty of intention;
- (6) certainty of subject;
- (7) certainty of object and beneficiary principle; and
- (8) constitution.

5.2 DECLARATION OF TRUST AND FORMALITIES

An express trust may be created with very little formality. A trust may be created by spoken words or in writing. A written declaration of trust is referred to as the trust instrument. Trust instruments may be *inter vivos*, written by a settlor to give effect to a trust between the living, or testamentary, written in a will to create a trust after the testator's death. Trust instruments may thus be in simple written form, on a scrap of paper or in a more formal form such as a deed, when they are usually referred to as "deed trusts".⁴ Trusts may also be declared in a settlement of property, a "settlement trust" (ST) or in a will, a "will trust".

In rare circumstances a trust even may be implied from the actions of the settlor. For example in *Re Kayford Ltd*,⁵ the court implied a trust from the actions of the insolvent company. The company had created a separate account for its customer pre-payments

⁴ A deed is a document that states it is a deed and must be signed by all parties, witnessed and delivered. If it is on behalf of a company, it must have the company seal attached: Companies Ordinance (Cap.622) s.121.

⁵ [1975] 1 WLR 279.

which it called the "customers' trust deposit account" and only transferred money from this account to its main account when it had sent the goods. The court held that the segregation of the money in a customer account with this title implied a declaration of trust evidencing an intention to place itself under a trust obligation.

The declaration of trust must evidence the three certainties:

- (1) *Certainty of intention* that the settlor intended the recipient of the property to receive the property under a trust obligation and nothing else.
- (2) *Certainty of subject matter*: the declaration must identify the property to be subject to the trust obligation.
- (3) *Certainty of object*: the declaration must identify, or provide the means to identify the beneficiaries of the trust.

There are also negative requirements for the declaration as it must not evidence any illegal purpose or purpose contrary to public policy, eg, a trust that is to encourage crime or that will continue forever. These are restrictions on the purposes of trusts which are discussed below.

The declaration of trust may also have to comply with requirements as to its form in certain circumstances to be valid. Formalities are requirements as to the method or manner of an action which must be complied with for the action to be valid and enforceable. Thus formalities of declaration are the specified requirements that must be complied with to make the declaration recognised as effective. The constitution of a trust may also be subject to formality requirements depending on the type of property forming the subject matter of the trust.⁶ At common law there are no formalities required for the valid declaration of a trust. Formalities are only required by statute and usually involve that most precious of commodities—land.⁷ Formalities are required for declarations of trusts of land because land is so important to society. Formalities are required because it is so easy to create a trust that society considers it necessary to focus the settlor's mind on the consequence of his actions.⁸ Formalities also provide evidence that a trust has been declared if there is a subsequent dispute.⁹

For *inter vivos* declarations of trust formalities are only required for declarations of trusts of land or disposals of equitable interests in land. Formalities are not required for *inter vivos* declarations of trust of personal property. All testamentary trusts as with any testamentary disposals of property are subject to the formalities required for the creation of a valid will and this applies to any form of property—land or personal.

⁶ For example, legal title in land must be conveyed by deed: s.4 of the Conveyancing and Property Ordinance (CPO). Formalities for constituting a trust will be dealt with in the chapter on constitution.

⁷ Formalities were only introduced for declarations of trusts of land in the Statute of Frauds 1677, "which distinguished sharply between express and constructive trusts": Paul Matthews, "The Words Which Are Not There: A Partial History of the Constructive Trust" in Charles Mitchell (ed), *Constructive and Resulting Trusts* (Hart Publishing, 2009) p.8. Land is defined in the CPO s.2: "land" includes—land covered by water; any estate, right, interest or easement in or over any land; the whole or part of an undivided share in land and any estate, right, interest or easement in or over the whole or part of an undivided share in land; and things attached to land or permanently fastened to anything attached to land.

⁸ Fuller considers formalities a cautionary factor making sure people do not rush into legal relationships without thinking of the consequences: Lon L Fuller, "Consideration and Form" (1941) 41 *Columbia Law Review* 799.

⁹ Austin noted that formalities perform many functions at law but the most important are as evidence that the relationship exists: John Austin, "Fragments—On Contracts" in R Campbell (ed), *Lectures on Jurisprudence, or The Philosophy of Positive Law* (London: John Murray, 1879; reprint, Bristol: Thoemmes Press, 4th rev ed., 2 Vols., 2002).

Formalities for the declaration of trusts thus apply to:¹⁰

- (1) Declarations of trusts of land: s.5(1)(b) of the CPO (Cap.219).
- (2) Dispositions of the equitable interest in a trust of land: s.5(1)(a) of the CPO.
- (3) A testamentary declaration of trust: s.5 of the Wills Ordinance (Cap.30).

5.2.1 Formalities for the declaration of an *inter vivos* trust of land

To declare a valid trust of land the declaration must comply with s.5(1)(b) of the CPO: "a declaration of trust respecting land or any interest therein *shall be manifested and proved in writing* signed by the person who is able to declare such trust or by his will".¹¹ (Emphasis added.)

Thus the formality requirement:

- (1) applies only to a declaration of a trust of land;
- (2) does not have to be declared in writing but "shall be manifested and proved" in writing. Thus later writing could satisfy this;
- (3) requires that the settlor must sign the proving document himself. An agent cannot.

The formality requirement will apply to any declaration of a trust or sub-trust of land. A trust may involve the legal owner transferring legal ownership to the trustee subject to the trust obligation to hold the property on trust for the beneficiary. It can also involve the legal owner declaring himself trustee of his own property, which he then holds subject to the trust obligation for the benefit of the beneficiary. In both cases if the property is land then s.5(1)(b) of the CPO applies.

$\Rightarrow S \rightarrow \frac{T}{B} \rightarrow$ Settlor transfers property to trustee to hold for beneficiary.

$S \rightarrow \frac{T(S)}{B} \rightarrow$ Settlor declares himself trustee and then holds his property for the beneficiary.

A declaration of sub-trust involves the beneficiary of a trust of declaring a trust of his beneficial interest in favour of another. The first beneficial owner now holds the equitable interest on trust for the new beneficiary. Thus there is already a trust and the beneficiary (B1) now declares he holds his beneficial interest on trust for someone else (B2).

$$\frac{T}{B1} \rightarrow \frac{T}{B2}$$

¹⁰ Further important formalities requirements are contained in the CPO for the constitution of a trust: s.4 CPO requires a conveyance of land to be by deed, and s.3(1) CPO:

"Subject to section 6(2), no action shall be brought upon any contract for the sale or other disposition of land unless the agreement upon which such action is brought, or some memorandum or note thereof, is in writing and signed by the party to be charged or by some other person lawfully authorized by him for that purpose."

In relation to s.3(1), CPO ignore references in English textbooks to s.2 of the Law of Property (Miscellaneous Provisions) Act 1989 which only applies in the United Kingdom.

¹¹ Note this is very similar to the English provision in s.53(1)(b) of the Law of Property Act 1925 (LPA 1925).

The trustee of the original trust is still the same but the beneficiary of this original trust (B1) is now trustee of his beneficial interest for the benefit of B2. Again, if the property is land then s.5(1)(b) of the CPO applies. To be enforceable the declaration of sub-trust must be manifested and proved in writing. It is important to distinguish the declaration of a sub-trust from a disposition of the equitable interest. The disposition of an equitable interest is the disposal, usually by sale or gift, of the beneficiary's beneficial interest in a trust; this is considered below as it may be subject to different, more stringent formality requirements.

If a declaration of a trust or sub-trust of land is made without complying with the formalities in s.5(1)(b) of the CPO, ie, it is not evidenced in writing, the trust is valid but unenforceable.¹² Thus, if the trustee carries out his obligations he will be fulfilling a valid trust and no one may challenge his actions,¹³ but if he does not the beneficiary cannot enforce the trust. However, the formality requirements do not apply to resulting, implied or constructive trusts because of s.5(2) of the CPO, which provides: "This section does not affect the creation or operation of resulting, implied or constructive trusts."¹⁴ Thus a court may recognise an implied trust even though it does not comply with the formalities required in the preceding provisions.¹⁵

The problem with formalities is that not everyone is aware of them and so insisting on formalities may cause injustice, as a settlor may have transferred land to a trustee making an oral declaration of trust which is unenforceable. The common law regards the transfer of legal title as transfer of ownership, thus the trustee is looked on as the legal owner. If the beneficiary cannot enforce the trust against the trustee because of the lack of formality in the declaration then the trustee will enjoy the property without the trust obligations. Of course, equity has always had more regard to the intentions of the parties than formality, *equity looks to the intent rather than the form*, and this was one of the reasons for the emergence of equity and the divergence of equity from the common law's insistence on formality. A maxim or method of statutory interpretation was thus developed by equity to deal with such situations—*equity will not permit a statute to be used as an instrument of fraud*.¹⁶ Thus if a defendant seeks to rely (or hide behind) on formality requirements in a statute to perpetuate a fraud, equity will not permit the fraud to be achieved by the use of the statutory provision.

Rochefoucauld v Boustead

[1897] 1 Ch 196

The *Comtesse de la Rochefoucauld* owned the Delmar Estates, which were large coffee plantations in Ceylon, subject to mortgage. She agreed that Boustead would purchase the plantations from the mortgagee, which had a power of sale, and that he would hold the plantations on trust for her. Boustead did purchase the plantations, but rather than act as trustee he treated them as his own. He mortgaged them and was eventually declared bankrupt. The *Comtesse* had not paid particular attention to the plantations or the trust, but

¹² *Gardner v Rowe* (1828) 5 Russ 258, 38 ER 1024.

¹³ This may seem of little value, but, as we shall see in the chapter on trustees, it is very important that a trustee has the power to carry out an action as he may attract personal liability if he carries out an action which is not valid.

¹⁴ Identical to s.53(2) LPA 1925.

¹⁵ See *Hodgson v Marks* [1971] Ch 892, discussed below.

¹⁶ Sometimes phrased as equity will not be used as an engine of fraud: *Wong Wing Tao v Wong Wai Keung* (HCA 1213/2002, [2003] HKEC 441), [11].

was now sufficiently aware to seek recognition of the trust so that the plantations would not be used to settle Boustead's obligations in bankruptcy. However, the declaration of trust was oral only and did not comply with s.7 of the Statute of Frauds 1677, the predecessor to s.53 (1)(b) of the Law of Property Act (LPA) 1925 in the UK and s.5 (1)(b) of the CPO in Hong Kong, which required that any trust of land must be evidenced in writing. The parol agreement between the Comtesse and Boustead that he would purchase the property from the mortgagee and hold it for her benefit amounted to a declaration of trust. There was no written evidence of the trust and so Boustead argued that the trust was unenforceable.

Judgment:

The court held that the Statute of Frauds 1677 was intended to prevent fraud when trusts of land were created. To allow the defendant to use a statute that had been intended to prevent fraud to perpetuate a fraud was unconscionable. Applying the maxim *equity will not permit a statute to be used as an instrument of fraud* the court allowed oral evidence to be admitted to prove the existence of the trust. The plantations were held by Boustead on trust for the Comtesse and did not form part of his property on bankruptcy. Lindley LJ said:¹⁷

"It is further established by a series of cases, the propriety of which cannot now be questioned, that the Statute of Frauds does not prevent the proof of a fraud; and that it is a fraud on the part of a person to whom land is conveyed as a trustee, and who knows that it was so conveyed to deny the trust and claim the land himself. Consequently, notwithstanding the statute, it is competent for a person claiming the land conveyed to another to prove by parol evidence that it was so conveyed upon trust for the claimant; and that the grantee, knowing the facts, is denying the trust and relying upon the form of conveyance and the statute, in order to keep the land himself."

The court clearly enforced the express trust which had been declared informally by the Comtesse thus ignoring the statutory provision. This was undoubtedly just, as the rogue Boustead should not have been allowed to profit from his fraud. However foolish the Comtesse's actions, but this does not sit comfortably with the constitutional principle of parliamentary sovereignty in Britain. The common law has generally developed in the eighteenth and nineteenth centuries to accept that courts must follow statute above the common law. Thus there are constitutional problems whenever a court disregards or at least seems to disregard a statute and this is in effect what the court was doing when it gave justice to the Comtesse.¹⁸ However, Gregory Allan has considered this case in depth

¹⁷ *Rochefoucauld v Boustead* [1897] 1 Ch 196, 206.

¹⁸ See RP Meagher, JD Heydon and MJ Leeming, *Meagher, Gummow and Lehane's Equity Doctrines & Remedies* (LexisNexis Butterworths, 4th ed., 2002) paras.12–130, where the authors conclude that the doctrine in *Rochefoucauld v Boustead* involves:

"a blunt refusal to follow legislation which in its terms applies to the facts at hand; this is no less than the exercise by equity of a suspending or dispensing power denied the executive branch of government since the Bill of Rights 1689".

For argument against a resulting trust being available in this context, see William Swadling, "A Hard Look at *Hodgson v Marks*" in Peter Birks and Francis Rose (eds), *Restitution and Equity Volume One: Resulting Trusts and Equitable Compensation* (Mansfield Press, 2000).

and analysed the judgments preceding and following this case and has identified that, although Lindley LJ would never have considered the trust he enforced a constructive trust, because of the changes effected by the LPA 1925, the trust which was enforced in this case would now no longer be classified as an express trust but would be regarded as a species of constructive trust.¹⁹ Thus there would be no constitutional issues. However, the constitutional implications of enforcing such trusts were again considered when similar circumstances arose in *Hodgson v Marks*.

Hodgson v Marks

[1971] Ch 892

Mrs Hodgson, an 83-year-old lady, had taken Mr Evans as a lodger. Eventually she looked on Evans as a "man of substance", she trusted him and allowed him to manage her business affairs. She had a nephew who was to inherit her house and who did not like Evans. Mrs Hodgson and Evans were concerned that the nephew would eject Evans from the house. Therefore Mrs Hodgson agreed to transfer the legal interest in the property to Evans and Evans agreed to look after the house for her benefit. The house was to be held on trust for Mrs Hodgson by the lodger Evans but there was no evidence of this in writing. Sometime after the house was conveyed to Evans he sold the house to Mr Marks. Marks had seen Mrs Hodgson when he visited the house and knew that a woman lived in one bedroom. Marks mortgaged the house and the mortgagee registered a charge against the property. After almost a year Mrs Hodgson eventually discovered that the house had been sold and mortgaged. She sought an order from the court that Evans had held the house on trust for her and that her interests overrode the sale of the house and the subsequent charge. The purchaser and mortgage company argued that if there were a trust it did not comply with the equivalent of s.5(1)(b) of the CPO and thus was unenforceable.

Judgment:

The Court of Appeal held that there was a trust and that Mrs Hodgson's interests overrode the purchaser's and the mortgagee's. Although the Court approved the decision in *Rochefoucauld v Boustead*, the reasoning of the present decision was quite different. In *Rochefoucauld v Boustead* the court had stated, "the trust which the plaintiff has established is clearly an express trust..." In *Hodgson v Marks* the Court said that the trust was a resulting trust, as the transfer of legal title had been gratuitous and it should always be presumed that Mrs Hodgson had intended that the equitable interest remain with her. As this was a resulting trust, the English equivalent of s.5(2) of the CPO expressly provided that resulting, implied and constructive trusts need not comply with the formality requirements. Thus the Court avoided the unfortunate constitutional implications of ignoring a statute.

In Hong Kong, *Hodgson v Marks* was followed by the CA in the case sometimes referred to as "the mini-bus driver's case".

¹⁹ Gregory Allan, "Ceylon Coffee, the Comtesse and the Consignee: A Historical Reappraisal of *Rochefoucauld v Boustead*" (2015) 36(1) *The Journal of Legal History* 43.

Wong Chim Ying v Cheng Kam Wing

[1991] 2 HKLR 253

A husband and wife moved in with the wife's mother when they married. After a short time the husband and wife's quarrels had become such that the mother asked them to leave the flat. The husband and wife decided to search for a flat of their own. The husband asked the wife to do this as he worked all day as a public light bus driver. The husband told the wife of a flat that might be suitable and they viewed it together. The wife liked the flat and the husband paid a small deposit to retain it. The husband transferred his savings of \$25,500 to the wife's bank account. The purchase price of the flat was some \$45,000. The wife negotiated loans from family members for the balance of the purchase price. The flat was purchased but the wife dealt with all the paperwork as the husband was too busy working. The flat was conveyed into the sole name of the wife. The husband, wife and their children lived in the flat for some years. The wife sold the flat for \$305,000 and arranged with the purchaser to remain in occupation for two months after purchase so that she could find new accommodation at licence fee of \$2,500 per month. The wife absconded two days after completion of the conveyance with \$300,000 of the purchase price. The purchaser sought possession from the husband but the husband refused to vacate. The husband claimed that the wife had never returned to her work as a wigmaker after marriage and had never contributed to the property. He had provided all the purchase monies and his wages, which he handed over to the wife every week, had been used to repay the family loans. The flat had only been conveyed into the wife's sole name for administrative convenience and was intended as a family home. Therefore he had an interest by way of resulting trust in the property and the purchaser had notice of his occupation of the flat and so was bound by this interest.

Judgment:

The CA held that the husband was the sole beneficial owner of the property by way of resulting trust. The presumption of advancement as between husband and wife did not arise because of the clear purpose behind the purchase in the wife's sole name. The purchaser had actual notice of his occupation and had not enquired as to whether or not he had any legal or equitable interest in it. Clough JA explained that, "The principle is that notice of occupation is notice of the occupier's rights."²⁰ As a result, the purchaser had constructive notice of the husband's beneficial ownership. The purchaser held the property on trust for the husband and had to transfer the title into his name.

In contrast an earlier English decision, *Bannister v Bannister*, had dealt with a similar problem by declaring that there was a constructive trust.

Bannister v Bannister

[1948] 2 All ER 133

When the defendant's husband died she inherited two cottages from him, one of which they had lived in. The deceased husband's brother, the plaintiff, negotiated with her to sell him

the two cottages. The cottages were worth about £400 but the defendant sold them to her brother-in law for £250 because he agreed to let her stay rent free in one of the cottages for life. When the sale was complete, the plaintiff sought possession of both cottages. The defendant claimed there was a trust but there was no writing evidencing this.

Judgment:

Although there was no question of fraud, the brother-in-law had not intended to take possession but had fallen out with his sister-in-law after the purchase, the court held that the plaintiff's conscience was affected by his promise and so he held the cottage on constructive trust for the defendant for her life. Again this neatly sidestepped the statutory requirements because of the English equivalent of s.5(2) of the CPO.

Thus courts will not allow the formalities required by statute to prevent fraud to be used to carry out fraud. However, although the decision in *Rochefoucauld v Boustead* is still good law it seems more likely that a court would consider either a resulting or constructive trust interpretation and s.5(2) of the CPO as preferable to just ignoring s.5(1)(b) of the CPO.²¹

5.2.2 Formalities for the disposal of an equitable interest in land

Formality is also required if the beneficial interest of a beneficiary is disposed of. As mentioned above the commonest dispositions are the sale or gift of the beneficial interest. This should be distinguished from the declaration of a sub-trust of a beneficial interest as described above. Thus, if a trust has been created the beneficiary may sell or gift his beneficial interest.

$$\frac{T}{B1} \rightarrow \frac{T}{B2}$$

In this example the beneficiary of the original trust (B1) may sell or give his beneficial interest in the trust to another (B2). The trustee remains the same, all that changes is the identity of the beneficiary on whose behalf the trustee holds the property, the original beneficiary should instruct the trustee that he now holds the property on behalf of B2. Sale may happen because a beneficiary's interest will not realise for some time and he wishes to sell his interest and so receive funds now. Gifts of beneficial interest often happen because parents are beneficiaries of family trusts and wish to give the interest to their children or grandchildren.

In *Timpson's Executors v Yerbury (Inspector of Taxes)*,²² Romer LJ identified four ways in which a beneficiary could dispose of his equitable interest in a trust in favour of a third party, the beneficiary:

1. "can assign it to the third party directly;
2. can direct the trustees to hold the property in trust for the third party...;
3. can contract for valuable consideration to assign the equitable interest to him; or
4. can declare himself to be a trustee for him of such interest".

²¹ Although in *Heng Kwai Shan v Heng Hock Shan* [1983] 1 HKC 335 it was confirmed that unwritten trusts of land would be enforced as in *Rochefoucauld v Boustead* and *Bannister v Bannister*.

²² [1936] 1 KB 645, 664. Confirmed in *Zeital v Kaye* [2010] WTLR 913.

A beneficiary may refuse to accept his beneficial interest in a trust; this is known as disclaiming his interest. If a beneficiary disclaims his interest before he has accepted it then this will not be a disposition of the interest;²³ however if he accepts the interest and then attempts to disclaim it this will be a disposition.

In Hong Kong, any disposition of an equitable interest in a trust of land must comply with s.5(1)(a) of the CPO:

"No *equitable interest in land* can be created or disposed of *except in writing* signed by the person creating or disposing of the same, or by his agent thereunto lawfully authorised in writing, or by will, or by operation of law." (Emphasis added.)

Thus the formality requirement:

- (1) applies only to disposals of an equitable interest in land;²⁴
- (2) provides that the disposition must be in writing,²⁵ thus later writing cannot effect the transfer retrospectively; and
- (3) can be signed by the owner or by an authorised agent (with written authority).

Thus to comply with the provision the beneficiary must instruct his trustee in writing to hold the beneficial interests for the new donee or beneficiary. If there is a failure to comply with the formality the disposition is void—it has not happened.²⁶ The reasoning behind the formality requirement is to allow the trustee, the court and the tax authorities to easily trace who is the beneficial owner of the trust property. If dispositions of equitable interests in land could be made informally it would be very difficult to establish the identity of the beneficial owner and so consequently who the trustee held the trust property for, whose rights the court could enforce, and who the taxman could tax.

The tax authorities have been most concerned about dispositions of the equitable interest in trusts, as transfers of ownership of certain property may attract taxation by stamp duty. In the UK particular importance has been dispositions of equitable interest in trusts of shares and most of the important cases involve attempts to avoid stamp duty on transfer of the beneficial interest in shares.²⁷ This formality does not apply in Hong Kong, as s.5(1)(a) of the CPO is limited to equitable interests in land. In England and Wales any disposition of an equitable interest in any trust must comply with s.53(1)(c) of the LPA 1925:

"a disposition of an equitable interest or trust subsisting at the time of the disposition, must be in writing signed by the person disposing of the same, or by his agent thereto lawfully authorised in writing or by will".

²³ *Re Paradise Motor Co Ltd* [1968] 1 WLR 1125.

²⁴ Thus, an equitable interest in any other property may be disposed of without a signed written instrument: *Yung Shu Wu v Vivienne Sung Wu* (2011) 14 HKCFAR 39.

²⁵ Although the writing does not have to be in the form of a deed; *Town Bright Industries Ltd v Bermuda Trusts (Hong Kong) Ltd* [1998] 2 HKC 445.

²⁶ Section 53(1)(C) of the LPA 1925 and s.5(1)(a) of the CPO are based upon s.9 of the Statute of Frauds 1677, which stated that unwritten dispositions "shall be utterly void and of no effect".

²⁷ The cases which involve the English provision, such as *Grey v Inland Revenue Commissioners* [1960] AC 1, *Vandervell v Inland Revenue Commissioners* [1967] 2 AC 291, *Re Vandervell's Trusts (No 2)* [1974] Ch 269, *Oughtred v Inland Revenue Commissioners* [1960] AC 206 and *Neville v Wilson* [1997] Ch 144, are only relevant in Hong Kong when considering what constitutes a disposition.

Thus the formality requirement:

- (1) applies to the disposition of any equitable interest no matter what the subject matter;
- (2) provides that the disposition must be in writing. Later writing cannot effect the transfer retrospectively; and
- (3) can be signed by the owner or by an authorised agent (with written authority).

If there is a failure to comply with the formality requirement the disposition is void—it has not happened.

Stamp duty is charged on written instruments in certain cases, therefore the writing requirements of s.53(1)(c) of the LPA 1925 may attract taxation. In Hong Kong these cases are only useful for considering what constitutes a disposition for the purposes of s.5(1)(a) of the CPO. These cases involve complicated financial transactions as they are undertaken by wealthy people, with expert financial and legal advice, and may have been intended to confuse the tax authorities.

Grey v Inland Revenue Commissioners

[1960] AC 1

Grey was a nominee of 18,000 shares, he held legal title to the shares on behalf of Mr Hunter. Hunter wished to transfer his beneficial interest to his six grandchildren; however if he complied with s.53(1)(c) of the LPA 1925 and did this in writing then the written instrument would be liable to *ad valorem* stamp duty. Therefore Hunter orally directed Grey to divide the beneficial interest into 6 parts of 3,000 shares each and hold these on separate trusts for his 6 grandchildren. Deeds of transfer were only completed subsequent to the oral direction by Grey and the other nominees. H claimed that the oral direction had transferred the equitable interest and so the transfer did not attract stamp duty. The Inland Revenue claimed that the oral declaration was not effective as it did not comply with s.53(1)(c). Therefore the disposition took effect only when the deeds were executed and these were liable to stamp duty.

Judgment:

As the oral direction did not comply with s.53(1)(c) of the LPA 1925 it was void. The transfer only occurred when the deeds were executed and so these were liable to stamp duty.

Grey seems quite straightforward, an oral direction to transfer the beneficial interests will be void because it does not comply with s.53(1)(C) and so does not take effect, but a deed executed to transfer the beneficial interests will satisfy s.53(1)(c) and be effective. More complicated is the case where parties attempt to take advantage of s.53(2) by claiming a resulting, implied or constructive trust.

Oughtred v Inland Revenue Commissioners

[1960] AC 206

This was another attempt to avoid stamp duty. Mrs Oughtred held 72,000 shares in a private company absolutely. There was also a trust in which trustees held 200,000 shares in the

company for Mrs Oughtred for life, with remainder to her son, Peter. Mrs Oughtred and her son entered into an oral contract by which Peter would forfeit his remainder interest in the 200,000 shares so that Mrs Oughtred would be absolutely entitled to them. In return Mrs Oughtred would transfer her 72,000 shares to the trustees to hold on bare trust for Peter. Thus Mrs Oughtred would have 200,000 shares absolutely and Peter would have 72,000 shares absolutely, the arrangement was beneficial for both. The problem was that *ad valorem* stamp duty was payable on "transfer on sale" of shares.²⁸

Subsequently a deed releasing Peter's life interest in the 200,000 shares and transferring legal title to the 200,000 shares to Mrs Oughtred was executed. The Inland Revenue argued that the oral contract could not transfer the beneficial interest in the shares because of s.53(1)(c) of the LPA 1925. Any transfer of the beneficial interest by this oral contract was void, thus the deed transferred the beneficial interest and attracted stamp duty. Mrs Oughtred argued that as the oral contract was for the transfer of shares in a private company, shares which are not available on the open market, it was specifically enforceable. With a specifically enforceable contract the transferor holds the beneficial interest in the property on constructive trust for the transferee. If the interest was held on constructive trust then s.53(2) of the LPA 1925 provides that the preceding formality requirements do not apply and the transfer did not have to be in writing. Thus there was no document to attract stamp duty. The later deed merely transferred bare legal title and so had little value for stamp duty.

Judgment:

The House of Lords held, by a 3:2 majority,²⁹ that the oral contract was void because it did not comply with the formality requirements. Thus the purchaser of the shares would only get the beneficial interest when the formal transfer took place and so stamp duty was payable on the full value of the transfer.

The argument in favour of the constructive trust was quite strong and was later applied in *Neville v Wilson*,³⁰ discussed below, although the circumstances of that case differ from those of *Oughtred v Inland Revenue Commissioners*.

The situation is also complicated if the beneficial interest is in a bare trust, this is a trust where the trustees are merely nominees for the beneficiary and have few trust duties apart from holding the property for the beneficiary. In effect the beneficiary may have control over the legal as well as beneficial interest.

Vandervell v Inland Revenue Commissioners

[1967] 2 AC 291

Vandervell wanted to donate £150,000 to the Royal College of Surgeons (RCS) to endow a professorship in pharmacology. His bank held 100,000 shares in his company for him on bare trust as nominees. Vandervell decided to pay the money to the RCS in dividends and

also avoid tax. Vandervell orally directed his bank (trustees) to transfer to the RCS both the legal estate (held by the bank) and the beneficial interest in the shares (held by Vandervell). The proposal was that subsequently a dividend of £150,000 would be declared on the shares, and no tax would be payable as the RCS is a charity. To ensure that the RCS would return the shares an option to re-purchase the shares once the dividend had been granted was included in the agreement in favour of Vandervell Trustees Ltd (VTL). VTL was intended to hold the shares on trust for beneficiaries to be nominated by Vandervell in the future—but he did not nominate beneficiaries at this time. Vandervell hoped to divest himself of any beneficial interest in the shares and therefore avoid surtax on the dividends. The Inland Revenue claimed that Vandervell was liable to pay the tax as the oral direction to transfer legal and equitable title to the shares was a disposition for the purposes of s.53(1)(c) of the LPA 1925 and so void. Thus Vandervell still held the beneficial interest in the shares and was liable to the surtax on the dividend.

Judgment:

The House of Lords held that, as V was the solely entitled beneficial owner under a bare trust, he was entitled to direct the trustees to divest both the legal and equitable interest in the shares. When this was done the equitable interest was extinguished and so s.53(1)(c) of the LPA 1925 did not apply. However, the option to buy back the shares was held by VTL and, as no beneficiary had been elected for this interest, the beneficial interest in the shares remained with Vandervell by way of resulting trust. Thus Vandervell still had an interest in the shares and was liable to surtax. As noted by Lord Wilberforce:

"The conclusion on the facts found, is simply that the option was vested in the trustee company as a trustee on trusts, not defined at the time, possibly to be defined later. But the equitable, or beneficial interest, cannot remain in the air: the consequence in law must be that it remains in the settlor."

Mr Vandervell's interests were subject to oral disposition but the resulting trust of the option meant that he had not completely divested himself of all interest in the shares. He tried to exercise the option in favour of his children to get rid of any interest but this again resulted in litigation.

Re Vandervell's Trusts (No 2)

[1974] Ch 269

Vandervell was still trying to divest himself of his beneficial interest in the shares. In 1961 Vandervell ordered the trustees of Vandervell Trustees Limited (VTL) to exercise the option on the shares and buy them back from the Royal College of Surgeons using money held on trust for Vandervell's children. This should have ensured that the beneficial interest in the shares would be held by the children and the legal title held by VTL. Therefore Vandervell could have no interest in the shares. VTL's solicitors wrote to the Inland Revenue informing them that the shares were held beneficially for the children's trusts. Between 1962 and 1964 the company paid dividends on the shares which Vandervell allowed to be added to the children's settlements. The Revenue still claimed that Vandervell had not divested himself of the interest on the shares and so in 1965 Vandervell executed a deed transferring any

²⁸ Stamp duty was payable on a transfer on sale of property: Stamp Act 1891 (c 39), s.54.

²⁹ Lord Radcliffe giving a particularly persuasive dissenting judgment, arguing that the beneficial interest in shares in a private company passed if there was a specifically enforceable contract. This was followed by the CA in *Neville v Wilson* [1997] Ch 144.

³⁰ *Ibid.*

interest he may have had in the shares to the children's trusts. Vandervell died in 1967 and his executors took action against VTL to recover the dividends paid between 1962 and 1964 as part of his estate.

Judgment:

The executors failed in their action as the transfer to the children's trust had occurred when Vandervell directed the trustees to exercise the option as this was under his direction and used the children's funds. The resulting trust of the option in his favour had come to an end at this point. Lord Denning MR noted:

"A resulting trust for the settlor is born and dies without any writing at all. It comes into existence whenever there is a gap in the beneficial ownership. It ceases to exist whenever that gap is filled by someone becoming beneficially entitled. As soon as the gap is filled by the creation or declaration of a valid trust, the resulting trust comes to an end."

Section 53(1)(c) of the LPA 1925 did not apply as this was a new declaration of trust and involved shares not land, therefore it was also not covered by s.53(1)(b) of the LPA 1925.

The English CA had to consider the issue of specifically enforceable contracts and constructive trusts as regards s.53(1)(c) of the LPA 1925.

Neville v Wilson

[1997] Ch 144

Trustees (nominees) held shares in U Ltd on trust for N Ltd (beneficiary). N Ltd was liquidated. The shareholders of N Ltd orally agreed to distribute the beneficial interests in the shares in U Ltd, which N Ltd owned beneficially, amongst each other. The court had to decide whether s.53(1)(c) invalidated the oral agreement to distribute the beneficial interest in the shares in U Ltd. If it did invalidate the agreement, the shares would have no beneficial owner, and would thus pass to the Crown on the principle of *bona vacantia*.

Judgment:

The oral agreement gave rise to a constructive trust in favour of the shareholders of N Ltd. Therefore s.53(1)(c) did not apply because of s.53(2). Therefore the disposition of the equitable interest did not have to be in writing and the agreement was valid. This follows the argument put forward on behalf of Mrs Oughtred, in *Oughtred v Inland Revenue Commissioners*, that her oral agreement with her son to exchange interests in shares in a private company was specifically enforceable and thus gave rise to a constructive trust. This had been the dissenting judgment of Lord Radcliffe in *Oughtred v Inland Revenue Commissioners*. Of course the circumstances of Oughtred are very different to Neville, as in the former the court was asked to decide whether Mrs Oughtred and her son had avoided taxation, whereas in the latter the court had to decide between the shareholders receiving the benefit or it going *bona vacantia* to the state. Whatever the outcome of a case however, the legal principles should be consistent.

These decisions have been much criticised by academics as showing little coherent reasoning about the nature of a disposition. This may be because they are tax cases and there is a tendency for the courts to interpret legislation in favour of the tax authorities on the principle that the legislature would not intend its legislation to be used to avoid taxation.

Thus whenever a transaction occurs which involves a beneficial interest the parties should be wary of falling foul of s.53(1)(C) of the LPA 1925, unless of course it is a deliberate attempt to avoid the writing requirement in order to avoid taxation.

5.2.3 Formalities for the creation of a valid testamentary trust

All declarations of testamentary trusts must comply with s.5 of the Wills Ordinance, the most important elements of which provide that a will shall be valid only if it is in writing, signed by the testator or by some other person in his presence and by his direction and the signature is witnessed by two or more witnesses.³¹ These formality requirements apply to all forms of property.

If a testamentary disposition does not comply with these formalities, for example it is not in writing or is not witnessed, it will be void. However, as we shall see equity will sometimes enforce testamentary trusts known as secret trusts even though they are not in writing in the will.

5.3 CAPACITY OF SETTLORS, TRUSTEES AND BENEFICIARIES

Capacity here refers to legal capacity, being legally able to do something. Everyone is presumed to be capable unless it is established otherwise.³² Thus it is the burden of the party seeking to establish they were not capable, or those they are acting for were not capable, to establish they were minors at the time of the transaction or acting under some legal incapacity. Some people are not recognised as having legal capacity, for example the mentally ill or minors, this is for their protection. The law will not automatically recognise some actions of these people so that they do not enter into transactions that they do not understand or do not intend. These restrictions on capacity are usually provided in statute.

Minors are those under the age of 18 years.³³ There are no restrictions on minors holding the legal estate in land in Hong Kong, although the minor may not have the capacity to deal with land during his minority. When a minor attempts to settle personalty, then the trust will be voidable at the instance of the minor at any time within a reasonable time of his attaining majority. A minor may not make a will;³⁴ therefore a minor cannot create a trust by will.

Those adjudged to be suffering from a mental illness,³⁵ or suffering from some other form of mental incapacity which means they are incapable of understanding what they are doing, are considered to have no capacity to contract, execute deeds, make dispositions or

³¹ This is almost identical to the UK Wills Act 1837, s.9.

³² The default presumption about capacity with regard to property transaction is provided in s.22 of the CPO: A party to any instrument shall be presumed, until the contrary is proved, to have full legal capacity to execute that instrument, to bind himself in terms of that instrument and to dispose of or hold any property or rights assigned under that instrument.

³³ Age of Majority (Related Provisions) Ordinance (Cap.410) s.2.

³⁴ Wills Ordinance (Cap.30) s.4.

³⁵ As defined in the Mental Health Ordinance (Cap.136).

manage their affairs. The court may administer the affairs of the mentally ill and make wills for them.³⁶

The parties to a trust have varying requirements as to capacity:

- Settlor:** Only a capable settlor or testator can make a valid declaration of trust. Generally anyone who is capable of owning property may settle it. Challenges to wills are often made on the grounds that the testator was not of sound mind when they made the will, so that they did not know what they were doing and so were incapable of creating a valid will.³⁷ An artificial person, eg, a company, has legal capacity and so can be a settlor.
- Trustee:** Only a capable trustee can administer a trust. The trustee must be capable of dealing with the property otherwise the trust cannot be carried out. The trustee must be capable of having the legal estate transferred to him. In Hong Kong a trustee must be at least 21 years-old.³⁸ If a trustee becomes incapable of dealing with the property, perhaps through mental or physical illness, a new trustee can be appointed to aid or replace the original trustee. An artificial person, eg, a company, has legal capacity and so can be a trustee. In fact companies that are formed especially for trust management administer many trusts; these are referred to as "trust corporations".
- Beneficiaries:** Anyone can be the beneficiary of a trust and trusts are often set up to protect those who are incompetent and so incapable of owning or dealing with property, eg, the mentally ill and children. A company can be the beneficiary of a trust. A trust may even be created which, for a time, has no beneficiaries; for example, I leave the residue of my estate to my grandchildren (yet to be born).

5.4 THE THREE CERTAINTIES REQUIRED TO CREATE A VALID PRIVATE TRUST

The three certainties required to create a valid private trust are often ascribed to Lord Langdale's judgment in *Knight v Knight*,³⁹ but had been recognised and required for some years before this judgment. To create a valid express private trust the declaration of trust must evidence the three certainties:

- (1) *Certainty of intention*—the certainty of the intention of the settlor to place the transferee of property under a trust obligation.
- (2) *Certainty of subject*—the certainty of what property is the subject matter of the trust.
- (3) *Certainty of object*—the certainty or means of ascertaining who the beneficiaries of the trust are.

³⁶ *Ibid.*, s.10.

³⁷ Again the presumption from s.22 CPO is that everyone is capable but evidence may be brought to disprove this.

³⁸ Trustee Ordinance s.37 provides that a court may replace any trustee who is under 21 years of age and may only appoint trustees who are 21 years old or older.

³⁹ (1840) 3 Beav 148, 49 ER 58. Confirmed in *Hong Thai Citizens Travel Services Ltd v Hang Seng Bank Ltd* [1987] 3 HKC 565.

The three certainties will be dealt with in some detail in the next chapters but a brief overview will clarify the requirements for a valid declaration of an express private trust.

The declaration of trust must be a declaration of the intention to create a trust and nothing else. The obligation of trust upon the trustee is so onerous that a court will only uphold the trust and impose the obligation if it is certain the transferor of property intended the transferee to be under this trust obligation and the transfer was nothing else.

We have already seen that other arrangements may appear similar to a trust, for example a contract; however the obligations and rights of the parties are very different. Therefore, the court will need evidence that a trust was intended when property was transferred and nothing else.

Property can be transferred for various reasons:

- (1) It can be sold or swapped—that is transferred for consideration.
- (2) It can be a gift.
- (3) It can be a trust.
- (4) It can be a transfer subject to a power to allocate by the transferee or someone else.

To uphold the creation of a valid express trust the court must be satisfied that the transferor did not transfer the property for another reason. To do this the court will look at the circumstances surrounding the transfer and the construction of the instrument purported to be the trust instrument. If consideration were given for the transfer then the court will probably construe the transfer as a contract, although it may be a contract to create a trust. If no consideration is given then it is more likely to be a gift, trust or power. If a written instrument was used to transfer the property then the instrument's construction will be considered. If words were spoken the court will hear evidence of the words spoken—did the transferor say "I give you this property" or "I give you this property to hold on trust"? However, as we will see, there is no need to refer to a "trust" in the trust instrument to create a trust but there must be evidence that a trust obligation was intended.⁴⁰

A transfer of property without consideration in return may be a gift or property transferred on trust. A gift is a gratuitous transfer of property. Gifts are valid and upheld at common law and in equity. Generally all that is necessary for the valid gift of property is an intention by the transferor to "give" the property to the transferee coupled with the transfer of the property. With chattels transfer is usually by delivery. With land certain formalities have to be complied with—a conveyance of land must be in writing in the form of a deed.⁴¹

Equity presumes that a gratuitous transfer of property with no evidence of the reason behind the transfer will create a resulting trust (the presumed resulting trust⁴²). Equity presumes that the absolute owner of property will not transfer it to another without consideration in return. Thus the transferee holds the property on a resulting trust for the transferor. However, transfers of property between certain classes of persons are subject to the equitable presumption that they are gifts. This usually involves close family members and is known as the presumption of advancement: if a transfer of property occurs between

⁴⁰ *Paul v Constance* [1977] 1 WLR 527.

⁴¹ CPO s.4.

⁴² *Dyer v Dyer* (1788) 2 Cox Eq Cas 92, 30 ER 42, and see *Hodgson v Marks*, above.

because a party has not identified a beneficiary for a trust or who will own an interest in property even if they have successfully transferred the trust property to the trustee as *equity abhors a vacuum* and will return the property to the settlor to close the gap in beneficial ownership. Automatic resulting trusts may arise if a party has contributed to a collection for a purpose which cannot be carried out or has been successfully completed. The automatic resulting trust is also the accepted theory behind the recognition and enforcement of *Quistclose* trusts where lenders have lent money to borrowers for an agreed purpose and the purpose has not been carried out. The borrower is said to hold the borrowed money on resulting trust for the lender with a power to use the monies for the agreed purpose. The monies do not have to be segregated from the borrower's other funds to be subject to the *Quistclose* trust. The main consideration in establishing that loan monies are subject to a *Quistclose* trust is that both parties considered that the monies were not at the free disposal of the borrower but had to be used for the agreed purpose.

CONSTRUCTIVE TRUSTS

13.1 INTRODUCTION

FW Maitland, the celebrated 19th century legal historian and author of several texts on equity, noted it had been claimed there was "one grand rule" for constructive trusts that, "wherever a person clothed with a fiduciary character gains some personal advantage by availing himself of his situation as a trustee, he becomes a trustee of the advantage so gained".¹ Although it is very attractive to reduce the requirements for a constructive trust to this level, Maitland explained that the constructive trust was not restricted in such a way.² Since the late 19th century the development of the constructive trust has been such that today it is very difficult to provide a simple definition of a constructive trust.³ This may in part be because the judiciary, whilst wishing to avoid the description "remedial" for the constructive trust, have also not wished to limit its application by a precise definition.⁴ To avoid claims that the constructive trust is used as a remedy at the discretion of judges available whenever justice would dictate the courts in Hong Kong and England refer to constructive trusts as institutional: the courts should only impose a constructive trust in certain prescribed situations. To support this institutional claim it has frequently been stated that a constructive trust arises by operation of the law, and not by reason of the intention of the parties.⁵ However, this ignores the opposite claims which are made to justify the common intention constructive trust.

13.2 CONSTRUCTIVE TRUSTS AND CONSTRUCTIVE TRUSTEES

Another issue to consider with regard to constructive trusts is the nature of the legal owner of property subject to a constructive trust—sometimes called the "constructive trustee". This term should be used carefully and it is important to remember that the legal owner of property subject to a constructive trust is not really a trustee at all in the usual sense as he has not accepted trusteeship but had trusteeship imposed upon him because of his conduct. Therefore the constructive trustee may not even be aware that he is a trustee until the court declares him such. Millett LJ, as he then was, attempted to clarify the use of the terms constructive trust and constructive trustee in *Paragon Finance Plc v DB Thakerar & Co.*⁶

¹ FW Maitland, *Equity: A Course of Lectures*, edited by J Brunyate (Cambridge: Cambridge University Press, revised ed., 1936) p.80. Maitland cited *Lewin on Trusts* and then noted the seminal case as *Keech v Sandford* (1726) 1 Sel Cas Ch 61, 25 ER 223, considered below in the chapter on fiduciaries.

² *Ibid.*, pp.81–85.

³ In fact the "constructive trust" has been described as a "fiction" as it is not a trust but courts orders to pay a sum of money or convey an interest in property: William Swadling, "The Fiction of the Constructive Trust" (2011) (64) *Current Legal Problems* 399–433.

⁴ See the comments of Edmund-Davies LJ in *Carl Zeiss Stiftung v Herbert Smith & Co (No 2)* [1969] 2 Ch 276, 300.

⁵ For example, "... express trusts are created by the will of the parties, whereas constructive trusts are imposed by law". Paul Matthews, "The Words Which Are Not There: A Partial History of the Constructive Trust" in Charles Mitchell (ed), *Constructive and Resulting Trusts* (Hart Publishing, 2009) p.4.

⁶ [1999] 1 All ER 400.

The distinction is made according to when the legal owner is under the trust obligation. Millett LJ said that the expressions constructive trust and constructive trustee "have been used by equity lawyers to describe two entirely different situations".⁷ The constructive trust:

"covers those cases ... where the defendant, though not expressly appointed as trustee, has assumed the duties of a trustee by a lawful transaction which was independent of and preceded the breach of trust and is not impeached by the plaintiff".

The constructive trustee is such "as a direct consequence of the unlawful transaction that is impeached by the plaintiff". Thus the constructive trust arose when it would be unconscionable for the legal owner of property to ignore the beneficial interests of another whereas the constructive trustee:

"... is not in fact a trustee at all, even though he may be liable to account as if he were. He never assumes the position of a trustee, and if he receives the trust property at all it is adversely to the plaintiff by an unlawful transaction which is impugned by the plaintiff. In such a case the expressions 'constructive trust' and 'constructive trustee' are misleading for there is no trust and usually no chance of a proprietary remedy; they are nothing more than a formula of equitable relief".⁸

13.3 PERSONAL OR PROPRIETARY ACTIONS—UNAUTHORISED PROFITS

The importance of the constructive trust is, of course, the consequent proprietary rights that the beneficiaries may have in the trust property. If the court declares that property is held on constructive trust then the beneficiaries may assert their proprietary interest as interests good as against others who may receive the property or be claiming the property or a remedy against the property or the person holding it. If the court declares that someone is accountable for loss to a trust then the remedy available to the beneficiary is purely personal, that is they may make the defendant account for any loss to the trust and recover misappropriated trust property, although if the property cannot be recovered they may have to provide equitable compensation, similar to common law damages as the defendant will provide money as compensation.⁹

If a defendant receives property knowing that it has been obtained in breach of trust (knowing receipt) he may hold that property on constructive trust for the beneficiaries. If the defendant cannot return the property then he may be liable to compensate the trust for the loss his receipt has caused. If a defendant aids in the misappropriation of trust property in breach of trust he may be liable in equity for any loss the breach has caused as an accessory to the breach (dishonest assistance). Defendants made liable under these principles may have traditionally, although incorrectly, been termed "constructive trustees". It has now been clarified that defendants found liable in such circumstances are not constructive trustees but made liable in equity.

⁷ *Ibid.*, 408.

⁸ *Ibid.*, 409.

⁹ For example, see the liability of an accessory to a breach of trust in chapter on liability of strangers to the trust.

There has been some debate over whether the trustee or fiduciary that makes an unauthorised profit from their position holds that profit on constructive trust or is a constructive trustee of the profit. A fiduciary owes obligations to act in good faith to his principal—these obligations become the fiduciary duties not to allow the fiduciary's interests to conflict with their duties to the principal and not to make an unauthorised profit from their position as a fiduciary. A trustee is a special type of fiduciary who owes fiduciary obligations to his trust and his beneficiaries. The fiduciary relationship, the relationship of a person owing a duty to act in the best interests of another based upon good faith, arises in the agency relationship. This is where someone asks another to act on his behalf, usually in business. Here the agent, the person acting on behalf of another, acts in the best interests of his principal, the person who has asked for the agent's help. There are accepted categories of fiduciary—as already mentioned the agent is a fiduciary of his principal and the trustee is a fiduciary of his trust and the beneficiaries of the trust. Other examples of fiduciary relationships include: a solicitor is a fiduciary of his clients; a company director is a fiduciary of the company. The fiduciary relationship may also arise in other situations and is discussed later. As noted above, it is part of the fiduciary duty not to make an unauthorised profit from your position as a fiduciary, this applies particularly to trustees. If a fiduciary makes an unauthorised profit from their position, then they will not be permitted to retain it. The fiduciary will have to account for this profit and will usually be required to pass it to the principal.¹⁰ It has been claimed that the trust or principal never had the profit the trustee or fiduciary does not hold this profit on trust for the trust or principal but is merely accountable as a constructive trustee. This is a very important issue as if the profit is held on trust then the principal or trustee has a proprietary interest which allows claims for the recovery of property which represents the bribe whereas if there is not trust then the principal or trust is limited to a personal claim which may be defeated by the property being transferred to others and by the bankruptcy of the trustee or fiduciary. However, as is discussed below, the Privy Council in *A-G of Hong Kong v Reid*,¹¹ adopted the general approach that if the trustee or fiduciary has received an unauthorised profit in the course of conducting business for their trust or principal, in *A-G of Hong Kong v Reid*, it was a bribe, the principal has a greater claim to the profit and so the trustee or fiduciary holds that property on constructive trust for their principal. The importance of this decision is that this is a proprietary interest and permits following this profit and tracing substitutions for the profit and their possible recovery using equitable principles of tracing. Although this principle was doubted in *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd*¹² by the Court of Appeal, the Supreme Court has reaffirmed the *Reid* principle in *FHR European Ventures LLP v Cedar Capital Partners LLC*.¹³

13.4 CONSTRUCTIVE TRUST: TRUST OR REMEDY OF EQUITY?

The constructive trust has most often been used to combat fraud. Here, of course, fraud is not used in the same sense as deceit at common law. This is the more general concept

¹⁰ For example, see *Boardman v Phipps* [1967] 2 AC 46.

¹¹ [1994] 1 AC 324.

¹² [2012] Ch 453.

¹³ [2015] AC 250.

described by Viscount Haldane LC in *Nocton v Lord Ashburton*:¹⁴ "any breach of the sort of obligation which is enforced by a court that from the beginning regarded itself as a court of conscience". Thus unconscionable behaviour is the basis of equitable fraud as equity, "correct men's consciences for frauds, breach of trusts, wrongs and oppressions".¹⁵ Therefore the court imposes or recognises a "constructive trust" that protects a beneficial interest in property in favour of the claimant and that is then held on trust by the legal owner.

The debate over the remedial or institutional nature of the constructive trust and the uses to which it is put, has led Swadling to argue that the constructive trust is not actually a trust but a remedy of equity.¹⁶ However, this has been countered by Wright who argues that the constructive trust is a trust however much it may differ from the express private trust, but that is to be expected as there are many types of trust and many have only limited similarity to the express private trust.¹⁷ Although there is academic disagreement surrounding the nature of the constructive trust we may consider the situations in which a constructive trust may arise—the categories of constructive trust.

13.5 ACCEPTED CATEGORIES OF CONSTRUCTIVE TRUSTS

Below are some categories of constructive trust—once again academic opinions vary on categorisation of these circumstances as constructive trusts. These are by no means exhaustive.

Constructive trusts may be imposed or recognised by the court:

- (1) when a trustee or fiduciary in breach of trust or their fiduciary duty makes a profit or takes an advantage from their fiduciary position;
- (2) when strangers to the trust have damaged the trust;
- (3) to prevent fraud;
- (4) when there has been unlawful killing;
- (5) to help parties under a specifically enforceable contract;
- (6) to enforce "special" testamentary trusts; and
- (7) to give effect to common intentions—the common intention constructive trust.

13.5.1 Trustee in breach of trust or fiduciary in breach of their fiduciary duty

A fiduciary is someone in a special relationship of good faith with another party, the principal, where the fiduciary has power to affect the interest of the principal. The fiduciary has strict duties of loyalty and good faith. For example company directors are fiduciaries of the company and owe duties of good faith to the company as a whole. They must not allow their interests to conflict with their duties to the company; they must not make unauthorised profits from their position and they must always act in the best interests of the company. As we shall see the trustee is a special type of fiduciary. If a fiduciary makes a profit or takes an advantage from his position he may be liable to account to his principal for any benefit

¹⁴ [1914] AC 932, 954.

¹⁵ *Earl of Oxford's Case* (1615) Rep Ch 1, 21 ER 485 (Lord Ellesmere).

¹⁶ Swadling (n.3 above) pp.399–433.

¹⁷ David Wright, "How Much of a Trust Is a Constructive Trust?" (2012) 18(3) *Trusts & Trustees* 264–272.

he receives, even if the principal has not made a corresponding loss. The profit may be held on constructive trust if the profit or advantage derives from the trust property. For example, in *Keech v Sandford*,¹⁸ the case which is said to be the first use of the constructive trust, a landlord refused to renew a lease to a trustee in favour of the trust which had an infant beneficiary. The trustee, Mr Sandford, took the new lease for himself. When the infant was an adult, now Mr Keech, he sued Sandford for the profits he had made on the lease. Lord King gave judgment:

"I must consider this as a trust for the infant, for I very well see, if a trustee, on the refusal to renew, might have a lease to himself, few trust-estates would be renewed to the *cestui que use*; though I do not say there is a fraud in this case, yet [Sandford] should rather have let it run out, than to have had the lease to himself. This may seem hard, that the trustee is the only person of all mankind who might not have the lease; but it is very proper that rule should be strictly pursued, and not in the least relaxed; for it is very obvious what would be the consequence of letting trustees have the lease, on refusal to renew to *cestui que use*. So decreed, that the lease should be assigned to the infant, and that the trustee should be indemnified from any covenants comprised in the lease, and an account of the profits made since the renewal."¹⁹

Thus the trustee held the lease for the benefit of the infant on constructive trust and had to pass the lease and the profits he had made on the lease to the plaintiff beneficiary.

As noted above, there has been some controversy over the status of property obtained from third parties that has never been trust property and was not derived from trust property.²⁰ If this is the case the profit may only be subject to a personal action based on a debtor and creditor relationship and not subject to a trust interest for the principal and the ensuing proprietary rights. However, this may be modified if the fiduciary nature of the relationship would have placed the fiduciary under a duty to pass the property to the principal, especially if the fiduciary would never have obtained the profit unless they held the fiduciary position.

Boardman v Phipps

[1967] 2 AC 46

Boardman was a solicitor to the Phipps family trust and, together with one of the beneficiaries, Tom Phipps, attended meetings of a private company and obtained information about the company, in which the trust held a substantial although minority shareholding. Boardman and Tom Phipps realised that there was the potential to make a substantial profit for the trust if the trust purchased more shares in the company and reorganised the company. They informed the trustee of this but the trustee was not in a position to purchase more shares at that time. Boardman and Tom Phipps therefore decided to purchase shares themselves and effect the reorganisation. They informed the trustees and beneficiaries of the family trust. Boardman and Tom Phipps reorganised the company and realised substantial profits for themselves and for the trust. One of the beneficiaries challenged their actions.

¹⁸ (1726) Sel Cas Ch 61, 25 ER 223.

¹⁹ (1726) Sel Cas Ch 61, 62, 25 ER 223, 223 (Lord King LC).

²⁰ *Tripole Trading Ltd v Prosperfield Ventures Ltd* (2006) 9 HKCFAR 1.

Judgment:

The House of Lords held, by a 3/2 majority, that Boardman and Tom Phipps should account to the trust for their profits. They had acted in good faith and they had made profits for the trust, but they had nevertheless made their profits purely as a result of information gained from their association with the trust. Boardman and Phipps made themselves *trustees de son tort, de facto* trustees because of their actions,²¹ and thus they were in fiduciary positions to the trust when they received this information. They had allowed their personal interests to conflict with their duties to the trust. They held these profits for the Phipps family trust.

The most intensive recent debate over the nature of a principal's interest in property has been generated by the cases involving fiduciaries taking bribes.²² In Hong Kong the most infamous case involves the government lawyer Warwick Reid. Warwick Reid may have been the type of problem lawyer Alexander Pope had in mind when he wrote, "Alas! The small discredit of a bribe, Scarce hurts the lawyers, but undoes the scribe".²³

A-G of Hong Kong v Reid

[1994] 1 AC 324

Reid was employed by the Hong Kong Government to prosecute bribery and corruption. He took bribes to "tip-off" those being investigated, to lose papers and to delay prosecutions. When he was caught he was sentenced to eight years' imprisonment for his criminal activities and ordered to pay HK\$12.43 million to the Crown. This represented the value of assets controlled by him which could not be accounted for by his income and may have been derived from bribes. No payment was made and the Attorney General for Hong Kong registered caveats, warnings of a claim or interest, against three properties in New Zealand as representing the money received as bribes and so held on constructive trust for the Crown. When the Attorney General attempted to renew the caveats in the New Zealand High Court the respondents relied on an English CA authority that a bribe received by a fiduciary was not subject to a proprietary interest in favour of the principal but merely subject to a debtor and creditor relationship and so a personal action. Thus the Crown could not assert a proprietary interest over the bribes or over any property which could be traced as representing the bribes. This interpretation of the principal's interest in a bribe was upheld by the New Zealand CA.

Judgment:

On appeal the Privy Council, led by Lord Templeman, adopted a creative approach to the question. First it was stated that the provider of the bribe had no right to recover the money as it was passed under an illegal transaction. Then Lord Templeman stressed that a fiduciary accepting a bribe caused loss or damage to his principal.²⁴ Thus, as soon as Reid

had received the bribes he knew he had no right to the money and should have handed it to his employer, the Crown, which had suffered damage because of the bribe. As it is a maxim of equity that *equity looks on as done that which ought to be done*, even though Reid had kept the funds equity would consider he had given them to his employer, the Crown. The only way Reid could retain the funds and still have given them to the Crown was if Reid held the funds on constructive trust for his employer.²⁵ If the funds were held on trust for the Crown then the Crown had a proprietary interest in the funds which could be traced into substitutions of property purchased with the funds. Any asset purchased with the funds would belong beneficially to the Crown, including the properties in New Zealand. The Crown could retain any increase in value in the properties, as the fiduciary was not permitted to retain the increase under the principle that he could not make a profit from his position. The decision of the Privy Council acknowledged English CA authority for bribes being merely subject to a debtor and creditor relationship as between the fiduciary and his principal, but relied on the House of Lords decision in *Boardman v Phipps*, a decision of the High Court of Singapore,²⁶ and extra-judicial comment by Sir Peter Millett,²⁷ as he then was.

This decision was followed in *Secretary for Justice v Hon Kam Wing*.²⁸ In this action the Hong Kong Government sought to recover what it alleged to be bribes and property paid for with those alleged bribes. Although the action itself was concerned with time limitation, the court was clear that if the action were to succeed then the defendant would hold the property on constructive trust for the Hong Kong Government, as the recipient of the alleged bribes held them on trust for the employer as soon as they were received.²⁹ The reasoning for the imposition of the trust was further clarified by Deputy Judge Barma SC:³⁰

"22. Prior to the decision in the Reid case, it had long been held that a fiduciary who received a bribe was merely a debtor in equity of the person to whom he owed fiduciary duties, and that the only remedy available against him was a personal claim requiring him to account for the value of the bribe received: see *The Metropolitan Bank v Heiron* (1880) 5 Ex D 319; *Lister & Co. v Stubbs* (1890) 45 Ch D 1. However, in the Reid case, the Privy Council disapproved these decisions, holding that in such a case, the bribe was held by the recipient on a constructive trust for his principal, so that the principal was entitled to recover not just the amount of the bribe, but any property that was acquired with it, or any profits made through the use of it.

23. In the Reid case, having described a bribe as 'a gift accepted by a fiduciary as an inducement to him to betray his trust' (p.330G), Lord Templeman explained how such a constructive trust arose at p.331B-H, where he said:

'When a bribe is offered and accepted in money or in kind, the money or property constituting the bribe belongs in law to the recipient. Money paid to the false fiduciary belongs to him. The legal estate in freehold property

21 See chapter on strangers to the trust.

22 See Sarah Worthington, "Fiduciary Duties and Proprietary Remedies Addressing the Failure of Equitable Formulae" (2013) 72(3) *Cambridge Law Journal* 720, 720.

23 David Hayton, "The Extent of Equitable Remedies: Privy Council versus Court of Appeal" (2012) 33(6) *Company Lawyer* 161-164.

24 [1994] 1 AC 324, 330-331.

25 However, the use of a constructive trust in these situations is not without criticism, see Andrew D Hicks, "The Remedial Principle of *Keech v Sandford* Reconsidered" (2010) 69(2) *Cambridge Law Journal* 287-320.

26 *Sumitomo Bank Ltd v Karitika Ratna Thakir* [1993] 1 SLR 735.

27 Sir Peter Millett, "Bribes and Secret Commissions" [1993] *RLR* 7.

28 [2003] 1 HKLRD 524.

29 *Ibid.*, [62].

30 *Ibid.*

conveyed to the false fiduciary by way of bribe vests in him. Equity, however, which acts *in personam*, insists that it is unconscionable for a fiduciary to obtain and retain a benefit in breach of duty... The false fiduciary who received the bribe in breach of duty must pay and account for the bribe to the person to whom that duty was owed. In the present case, as soon as [Reid] received a bribe in breach of the duties he owed to the Government of Hong Kong, he became a debtor in equity to the Crown for the amount of that bribe. So much is admitted. But if the bribe consists of property which increases in value or if a cash bribe is invested advantageously, the false fiduciary will receive a benefit from his breach of duty unless he is accountable not only for the original amount of the bribe but also for the increased value of the property representing the bribe. As soon as the bribe was received it should have been paid or transferred instantaneously to the person who suffered from the breach of duty. Equity considers as done that which ought to have been done. As soon as the bribe was received, whether in cash or in kind, the false fiduciary held the bribe on a constructive trust for the person injured... The authorities show that property acquired by a trustee innocently but in breach of trust and the property from time to time representing the same belong in equity to the *cestui que* trust and not to the trustee personally whether he is solvent or insolvent. Property acquired by a trustee as a result of a criminal breach of trust and the property representing the same must also belong in equity to his *cestui que* trust and not to the trustee whether he is solvent or insolvent.'

24. At p.337E-H, Lord Templeman cited with approval the views expressed by Millett L J in his article 'Bribes and Secret Commissions' [1993] *R.L.R.* 7, at p.20, where Millett L J said:
- '[The fiduciary] must not place himself in a position where his interest may conflict with his duty. If he has done so, equity insists on treating him as having acted in accordance with his duty; he will not be allowed to say that he preferred his own interest to that of his principal. He must not obtain a profit for himself out of his fiduciary position. If he has done so, equity insists on treating him as having obtained it for his principal; he will not be allowed to say that he obtained it for himself. He must not accept a bribe. If he has done so, equity insists on treating it as a legitimate payment intended for the benefit of the principal; he will not be allowed to say that it was a bribe.'
25. It is clear from the judgment of Lord Templeman that the constructive trust arising in respect of the bribe received by a fiduciary such as Reid arose upon receipt of the bribe. It also seems clear that the manner in which the trust arises involves the use of two of the techniques of equity. First, because the fiduciary cannot be heard to say that he preferred his own interests to those of the person to whom he owed his fiduciary duties, equity regards the bribe as a legitimate payment, intended for his principal. Second, as the bribe is something that must be paid over at once (instantly) to the principal, equity treats as done that which ought to be done, and imposes a constructive trust over it for the benefit of the principal.'

This principle seemed settled until the English CA decision in *Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd*.

Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd

[2012] Ch 453

A fiduciary used the principal's funds to give the impression of trading activity to generate confidence in a complicated Ponzi scheme. The confidence in the trading of the companies increased the price of the companies' shares. The fiduciary sold the shares for some £28 million. The shares should have been worthless. The gain represented an unauthorised profit from the use of the principal's funds and should have been accounted for by the fiduciary to the principal. The problem was that the funds had been paid to the fiduciary's creditors which were banks including those with floating charges. Although the profits were not bribes the nature of the fiduciary's interest in the funds was very important. If the interest was proprietary it would succeed against the banks unless they were *bona fide* purchasers without notice of the principal's interest. If not the interests was personal against the fiduciary and no action lay against the banks.

Judgment:

The CA declared itself bound by its own previous decisions and declined to follow *A-G of Hong Kong v Reid*, holding where there was a bribe the principal had never had the property so there could never be a trust in favour of the principal. Thus there was no proprietary interest merely a personal remedy for the principal against the agent. It should be noted that Lord Neuberger MR in giving the judgment of the Court noted that the profits made in the case before the Court were not made from bribes and there was a distinction between such profit, made by way of share dealing in a "classic Ponzi scheme"³¹ and a bribe which is handed directly to a fiduciary to induce him to betray his principal.³² The Court proceeded to consider the nature of the principal's interest in a bribe to a fiduciary and held itself bound by five previous CA decisions that these were subject to account and equitable compensation only not a proprietary interest. Lord Neuberger MR opined that he was far from satisfied that the Supreme Court would follow *A-G of Hong Kong v Reid* if it was called upon to consider the principle as the decision in *A-G of Hong Kong v Reid* was "unsound", and might result in unfairness for other creditors of the fiduciary in the event of his insolvency.³³

However, in *FHR European Ventures LLP v Cedar Capital Partners LLC*,³⁴ the Supreme Court reaffirmed the *Reid* principle that there is a proprietary interest in a bribe but basing this on the law of agency. The Court also noted that many jurisdictions had considered the issue of the principal's proprietary interest in a bribe and had decided to follow the *Reid* approach as this followed the general principles of the law of agency. The unanimous judgment of the Court included Lord Neuberger's clarification:

31 A Ponzi scheme involves a rogue taking investments from various parties in low-yield or non-existent business ventures; the earlier investors receive their interest payments from the funds of new investors and the cycle of paying earlier investors with capital from new investors continues until the fraud is discovered or the fraudster disappears with the funds: see for example *Jeremy D Stone Consultants Ltd v National Westminster Bank Plc* [2013] EWHC 208 (Ch).

32 [2012] Ch 453, [56].

33 *Ibid.*, [76]–[83].

34 [2015] AC 250.

- "33. The position adopted by the respondents, namely that the Rule applies to all unauthorised benefits which an agent receives, is consistent with the fundamental principles of the law of agency. The agent owes a duty of undivided loyalty to the principal, unless the latter has given his informed consent to some less demanding standard of duty. The principal is thus entitled to the entire benefit of the agent's acts in the course of his agency. This principle is wholly unaffected by the fact that the agent may have exceeded his authority. The principal is entitled to the benefit of the agent's unauthorised acts in the course of his agency, in just the same way as, at law, an employer is vicariously liable to bear the burden of an employee's unauthorised breaches of duty in the course of his employment. The agent's duty is accordingly to deliver up to his principal the benefit which he has obtained, and not simply to pay compensation for having obtained it in excess of his authority. The only way that legal effect can be given to an obligation to deliver up specific property to the principal is by treating the principal as specifically entitled to it."

Thus the focus of the Court was on the general principles of the law of agency and the fiduciary nature of such a role. If the remedy of specific performance is available then the holder of the relevant property will hold that property on constructive trust.

This area of the doctrine of constructive trusts is intertwined with the confused law of fiduciaries generally.³⁵

It is also important in Hong Kong to consider that the principle in *A-G of Hong Kong v Reid* is a very important principle in combating corruption which has been described as "an evil practice which threatens the foundations of any civilised society".³⁶ This principle therefore has a particular importance for Hong Kong where these practices have been described as "cancerous activities",³⁷ as, although the common law generally "abhors corruption and fraud",³⁸ Hong Kong has taken a particular stand against bribery and corruption which was considered endemic in the 1960s and early 1970s and led to the setting up of the Independent Commission Against Corruption in 1974. In Hong Kong it has been said that corruption "must be kept in check" as an "imperative of our legal system",³⁹ which is the justification for the courts of Hong Kong allowing that "special powers of investigation" are necessary to combat corruption.⁴⁰ The importance of *A-G of Hong Kong v Reid* is that it prevented Reid taking advantage of his criminal activities and the limits of a personal action so that he and his wife (and possibly his solicitor) could sell the properties and, in the words of Lord Templeman, "the proceeds whisked away to some Shangri-La which hides bribes and other corrupt moneys in numbered bank accounts".⁴¹

13.5.2 When strangers to the trust have damaged the trust

A constructive trust may be imposed upon somebody who intermeddles with trust property; or somebody who dishonestly assists in a breach of trust or somebody who knowingly receives trust property. These parties are known as strangers to the trust and will be discussed later.

³⁵ See Worthington (n.22 above) pp.720-752.

³⁶ *A-G of Hong Kong v Reid* [1994] 1 AC 324, 330-331.

³⁷ *R v Chong Ah Choi* [1994] 2 HKCLR 263.

³⁸ *R v Whitaker* [1914] 3 KB 1283, 1297.

³⁹ *Attorney-General v Hui Kin Hong* [1995] 1 HKCLR 227 (Bokhary JA).

⁴⁰ *Ibid.*

⁴¹ *A-G of Hong Kong v Reid* [1994] 1 AC 324, 339.

13.5.3 To prevent fraud

As previously noted the equity jurisdiction has existed to prevent fraud thus constructive trusts are often imposed to prevent fraud or unconscionable conduct.

Peffer v Rigg

[1977] 1 WLR 285

Mr and Mrs Rigg purchased a house jointly with Mr and Mrs Peffer, legal title being conveyed into Mr Rigg's sole name. Mr Rigg sold the house to his wife for £1 as part of his divorce settlement. Mr and Mrs Peffer had not entered their interest at the Land Registry but it was held that Mrs Rigg held the property on constructive trust for herself and the Peffers.

Binions v Evans

[1972] Ch 359

Binions purchased a house at a discounted price subject to an express agreement to permit Mrs Evans to live in the property. When Binions sought to evict Mrs Evans, who was merely a contractual licensee, the court held that she had a life interest by way of constructive trust.

13.5.4 When there has been unlawful killing⁴²

It is a principle of public policy that "the bloody hand shall not inherit":⁴³ if a beneficiary under a will or intestacy unlawfully kills the testator or intestate and thereby acquires legal title to the deceased's property a constructive trust will be imposed in order to prevent the killer from benefiting from his crime.⁴⁴

Re Estate of Cunigunda Crippen

[1911] P 108

Crippen murdered his wife. She died intestate so Crippen was the beneficiary of her estate. Crippen was convicted of his wife's murder and hanged. Crippen had executed a will leaving all his estate to his mistress. In an action for probate Crippen's personal representative was passed over in favour of administration to the wife's next of kin. Sir Samuel Evans commented:

"It is clear that the law is, that no person can obtain, or enforce, any rights resulting to him from his own crime... The human mind revolts at the very idea that any other doctrine could be possible..."⁴⁵

⁴² Equity has used the constructive trust or constructive trusteeship to combat many types of illegal gain for example in *A-G of Hong Kong v Reid* [1994] 1 AC 324, a constructive trust was applied to prevent Reid from benefiting from bribes he had received as the Director of Public Prosecutions in Hong Kong.

⁴³ See Steven Gallagher, "The Bloody Hand May Not Inherit: Why Hong Kong Killer Henry Chau Will Not Get a Cent from the Estate of His Parents" *South China Morning Post* (10 November 2015), available at <http://www.scmp.com/news/hong-kong/article/1877189/bloody-hand-may-not-inherit-why-hong-kong-killer-henry-chau-will-not>.

⁴⁴ A similar rule of public policy applies if a joint tenant unlawfully kills a fellow joint tenant. The rule of survivorship in the killers favour is not applied. See John Wilson, "Death, Severance and Survivorship" [2007] *Fam Law* 1082.

⁴⁵ [1911] P 108, 112 (Sir Samuel Evans).

Scotching v Birch

[2008] EWHC 844 (Ch)

Parents of a boy had separated. The mother killed the son in what she claimed was a suicide pact and was awaiting trial for murder. A dispute arose between the parents over the burial of the son. The son had died intestate and so the parents were entitled equally to his estate and also to his corpse. The father argued that the mother was not entitled because it was a rule of public policy that a person who unlawfully kills another is prohibited from taking a benefit under the will or intestacy of the victim. The court upheld this principle. If any property had passed to the mother she would hold it on constructive trust for her son's estate.

The rule of public policy preventing anyone from gaining from unlawful killing may not be applied if the circumstances are such that it would be unjust to enforce the rule. For example, a wife who had been subject to repeated domestic violence and abuse shot her husband dead and was allowed to take the property she inherited from him absolutely and not on constructive trust.⁴⁶

In the United States of America the principle is often referred to as the "slayer rule". This rule is based upon the policy of the common law that no one should be allowed to profit by his own wrong which applies at law or in equity: *nullus commodum capere potest de injuria sua propria*. The slayer rule has been incorporated into many statutes in the different states in the USA and usually is applied in three ways:

- (1) the wrongdoer may not be barred from inheriting;
- (2) the wrongdoer is barred from inheriting; or
- (3) the wrongdoer is not barred from inheriting, but equity imposes a constructive trust on the wrongdoer to pass over to another beneficiary—either the slayer's own heirs or the victim's next of kin.

13.5.5 To help parties under a specifically enforceable contract

The ancient principles of bargain and sale for land recognised that on the completion of the agreement and the payment of the purchase money, the legal title to the land was held by the vendor on an implied use for the purchaser.⁴⁷ The modern development of this is that, as equity considers as done that which ought to be done, the interest of the purchaser of property under a specifically enforceable contract for sale is deemed to arise in equity from the moment that the contract is made. A constructive trust is imposed upon the vendor. Between exchange of contracts and completion the vendor holds the property on trust for the purchaser. It was said in *Lysaght v Edwards*,⁴⁸ "the vendor is a constructive trustee for the purchaser of the estate from the moment the contract is entered into".

13.5.6 To enforce "special" testamentary trusts

There is some controversy over these examples but it may be that mutual wills, secret trusts and *donationes mortis causa* are enforced by way of constructive trust. Although mutual

wills do not comply with the usual principles applicable to the doctrine of wills they are enforced in equity. There is some dispute over how these mutual wills are enforced; some authorities have referred to a contractual basis for enforcing the obligations and other to a "floating" constructive trust. Similarly, there has been academic debate as to whether a secret trust is an express or implied trust, as enforcement of secret trusts requires communication of the trust obligation to the trustee it may be that they are express trusts; however, if they are express trusts they do not comply with the formalities required in s.5 of the Wills Ordinance (Cap.30) and so should not be valid. Thus they may be enforced by way of the constructive trust. The *donatio mortis causa* may be considered a constructive trust, as it is a gift made in contemplation of death that is only perfected on the death of the donor and may be recalled at any time before death. Thus the constructive trust crystallises on the death of the donor.

13.5.7 To give effect to common intentions—the common intention constructive trust

These trusts are used to uphold informal trusts of land which could not be enforced because they lack the formality required for a declaration of such a trust,⁴⁹ or for a binding contract. The former situations have usually been confined in most jurisdictions to the domestic home and the latter to commercial relationships. Informal interests in land may arise by way of resulting trust, constructive trust or as a remedy imposed through proprietary estoppel.

For a constructive trust to be declared a common intention to create a trust must be found from the evidence of the parties—this can be either an express agreement or inferred from the facts. When deciding the share held on constructive trust the question that the court must ask is—what proportion is needed fulfil the intention and to address the unconscionability of the legal owner? The use of the common intention constructive trust to settle disputes over ownership of the family home will be considered in detail in Chapter 11 *Equity and the Family Home*.

In most jurisdictions it is generally accepted that it is difficult to establish a common intention constructive trust with regard to a commercial transaction.⁵⁰ However, it should be noted that in Hong Kong the use of the common intention constructive trust has been extended to commercial relationships.⁵¹ This use includes but is not limited to what is often referred to as the "*Pallant v Morgan* equity" after the eponymous case of *Pallant v Morgan*.⁵² These constructive trusts arise because the parties have agreed to enter into a transaction whereby one of them acquires a property and they then exploit it together. The parties have not entered into a binding contract. One party acquires the land and then exploits it without the other. Equity will hold that the legal owner of the property holds it on constructive trust for both parties. The constructive trust is awarded based upon the defendant's unconscionable behaviour in an agreement "keeping out of the market" the claimant. The agreement has been described as a joint venture and usually involves protracted negotiations but not a binding contract.⁵³ The main problem for a claimant trying to establish that the defendant has acted unconscionably is in establishing that the agreement was a joint venture.

⁴⁶ *Re K (Deceased)* [1986] Ch 180.

⁴⁷ See Jean Howell, "Land Law in an E-Conveyancing World" (2006) *Conv* 553, 560.

⁴⁸ (1875–1876) LR 2 Ch D 499, 506.

⁴⁹ Section 5(1)(b) CPO.

⁵⁰ *Geary v Rankine* [2012] 2 FLR 1409.

⁵¹ *Pang Ketian Sally v Tam Yak Hung Annie* (HCA 298/2012, [2013] HKEC 990).

⁵² [1953] Ch 43.

⁵³ *Banner Homes Group Plc v Luff Developments Ltd* [2000] Ch 372.

If the parties have negotiated "subject to contract" and such clauses have been inserted into the negotiation correspondence then there will be no joint venture. In *Kilcarne Holdings Ltd v Targetfollow (Birmingham) Ltd*,⁵⁴ the court at first instance found that there was no joint venture because of such clauses. This was upheld by the CA which, following *Banner Homes Group Plc v Luff Developments Ltd*,⁵⁵ clarified that what was required for a successful claim for a constructive trust was:⁵⁶

- (1) an arrangement or understanding between the parties; and
- (2) the claimant must act (usually to their detriment in not taking advantage of a commercial opportunity) in reliance upon this understanding.

These elements were confirmed in *Alan Hoo v Benjamin Lung*.⁵⁷ In these circumstances it will be unconscionable for the defendant to ignore the understanding and equity will enforce a constructive trust. There is a marked similarity between the commercial common intention constructive trust and proprietary estoppel, a similarity that is echoed in its domestic counterpart and discussed in the next chapter. Thus actions may be based on both.⁵⁸ Interestingly, although traditionally categorised as a constructive trust,⁵⁹ there has been judicial indication, although in a minority, that the better way to consider the equity in *Pallant v Morgan* is by way of holding the defendant to account in equity.⁶⁰

13.6 SUMMARY

Constructive trusts are difficult to define and classify. Constructive trusts may be remedial or institutional. A constructive trust may be imposed if it would be unconscionable to allow the legal owner of property to assert his legal rights and ignore the beneficial interest of the non-legal owner. Thus most constructive trusts arise when the legal owner of property has received property as a consequence of equitable fraud. However, in Hong Kong we describe constructive trusts as institutional as they arise in certain accepted circumstances. The most interesting development in the doctrine of constructive trusts has been the common intention constructive trust which is most often recognised by the court in disputes between unmarried couples with regard to real property purchased as a family home.

EQUITY AND THE FAMILY HOME

Most of the cases and situations discussed in this part involve couples cohabiting in property as a "family home"; however principles considered may also be used to decide if parties in a commercial venture have interests in property and what the extent of those interests are, for example, the presumption of resulting trust is considered here but is usually categorised as a commercial presumption so that it applies when property is purchased with contributions from parties for commercial purposes perhaps even more than when a property is purchased for domestic habitation. Conversely the common intention constructive trust is usually considered to be a familial doctrine, applying only when property is purchased for family occupation; however, may also arise when there is a joint venture commercial purchase of property arising from the *Pallant v Morgan* equity.¹

This chapter begins with a consideration of women's rights and the benefits of marriage over cohabitation, at least the benefits of marriage in establishing property rights and interests. The issues of establishing property interests in the family home are then considered using a series of questions:

- (1) Are the parties married?
If the parties are married and are divorcing or undergoing judicial separation² then the principles in the statutory provisions in the Matrimonial Proceedings and Property Ordinance (Cap.192) should be applied.
If the parties are not married or if parties are married but this is a question regarding property interests because of the claim of a third party, for example a bank attempting to enforce security against a property, further questions have to be asked:
 - (a) Is there a valid and enforceable express trust of the land?
 - (b) Are both parties the legal owners of the property in dispute?
 - (c) Is one party the legal owner of the property in dispute?
 - (d) Is neither party the legal owner of the property in dispute?

It should be noted that principles which may be applied to decide if unmarried cohabiting couples have interest in a property may apply to same-sex couples as well as to man-woman couples—equity is not discriminatory. Furthermore these principles do not apply only to cohabiting couples in a sexual relationship as they may apply to any parties purchasing or deciding to share a home. As Lord Denning noted in *Cooke v Head*:³

"Whenever two parties by their joint efforts acquire property to be used for their joint benefit, the courts may impose or impute a constructive or resulting trust. The legal owner is bound to hold the property on trust for them both. This trust does not need

⁵⁴ [2005] 2 P & CR 8.

⁵⁵ [2000] Ch 372.

⁵⁶ *Kilcarne Holdings Ltd v Targetfollow (Birmingham) Ltd* [2005] EWCA Civ 1355.

⁵⁷ [2007] 3 HKLRD 169.

⁵⁸ See *Cobbe v Yeoman's Row Management Ltd* [2008] 1 WLR 1752, where the House of Lords declined to find the claimant had an interest by way of constructive trust or proprietary estoppel.

⁵⁹ For example, Lord Millett was quite clear that this interest is by way of a constructive trust: *Paragon Finance plc v Thakerar* [1999] 1 All ER 400, 409.

⁶⁰ *Crossco No 4 Unltd v Jolan Ltd* [2012] 2 All ER 754, [88] (Etherton LJ).

¹ [1953] Ch 43. In Hong Kong see *Ip Man Shan Henry v Ching Hing Construction Co Ltd (No 2)* [2003] 1 HKC 256, *Pang Ketian Sally v Tam Yak Hung Annie* (HCA 298/2012, [2013] HKEC 990).

² See s.5 of the Matrimonial Causes Ordinance (Cap.179).

³ [1972] 1 WLR 518, 520.

any writing. It can be enforced by an order for sale, but in a proper case the sale can be postponed indefinitely. It applies to husband and wife, to engaged couples, and to man and mistress, and maybe to other relationships too."

Thus in *Liu Wai Keung v Liu Wai Man*,⁴ it was held to apply between brother and sister and it may also arise between parent and child.⁵

14.1 EQUITY AND WOMEN'S PROPERTY RIGHTS

As Britain has recently appointed its second woman Prime Minister, Theresa May, who appointed the first woman Lord Chancellor, Elizabeth Truss,⁶ it is interesting to consider the assistance and protection equity has afforded woman.

The common law has, until relatively recently, largely ignored the independent property rights of women, especially a married woman who was described as a "shadow of her husband" in the relatively recent judicial pronouncement of *Caunce v Caunce*.⁷ However, the Chancellor has intervened to protect women's property rights using trust concepts from the early years of the separate equity jurisdiction. For example, the origins of the law of trusts may be traced to attempts to provide for widows and daughters who might be subject to legal disability on inheritance of land or, if they could inherit, easily displaced from their legal ownership by avaricious relatives or husbands. We have previously considered *Wassell v Leggatt*,⁸ where a husband had forcibly deprived his wife of a legacy she received during her marriage. The woman had no right to property independent of her husband; this right only arose after the Married Women's Property Act 1882 was implemented.⁹ However, in this case equity was able to recognise and protect her interest in the legacy by way of the constructive trust. Equity also protected women's property rights with the presumption of advancement, as it presumed any transfer of property into a wife's name or contribution towards property purchased in a wife's name by a husband as a gift of this property or contribution. Such transfers or contributions did not give rise to the presumption of resulting trust.¹⁰

It is strange that even today, after legislation designed to promote equality has been passed in almost all common law jurisdictions and is reflected in almost all areas of the law, property rights for some women may still only be protected by way of the law of trusts, a law which, it has been argued, has become more suited to commercial purposes than disputes over the family home.¹¹

14.2 THE PROBLEM WITH COHABITING

When a couple decide to live together, whether they marry or decide to cohabit without marrying, they often do not consider their relationship ending and what will happen to the property they live in if their relationship ends. Cohabiting may involve one partner moving into a property already owned by the other party, or the purchase of a property together. Traditionally if a couple married the marital home was held in the name of the husband alone. Even today married and unmarried couples may decide to convey the family home into the name of one partner alone because of the requirements of the bank to which the property is mortgaged or other financial obligations or restrictions, for example gender pay imbalances may affect decisions as to loans.

However the legal title to property is held, both parties may contribute to the purchase of the property through contributions to the deposit and/or paying legal fees associated with the purpose, and either or both may take on the burden of repaying a mortgage granted over the property. Once the property has been purchased one party's income may be used for mortgage payments and the other party's used for general household expenses such as food and utility bills. Unfortunately there is a chance that the relationship will break down and the most bitter of disputes usually occur on the break-up of a relationship. There will often be dispute over the ownership of the most valuable asset of the couple—the family home. This dispute may be exacerbated by financial difficulties which may have contributed to the end of the relationship, and involve claims against one or both of the parties by a third party, usually a bank or building society, for possession and sale of the family home.¹² Relationships of love and affection often give rise to property transactions based upon implied not express trust; there is rarely an express agreement that the sole legal owner of the family home holds the property on trust for both. Even if there is an agreement it will usually have been expressed orally, not in writing.

If the couple are married the Matrimonial Proceedings and Property Ordinance¹³ ss.4 and 6,¹⁴ gives the court "almost limitless" discretionary power upon divorce to decide what the property of a marriage is and to make an order for the division of that property between the parties; these powers are discussed briefly below.¹⁵ However, if the couple are unmarried there may be problems ensuring both parties get their "fair share" of the family home as the courts do not have these statutory powers and may not award interests in properties at will but must only use established legal principles which come from equity and the law of trusts.¹⁶ Thus a cynical view may be that one of the benefits of marriage is divorce—as divorcing spouses may find it easier to claim an interest in property than if they had never married.

4 [2013] 5 HKLRD 9.

5 *Wong Kwok Ki Stephen v Lee Lai Ying* (DCCJ 677/2013, [2013] HKEC 189). Although the Court held there was no constructive trust here.

6 Appointed 14 July 2016.

7 [1969] 1 WLR 286.

8 [1896] 1 Ch 554.

9 Containing similar provisions to the Married Persons Status Ordinance (Cap.182), as amended.

10 See for example *Kingdon v Bridges* (1688) 2 Vern 67, 23 ER 653, *Bennet v Bennet* (1879) 10 Ch D 474.

11 Anne Barlow and Craig Lind, "A Matter of Trust: The Allocation of Rights in the Family Home" (1999) 19 *Legal Studies* 468–488.

12 See Simone Wong, "Constructive Trusts over the Family Home: Lessons to be Learned from Other Commonwealth Jurisdictions?" (1998) 18(3) *Legal Studies* 369–390.

13 Some jurisdictions have extended the rights and powers of the court to divide property to the dissolution of relationships of same sex couples in a civil partnership, eg, in the UK a civil partnership registered and recognised under the Civil Partnership Act 2004.

14 See for example *K v W* (FCMC 5641/2001, [2010] HKEC 863). The CFA has now confirmed that the approach to the division of assets on divorce should follow the English approach of equal division (*White v White* [2001] 1 AC 596) unless the marriage is only of short duration or there is some other deciding factor. See *Kan Lai Kwan v Poon Lok To Otto* (2014) 17 HKCFAR 414.

15 *Thomas v Thomas* [1995] 2 FLR 668.

16 See the comments of Lord Diplock in *Gissing v Gissing* [1971] AC 886, 905–906, quoted below.

Surprisingly, there may be fewer problems if the legal owner of the family home dies than if the couple separate.

14.2.1 Inheritance (Provision for Family and Dependants) Ordinance (Cap.481)

If the legal owner of a property dies intestate or fails to provide for his dependants in his will the court has power under the Inheritance (Provision for Family and Dependants) Ordinance to order provision for a partner. The application is not limited to spouses or children of the deceased; however, the court will only order provision for an applicant if it is satisfied the survivor was dependant on the deceased and the deceased failed to provide adequate provision for the survivor. Often a claim under the Inheritance (Provision for Family and Dependants) Ordinance for a property will include linked or alternative claims that there was a trust or a claim for an interest by way of proprietary estoppel.¹⁷

If the application under the Ordinance is made by a wife then if a remedy is granted it will usually be to provide for a wife so that she will be no worse off on the death of her husband than she would have been if they had divorced, and vice versa if the application is made by a husband.¹⁸

The Ordinance is considered in more detail in the chapter dealing with succession and wills.

14.2.2 Unmarried couples and law reform

It has been suggested that unmarried cohabiting couples should be given the same protection and rights as married couples. However, it is unlikely that this will be legislated in Hong Kong in the near future as marriage is seen as an important institution for social cohesion and stability and thus accorded a special status at law. In some jurisdictions the status of marriage has been confused by the term "common-law marriage", which has no legal recognition for the application of property division powers of the court upon divorce in England and most common law jurisdictions. However, because of the different social customs of the people of Hong Kong the legislature has extended the status of "wife" in Hong Kong to include relationships such as the concubine, the "de facto wife according to custom", the "secondary wife" and the "equal" wife.¹⁹ Thus there is a general provision in s.2 of the Inheritance (Provision for Dependants) Ordinance, which provides that husband or wife in relation to a dead person includes a person who in good faith entered into a void marriage with the deceased.

Section 14 of the Legitimacy Ordinance (Cap.184), provides that the *Chinese customary status of concubine* is defined as a union of concubinage, entered by a male partner and a female partner before 7 October 1971, under which union the female partner has, during the lifetime of the male partner, been accepted by his wife as his concubine and recognised as such by the family generally. The status or rights of concubine cannot be lawfully acquired after 7 October 1971.²⁰ The judiciary have also accorded the common law privileges of a wife to the presumption of advancement to a concubine.²¹

Those having the status of "de facto wife according to custom" were recognised by the Court in *Cheung Pui Yuen v Worldcup Investments Inc.*²² as having the same privileges under the presumption of advancement as a *de jure* wife.²³

The status of "equal wife" in Chinese customary law arises if one of two brothers has one son and the other brother none, then the childless brother may adopt the nephew to continue his line. The adopted son now marries a second or "equal" wife to have children for his uncle's line.²⁴

The development of these additional categories of "marriage" supports the reluctance of the courts to interfere in the affairs of those whose relationship does not come within these categories. Thus, the fact that the parties are not married, and that their relationship does not come within the recognised marriage-like categories of Chinese custom in Hong Kong, may lead the court to infer that strict separation of finances was intended, as Deputy Judge Tong noted: "But the fact that the parties are not married, may well be a pointer that their respective independent separate interests should be recognised".²⁵ In such cases any dispute over the family home will be decided using trust law principles.

Many of the cases in this chapter are from the early 1970s in England as this was a time of rapid development of this area of the law. The cases often involve married couples, as the Matrimonial Causes Act, containing similar provisions to the Matrimonial Proceedings and Property Ordinance, was not in force until 1973 and the courts in England were developing common law trusts principles in anticipation of their greater legislative power. The development of common law trusts principles was extended to help decide disputes over property by cohabiting couples and has continued to be applied and developed by the courts to issues involving the family home.

We begin our consideration of the division of property on the breakdown of a domestic relationship with the first question—are the couple married?

If they are married and the dispute over property is part of divorce, nullity or judicial separation proceedings then the next section gives an overview of the relevant law.

If they are married but not divorcing or separating but the dispute over the property is between one of the parties to the marriage and a third party or the parties in dispute are not married then we must ask further questions concerning who is the legal owner of the property in dispute.

14.3 ARE THE COUPLE MARRIED AND IN DIVORCE PROCEEDINGS?

If the couple are married and the dispute over property is part of divorce proceedings, nullity or judicial separation then the Matrimonial Proceedings and Property Ordinance²⁶ ss.4–6A,²⁷ gives the court "almost limitless" discretionary power on divorce to decide the

¹⁷ See *Yiu Lin Tei v Liu Pui Lan* (HCMP 1359/2008, [2011] HKEC 1154).

¹⁸ *Re Estate of CNC* [2011] 4 HKLRD 544.

¹⁹ For a concise consideration of the status of "equal wives", marriage according to Chinese custom, concubinage and secondary wives in China, see the comments of Master Levy in *Re Estate of Tse Chu* [2012] 3 HKLRD 340.

²⁰ Marriage Reform Ordinance (Cap.178) s.5.

²¹ *Li Hung Chan v Wong Woon Heung* (1950) 34 HKLR 213.

²² (2009) 12 HKCFAR 31.

²³ See also *Re Estate of CNC* [2011] 4 HKLRD 544.

²⁴ *Leung Sai Lun v Leung May Ling* (1999) 2 HKCFAR 94, 103.

²⁵ *Lui Kam Lau v Leung Ming Fai* [1994] 3 HKC 477, 488.

²⁶ Some jurisdictions have extended the rights and powers of the court to divide property to the dissolution of relationships of same sex couples in a civil partnership or same sex marriage: eg, in the UK a civil partnership registered and recognised under the Civil Partnership Act 2004.

²⁷ See discussion in note 14.

division of the property of the marriage between the parties.²⁸ These orders may be made as part of the ancillary relief application (ancillary relief is the request for financial aid that are made alongside the petition for divorce, nullity or separation).

The Court's powers under these provisions are subject to the principle that they should be exercised as provided in s.7(1)(a):

"It shall be the duty of the court ... to have regard to the conduct of the parties and all the circumstances of the case including the following matters, that is to say—(a) the income, earning capacity, property and other financial resources which each of the parties to the marriage has or is likely to have in the foreseeable future"

Thus not only may the court take account of all relevant factors pertaining to property of the marriage—the court has a duty to consider all relevant factors.

Some of the many factors the court may take into account are: whether they have signed an agreement as to the division of their property on divorce before they divorce (an ante-nuptial or post-nuptial agreement); whether the parties have agreed that their property is held on trust; whether both or one of the parties have placed property into a trust seemingly for the benefit of others or others and themselves; whether both or one of the parties have placed property into the possession of a company; and whether they are receiving support from their families—a principle sometimes referred to as "judicious encouragement".

As the court may have regard to the existence of a trust the court may still seek to establish whether there is a resulting trust or whether the husband and wife have established a common intention constructive trust.

14.3.1 Ante-nuptial (pre-nuptial) and post-nuptial (separation) agreements

The statutory powers of the court to divide property between a married couple on divorce which are derived from the Matrimonial Proceedings and Property Ordinance permit the court to consider all the circumstances of the marriage and all the agreements between the parties. If the parties have agreed that certain property is to belong to one party during the term of the marriage the court may consider this and enforce that agreement or set it aside. If the parties have agreed that property is held in trust the court may enforce the trust or set it aside. This principle extends to the recognition of agreements entered into before or during the marriage as to how property should be divided between the husband and wife if they were to divorce.

In recent years it has become popular, especially amongst the wealthy, to draw up an ante-nuptial or pre-nuptial agreement. This is an agreement made between the parties before their marriage as to the division of property on the eventual break-up of the marriage. The traditional position of the courts in England and Hong Kong was to disregard these agreements, as, whilst they might not constitute an encouragement to divorce, they were not seen as in-line with the traditional belief that marriage is a "voluntary union for life".²⁹ In fact they might be regarded as similar to trusts that contain provision for the couple on separation, which have been traditionally declared void for offending public policy.³⁰

²⁸ *Thomas v Thomas* [1995] 2 FLR 668.

²⁹ Marriage Reform Ordinance s.4.

³⁰ For example, in *Earl of Westmeath v Countess of Westmeath* (1821) Jac 126, 37 ER 797, Lord Eldon queried an agreement to pay an annuity to a wife whilst the couple was separated as it might prevent the future reconciliation of the couple.

Parties discussing divorce might also reach their own separation or post-nuptial agreement on how to divide their property. These have received more favour from the courts in England and Hong Kong although the Court is still free to depart from the agreement if it thinks this is necessary.

The Court of Final Appeal considered the matter of ante-nuptial and post-nuptial agreements in *SPH v SA*,³¹ and the development of the law in this area. The following is based on the Court's comments and indications.³²

14.3.1.1 Post-nuptial or separation agreements

Post-nuptial or separation agreements have a relatively long history of being followed by the courts if the court is satisfied that the agreement was freely entered into. In *Edgar v Edgar*,³³ it was decided that, although the powers of the court to grant ancillary relief were not limited by such agreements, they carried considerable weight and should be upheld unless there were vitiating factors or a compelling case of unforeseeable circumstances.

The issue of such agreement was considered by the Court of Appeal in *L v C*.³⁴ The Court confirmed that such agreements when freely entered into by parties who are sui then, in the absence of unfair or unconscionable circumstances surrounding the conclusion of the agreement and material and drastic unforeseen circumstances arising thereafter such as to cause manifest prejudice to one of the parties, the courts will hold the parties to their bargain. The court would only allow one of the parties to depart from an agreement if that party demonstrated good and substantial grounds for doing so.³⁵

14.3.1.2 Ante-nuptial or pre-nuptial agreements

The CFA, in *SPH v SA*,³⁶ noted that the development of the law in relation to ante-nuptial agreements established that the recognition of such agreements by the courts as being influential in their orders was considerably less likely than the recognition of post-nuptial agreements by the courts and where this had occurred of much more recent date. In *MacLeod v MacLeod*,³⁷ the Privy Council held that it could not reverse the long standing rule that ante-nuptial agreements were contrary to public policy and thus not valid and binding in the contractual sense, since it was more appropriate that any such policy change should be made by legislation rather than by judicial development.

However, shortly after the Supreme Court gave some guidance on when ante-nuptial agreements could be followed in *Granatino v Radmacher*.³⁸ Therefore, although such agreements are not binding on the court, the court may take account of these agreements, as long as they are freely entered into with a full appreciation of the implications of the agreement and there is no evidence of a vitiating factor such as duress, undue influence,

³¹ (2014) 17 HKCFAR 364.

³² See Lawrence Li, "Be Prepared in Advance: A Case for Allowing Binding Prenuptial Agreements in Hong Kong" (2014) 28 *International Journal of Law, Policy and The Family*, 339–362.

³³ [1980] 1 WLR 1410.

³⁴ [2007] 3 HKLRD 819.

³⁵ *SPH v SA* (2014) 17 HKCFAR 364, [30].

³⁶ *Ibid.*

³⁷ [2010] 1 AC 298.

³⁸ [2011] 1 AC 534.

fraud or misrepresentation.³⁹ The Supreme Court also noted that the nature of the agreement does not have to be contractual as:

“...The value of a contract is that the court will enforce it. But in ancillary relief proceedings the court is not bound to give effect to nuptial agreements, and is bound to have regard to them, whether or not they are contracts”.⁴⁰

The Supreme Court noted that the circumstances surrounding the agreement were all important in deciding whether to follow or depart from the agreement:⁴¹

- (1) Were there circumstances attending the making of the agreement that detract from the weight that should be accorded to it?
- (2) Were there circumstances attending the making of the agreement that enhance the weight that should be accorded to it; the foreign element?
- (3) Did the circumstances prevailing when the court's order was made make it fair or just to depart from the agreement?

The CFA noted that there had been signs of approval of *Granatino v Radmacher* in *LKW v DD*,⁴² although these comments were *obiter*. The Court then noted that:

“In the view of this court, the principles enunciated in *Granatino v Radmacher* should also be regarded as the law in Hong Kong. In common with the UK Supreme Court, we see no reason for distinguishing between ante-nuptial agreements and separation agreements...the old rule that agreements providing for future separation are contrary to public policy is obsolete, and we endorse its judgment. We agree with the UK Supreme Court that this should not be restricted to separation agreements.

None of the supposed distinctions between them can any longer be supported, although we accept that there may be circumstances where it is appropriate to distinguish between an ante-nuptial and a separation agreement...the circumstances surrounding the agreement may be very different dependent on the stage of the couple's life together at which it is concluded, but it is not right to proceed on the premise that there will always be a significant difference between an ante-nuptial agreement and a separation agreement.”⁴³

Thus both ante-nuptial and post-nuptial agreements may now be persuasive for the Court in deciding on ancillary relief although the Court will still have overriding authority to decide how to divide the property. The agreements must be freely and fairly entered into. It may still be that a post-nuptial agreement would be more persuasive to a court than an ante-nuptial agreement, as, because it is made after marriage, the parties' rights have crystallised upon marriage and they have subsequently agreed to vary these rights.⁴⁴

³⁹ *Ibid.*, [75] (Lord Phillips of Worth Matravers): noted with approval in *SA v SPH* [2013] 2 HKC 130 (CA).

⁴⁰ *Ibid.*, [62] (Lord Phillips).

⁴¹ *Ibid.*, [67] (Lord Phillips).

⁴² (2010) 13 HKCFAR 537, [53], [105] (Ribeiro PJ).

⁴³ (2014) 17 HKCFAR 364, [39] and [40].

⁴⁴ The author is grateful for these suggestions to the noted English family law practitioner Mr Frederick Cosgrove-Gibson. For an example of a postnuptial agreement which was not freely entered into and was subject to misrepresentation and so not binding see *Kremen v Agrest* [2012] 2 FLR 414.

14.3.2 Property held by companies or trusts as property of the marriage

The statutory powers of the court to frame orders for the division of the property of the marriage are such that at times an order may be framed against one or both of the parties so that it seems to pierce the corporate veil, the separate legal personality of a company, or even goes behind a trust. For example, it is common for couples contemplating divorce to attempt to move assets out of their legal possession; they may do this by placing property into the possession of a company or into a trust. The concept of separate legal personality for a company is such that even though a person may own all the shares in the company they do not own the property that is owned by the company because the company is a separate legal entity.⁴⁵ This principle means that a shareholder of a company, even though he owns all or nearly all the shares in a company, may be guilty of theft of company property if he takes it for himself.⁴⁶ Similarly we have already considered that when a settlor place this property in trust, unless he has made himself a beneficiary he ceases to have an interests in that property. Thus if a husband places his property into a company or trust (of which he is not a beneficiary, then he may have no interests in that property and may claim he does not own it. However, if the court still considers this to be property of the marriage the court has the power under the Matrimonial Proceedings and Property Ordinance to make an order against the husband which takes account of this property. If the husband does not comply with the order he will be in contempt and may go to prison.

Husband and wife no longer wish to be together. Husband has a successful business which is run by way of a company which has been valued at \$200 million. The husband holds all of the shares in the company and receives dividends on these shares whenever they are declared. In anticipation of divorce and the consequent the ancillary relief proceedings the husband places the shares in a trust which is established in Hong Kong. The beneficiary of this trust is identified as a company in the British Virgin Islands. The shares of this company are placed in trust in a VISTA trust in the British Virgin Islands. The beneficiary of this trust is a trust in the Cayman Islands. This trust identifies the children and grandchildren of the couple as possible beneficiaries and provides that the trustees may identify new beneficiaries in the future. At this point the husband can say he no longer owns his business and is not an identified beneficiary of the trust. However he may, and usually does, have control over the trustees and be able to identify himself as a beneficiary in the future—after his divorce. In the ancillary relief proceedings the court may decide that even though the husband seems to have no legal ownership of the property it is property other marriage and is under his control. The court may make an order that the husband pays the wife \$100 million, half the valuation of the business even though he does not legally own it.

The powers of the court to consider possible interests in trust as property of the marriage was considered in *Kan Lai Kwan v Poon Lok To Otto*. This unanimous decision of the CFA, delivered by Ribeiro PJ, considered a number of issues linked to ancillary relief and trusts including the identification of property held in discretionary trust as assets to be taken into account for ancillary relief calculation.

⁴⁵ *Salomon v A Salomon & Co Ltd* [1897] AC 22.

⁴⁶ *Re A-G's Reference (No 2 of 1982)* [1984] QB 624.

This issue arose because a beneficiary under a discretionary trust has only a hope (*spes*) of an interest; however, the trust may be of such a nature that the beneficiary, even though not yet appointed to have an interest because the trustees have not yet exercised their discretion, may be considered to have some interest in the property.

Kan Lai Kwan v Poon Lok To Otto

(2014) 17 HKCFAR 414

The couple married in 1969 and had three children. The husband started his own engineering business which after initial setbacks was extremely successful. In 1994 the business was restructured as a series of offshore holding companies to run the Hong Kong business and the shares in these companies were settled in trust on an offshore discretionary trust. The Otto Poon Family Trust (the Trust) was established under the laws of Jersey with HSBC International Trustee Limited as the Trustee. The Trust property consisted of shares in Analogue Holdings Ltd (Analogue) and another private company, Realty Limited. Analogue was incorporated in Bermuda in July 1995 with the husband as the Chairman. Analogue owned all the shares in all of the operating companies of the husband's business. Realty Limited owned the family residences: first a flat in Pokfulam, this was later sold and replaced by a house in Sai Kung. The husband's stated purpose for the Trust was:⁴⁷

"As previously discussed, the principal purpose of establishing the trust is to provide for continuity in the ownership of the Analogue group of companies for the benefit of you and your family, to avoid a requirement for probate in respect of your interests in the Analogue group following your death and to relieve your estate of the liability to estate duty that would arise in respect of your shareholdings in the Analogue group."

The terms of the Trust provided that:

"The trustee is given power in its absolute discretion from time to time to appoint capital and to distribute income to any eligible object of its discretion to the exclusion of the others. It also has power in its absolute discretion to appoint additional persons to become beneficiaries."⁴⁸

Two tragedies befell the family. In 1995 the youngest daughter was killed in a car crash which also injured the other daughter Karen and killed Karen's boyfriend. Both husband and wife attributed the beginning of their drift apart to this tragedy. In 2000 their son committed suicide by jumping from the balcony of their Pokfulam flat. The trial judge accepted the husband's submission that this second tragedy marked the end of the relationship. The flat was sold and the family moved to Sai Kung. The husband's business continued to prosper with operating losses only recorded during the SARS outbreak. At trial it was accepted that the Analogue Group consisted of "13 electrical and mechanical engineering companies employing around 1,500 staff and achieving a turnover in excess of HKD2.5 billion a

year". In 2008 the wife confronted the husband about his long-term relationships with a young female employee and the husband moved out of the flat. In November 2008 the wife petitioned for divorce on the evidence of one-year separation and consent. In December the Trustee transferred the shares in Realty Ltd to the wife at the direction of the husband, thereby effectively transferring control of the house in Sai Kung to her. The petition was dismissed by consent and in February 2009 the husband issued a petition evidenced by two years' separation. In this the husband affirmed that the parties had lived apart since February 2001 and both parties deposed this date in their filed Form E financial statements. The wife did not defend and decree nisi and decree absolute were issued in May and September 2009 respectively. The wife later made an affirmation stating that the February 2001 separation date was incorrect and that separation had occurred "some time in 2008".

The court considered how the trust ought to be approached as an asset of the marriage. The husband contended that the Court ought to consider that Karen had a "one-third interest" in the Trust which was not an asset for the marriage. The Trustee was joined to the proceedings and adopted a position consistent with the husband's.

Judgment:

Court of First Instance (December 2011)

Deputy Judge Carlson approved the asset divisions that had already been agreed by the parties. Deputy Judge Carlson held that the Trust assets were not a "resource" of the husband. However, Deputy Judge Carlson ascribed equal shares of a sum of \$1,040,457,300 to the husband and wife as representing two-thirds of the Analogue shares and these being an asset of the marriage. After all adjustments for other assets and applying the principle of equal sharing the husband should pay the wife \$508 million. However, the Judge departed from the principle of equal sharing because the wife was estopped from claiming the marriage had continued until 2008, they had lived separately for the last 10 years of the marriage, and the perceived liquidity of the Analogue Group needed to be preserved. Thus the husband was ordered to pay 72.83 per cent of the sum—a figure of \$370 million.

CA (March 2013)

Cheung JA gave the unanimous decision of the Court in upholding the Judge's decision that only two-thirds of the Trust assets should be regarded as matrimonial assets. However, the Court substituted a separation date of February 2007 and held that there was no reason to depart from the principle of equality disagreeing with the Judge's reasoning as regards liquidity of Analogue and separation of the couple. Thus after netting off the wife was awarded \$510.4 million. The award was to be paid in three tranches: \$250 million within one month and two tranches of \$130 million each to be paid before 1 March 2014 and 1 March 2015 respectively. The first two tranches were paid.

CFA (July 2014)

Both parties appealed. The wife challenged the restriction of two-thirds of the Trust assets to be considered as matrimonial assets. The husband challenged the CA's substitution of a later separation date of February 2007 for the original separation date of February 2001.

⁴⁷ Letter accompanying deed for trust 21 March 1995.

⁴⁸ (2014) 17 HKCFAR 414, [61].

14.3.2.1 *The approach of the Court to identification of financial resources*

Ribeiro PJ noted that as s.7(1)(a) is closely modelled on the equivalent English provision, s.25(2)(a) of the Matrimonial Causes Act 1973, English decisions on s.25(2)(a) are “helpful and persuasive”.

Ribeiro PJ outlined the steps the Court should take in identifying a “financial resource” which H has or is likely to have in the foreseeable future within the meaning of s.7(1)(a)...⁴⁹

- (1) As pointed out in *LKW v DD*,⁴⁹ the first step is:

“...to ascertain the financial resources of each of the parties calculated as at the date of the hearing. ...At this stage, the court need not attempt to distinguish between matrimonial and non-matrimonial property, that being an exercise best undertaken (if necessary) when considering distribution of the assets”.

- (2) The central question was identified by the English CA in *Charman v Charman*,⁵⁰ in which Wilson LJ formulated the test as follows:

“Superficially the question is easily framed as being whether the trust is a financial ‘resource’ of the husband for the purpose of section 25(2)(a) of the Matrimonial Causes Act 1973, as substituted by the Matrimonial and Family Proceedings Act 1984, section 3. But what does the word ‘resource’ mean in this context? In my view, when properly focused, that central question is simply whether, if the husband were to request it to advance the whole (or part) of the capital of the trust to him, the trustee would be likely to do so.”⁵¹

- (3) This test was elaborated in *Whaley v Whaley*⁵² by Lewison J:

“...a discretionary beneficiary has no proprietary interest in the fund. But under section 25 the court looks at resources; not just at ownership. Thus whether a beneficiary under a discretionary trust has a proprietary interest is not relevant. The resource must be one that is ‘likely’ to be available. This is the origin of the ‘likelihood’ test. No judge can make a positive finding about the future: the best that can be done is to assess likelihood. What is relevant is the likelihood of the trust fund or part of it being made available to him, either by income or capital distribution. If the husband were to ask the trustees to advance him capital, would the trustees be likely to do so...? The question is not one of control of resources: it is one of access to them”.

- (4) “The question is whether, looking at all the evidence, the Court should be satisfied that if H were to request the trustee to advance the whole or part of the capital or income of the trust to him, the trustee, acting in accordance with its duties and after having regard to all relevant considerations, would on the balance of probabilities be likely to do so.”⁵³

Ribeiro PJ noted that the *Charman* test was cited with approval by the CFA in *KEWS v NCHC*⁵⁴ and that:⁵⁵

“It is right that the *Charman* test should be adopted in this jurisdiction since the issue arising in cases like the present and since the Hong Kong provision are materially identical. To decide whether a discretionary trust is a financial resource of one of the parties, the Court asks whether, if that party were to request the trustee to advance the whole or part of the capital or income of the trust to him or her, the trustee would, on the balance of probabilities, be likely to do so.”

There were many factors the Court could take into account when making its assessment:

“In making its assessment the Court is able to consider the creation and terms of the trust; H’s letters of wishes; the nature of the trust assets; and previous distributions made by the trustee. As was held in *KEWS v NCHC*,⁵⁶ the Court looks at the reality of the situation and regards past conduct as a useful guide.”⁵⁷

Ribeiro PJ then noted that the husband as settlor had framed the terms of the trust and his letter of wishes to the Trustee with an intent to retain a dominant position with regard to the trust,⁵⁸ for example the husband had made himself protector of the Trust and retained the power to replace the trustees. The husband had also been one of the class of potential beneficiaries and able to instruct the trustees to make funds available to him.⁵⁹ The husband had also ensured that the Trustee had no active role in managing or supervising the Analogue group of companies reserving that role to himself. The Trustee accorded the husband’s wishes “great weight” having followed his instructions to transfer the shares in Realty Limited to the wife and having made distributions to the husband as a beneficiary following his letters of wishes on four occasions between 2002 and 2011 amounting to \$68.5 million. The last two such payments were to satisfy the payment of the awards of the Courts below to the wife and were categorised by the Trustee as “loans”.

Thus the Court held that the entire trust fund valued at \$1,560,686,000 should be regarded as a financial resource available to the husband for the purposes of s.7(1)(a). The “yardstick of equality” should be applied to the division of the assets.

Ribeiro PJ also noted that the *Charman* test does not “postulate any impropriety on the trustee’s part”. As noted in *Charman v Charman* by Wilson LJ:⁶⁰

“A trustee—in proper ‘control’ of the trust—will usually be acting entirely properly if, after careful consideration of all relevant circumstances, he resolves in good faith to accede to a request by the settlor for the exercise of his power of advancement of capital, whether back to the settlor or to any other beneficiary.”

49 (2010) 13 HKCFAR 537.

50 [2006] 1 WLR 1053: a case concerning a discretionary trust situated in Bermuda.

51 This was confirmed to be the test in *Charman v Charman* [2007] 1 FLR 1246.

52 [2011] WTLR 1267, [113]. Referring to the test in *Charman v Charman* [2006] 1 WLR 1053, *A v A* [2007] 2 FLR 467, 499.

53 *Ibid.*, [36].

54 (2013) 16 HKCFAR 1, [53].

55 (2014) 17 HKCFAR 414, [29].

56 (2013) 16 HKCFAR 1, [37] and [38].

57 (2014) 17 HKCFAR 414, [60].

58 *Ibid.*, [76].

59 *Ibid.*, [84].

60 [2006] 1 WLR 1053, [33].

Thus the court may consider a possible interest under a discretionary trust and “vary” that interest by taking account of it in the calculations for ancillary relief and the framing of the order for ancillary relief.

14.3.3 Family financial support and the concept of “judicious encouragement”

A contentious issue that has arisen in recent years is the ability of the court to frame an order for ancillary relief taking account of support which has been provided to husband or wife or both parties by the family of one or both parties during the marriage. Families of one or both spouses may have provided support to either spouse or both during the marriage and this may have been to such an extent that this support might be regarded as an asset to be taken into account for ancillary relief. The question for the court is whether it can take the previous support into account as an asset to be considered in the ancillary relief and so frame an order against one party to the divorce intended to “judiciously encourage” the family to continue to provide the financial support to the party who will have to “pay” the ancillary relief. The principle of “judicious encouragement” was propounded in *Thomas v Thomas*;⁶¹ however the principle has been questioned and doubted in England.⁶² The CFA was asked to consider the question in *KEWS v NCHC*.⁶³ The question for the Court was:

“whether it is permissible for the court to shape an award of ancillary relief in such a way as to ‘judiciously encourage’ third parties to financially support the party who will have to ‘pay’ the ancillary relief”.⁶⁴

The Court decided that it can take third party resources into account if the previous extent and likely continuation of access to those resources can be satisfactorily determined, although Ma CJ recommended that the phrase no longer be used in Hong Kong.⁶⁶

If the couple in dispute over a property are not married then the court does not have the statutory powers to make an order dividing the property. Therefore the court may only use the principles of equity and the law of trusts.

14.4 ARE THE COUPLE UNMARRIED OR DOES THE DISPUTE INVOLVE A THIRD PARTY?

If the couple are not married or if the couple are married but the dispute is not part of divorce proceedings or a decree of nullity or judicial separation but involves a third party perhaps attempting to enforce security against the family home, then the court will use trust law principles to decide on interests in the home. An example of the latter circumstance is given in the facts of *Lloyds Bank Plc v Rosset*.⁶⁷ The plaintiff bank was trying to enforce its security against Mr Rosset who was sole legal owner of the property and Mrs Rosset was

⁶¹ This principle was suggested in *Thomas v Thomas* [1995] 2 FLR 668.

⁶² *TL v ML (Ancillary Relief: Claim Against Assets of Extended Family)* [2006] 1 FLR 1263, [85].

⁶³ (2013) 16 HKCFAR 1, [53].

⁶⁴ For detailed analysis of the judgment of the CFA and the development of the principle see Professor Anne Scully-Hill, “Judicious Encouragement in the Court of Final Appeal: Nothing New?” (2013) 43 *HKLJ* 421–435.

⁶⁵ *Ibid.*, p.421.

⁶⁶ *KEWS v NCHC* (2013) 16 HKCFAR 1, [53].

⁶⁷ [1991] 1 AC 107.

trying to claim an interest in the property by way of common intention constructive trust to prevent the Bank ordering the sale of the property. Similarly in *Re Chow Chung Kwan*,⁶⁸ the husband subject to an action for bankruptcy and the Court had to consider the wife’s interest in the property.

The courts have approached the division of the family home on a different basis from commercial property, as persons “engaged in business can be regarded as capable of looking after themselves”.⁶⁹ The leading common law case on informal trusts of the family home is the House of Lords decision in *Stack v Dowden*.⁷⁰ The House of Lords attempted to clarify how a court should approach the problem of division of the family home when the cohabiting couple were not married.⁷¹ The Supreme Court in the United Kingdom revisited this area in *Jones v Kernott*,⁷² and approved and clarified much of the guidance in *Stack v Dowden*.

Note

In *Stack v Dowden*, the House of Lords emphasised that these principles apply only to non-commercial family arrangements.⁷³

Although in *Jones v Kernott*, Lord Walker and Lady Hale gave a joint judgment in which they emphasised the different approach that should be taken for properties held in joint or single names, it is submitted that in all these cases the court is faced with two questions:

- (1) is there an interest? And, if there is, and
- (2) how much will the claimant party get?

To decide if there is an interest the court will first consider legal ownership of the property, that is—in whose name the property is held at law? This is considered in four questions:

- (1) Is there a valid and enforceable express trust of the land?
- (2) Are both parties the legal owners of the property in dispute?
- (3) Is one party the legal owner of the property in dispute?
- (4) Is neither party the legal owner of the property in dispute?

14.5 IS THERE A VALID AND ENFORCEABLE EXPRESS TRUST OF THE LAND?

If there has been a written declaration of trust which complies with s.5(1)(b) of the Conveyancing and Property Ordinance (Cap.219) (CPO), which requires that it is manifested and proved in writing and signed by the person able to declare such a trust, then the court should enforce this trust even though it does not conform to the legal ownership of the property. Thus

⁶⁸ See for example (HCB 2942/2005, [2015] HKEC 2112).

⁶⁹ *Royal Bank of Scotland v Etridge (No 2)* [2002] 2 AC 773, [88] (Lord Nicholls of Birkenhead).

⁷⁰ [2007] 2 AC 432.

⁷¹ However there has been some academic debate about the value of the judgment in *Stack* in clarifying this area of the law, see for example Martin Dixon, “The Never-Ending Story: Co-Ownership after *Stack v Dowden*” [2007] 71 *Conv* 456, and Mathew Harding, “Defending *Stack v Dowden*” [2009] *Conv* 309.

⁷² [2012] 1 AC 776.

⁷³ Thus they might not apply to cases of the “*Pallant v Morgan* equity” discussed in the previous chapter: *Pallant v Morgan* [1953] Ch 43.

if the couple have bought the property in joint names but then declared a trust of the property in favour of both of them but not in equal proportions or in favour of one of the couple only and this declaration is evidenced in writing signed by both of them then the court should give effect to this trust and enforce it. In fact an express declaration of trust should preclude the operation of the presumption of resulting trust or the common intention constructive trust. For example in *Pankhania v Chandegra*,⁷⁴ a property was transferred into the joint names of aunt and nephew with an express clause that specified that they held as equitable tenants in common in equal shares. The nephew applied for an order to sell the property and have proceeds divided equally. The aunt claimed that at the time of purchase there was a common intention constructive trust that the two were to hold the property on trust for her alone. The English CA held that the express declaration was conclusive and they held as equal beneficial owners.

Developing this principle, even though both parties have paid for the flat and paid in unequal amounts, a valid and enforceable declaration of trust (ie, a declaration evidenced in writing) that the party who had paid the least for the property was the sole beneficiary of the trust would preclude the operation of the presumption of resulting trust in favour of the party who had paid the majority of the purchase price.

Gary and Anne purchase a flat in joint names. Gary pays 90 per cent of the purchase monies and Anne provides 10 per cent. Shortly after purchase Gary and Anne sign a declaration of trust with Anne as the sole beneficiary. Three years later Anne and Gary argue and Anne seeks a declaration that she is the sole beneficial owner of the flat and that the flat must be conveyed to her and Gary must move out. Unless the trust agreement has been procured by fraud, misrepresentation or undue influence the court should enforce the trust and Gary and Anne will have to convey the flat to Anne absolutely.

Therefore the trust should be enforced unless there is any evidence of a vitiating factor such as fraud, misrepresentation or undue influence when the agreement may be set aside. The trust may also be set aside if it can be proved that this trust does not represent the parties' intentions or that these intentions changed and the court should give effect to the change. The court's power to infer a change in beneficial interest when a property is held as joint tenants is discussed below in *Jones v Kernott*.

Unfortunately most couples do not write agreements as to how they hold any property that is purchased to live in as the family home. This is natural as the couples are in love and trust each other that the property will be for them both for the rest of their lives. It has been suggested that the burden of reminding couples that their love may not last forever and that they should be practical and consider property ownership should fall to the conveyancer. Lord Ward noted this as a simple solution to the problem of lack of written evidence of beneficial interests:⁷⁵

"Perhaps conveyancers do not read the law reports. I will try one more time: always try to agree on and then record how the beneficial interest is to be held. It is not very difficult to do."

⁷⁴ [2013] WTLR 101.

⁷⁵ *Carlton v Goodman* [2002] 2 FLR 259.

In defence of conveyancers it should be noted that trying to tell a couple who are embarking on a romantic undertaking, which involves the purchase of property or letting one party move into the other's property, that they should plan for their eventual break-up requires an enormous amount of tact and might result in very unhappy clients. In the UK the addition of a box to clarify the beneficial interest in the property on the form for registration of transfers of land may have helped reduce the incidence of these disputes,⁷⁶ but of course this will not help where a party is moving into a property already owned by their new partner.

If there is no valid and enforceable trust of the property the next question is as to legal ownership of the property.

14.6 ARE BOTH PARTIES LEGAL OWNERS OF THE PROPERTY IN DISPUTE?

If a property is conveyed into joint names then equity follows the law and it is presumed that both parties have a beneficial interest in the property. This presumption may be rebutted by evidence that one of the parties was not intended to have an interest.

Carlton v Goodman

[2002] 2 FLR 259

Mr Goodman purchased his house, which was conveyed into his name and that of Mrs Carlton, whose name was necessary to secure mortgage finance. Mr Goodman told Mrs Carlton that her name would be taken off the legal title after one year. Mr Goodman made all of the mortgage repayments and lived alone in the house. Mr Goodman died intestate and the question arose as to whether Mrs Carlton had acquired the property beneficially by survivorship,⁷⁷ or whether she held the property on resulting trust for Mr Goodman's estate. The CA held that she held the property on resulting trust for the estate as Mr Goodman had purchased the property himself, and Mrs Carlton's assistance was only temporary and nominal.

To decide the extent of the interest the court will consider if any express declaration as to how the property is owned beneficially has been made. This consideration may be summarised as three questions:

- (1) Has the property been conveyed into the couples' joint names as joint tenants?
- (2) Has the property been conveyed into the couples' joint names as tenants in common?
- (3) Has there been no express identification as to how the beneficial interests in the property are to be held?

If legal title to the property is in joint names then the court will presume that, as equity follows the law, if both parties are legal owners they must both be beneficial owners

⁷⁶ This box is in the official Land Registry application form (TR1). See the comments in *Jones v Kernott* [2012] 1 AC 776, [18] (Lord Walker and Lady Hale); see also Moran, "Anything to Declare? Express Declarations of Trust in *Stack v Dowden*" [2007] 74 Conv 364.

⁷⁷ In the UK legal title to property can only be held as joint tenants, s.1 of the Law of Property Act 1925, thus survivorship applies. However, the beneficial interest may be held as tenants in common.

as well. It therefore follows that either party wishing to establish this is not so has the legal burden of proving this. Thus a party wishing to establish a trust must bring reliable evidence of this trust; a party wishing to establish the property is held as joint tenants must bring reliable evidence of this; and a party wishing to establish the property is held as tenants in common and that they have contributed more to the property and so should have a greater share by way of the presumption of resulting trust must bring reliable evidence to establish this.

Note

Whether legal title is in joint or single names, the burden of proof is on the party seeking to establish that beneficial interest is different from the legal interest, because "he who asserts must prove". As these cases are civil then the burden of proof is the balance of probabilities; the party seeking to establish a different beneficial interest from the legal title will have to prove to the court that it is more likely than not that the interest is held as they claim.

14.6.1 Has the property been conveyed into the couples' joint names as joint tenants?

The express agreement to convey a property into joint names to be held as joint tenants is a declaration of trust. This is because the property is then owned equally at law and, as equity follows the law, the beneficial interests are also owned equally. So the joint tenants hold the beneficial interest on trust for themselves equally.

Goodman v Gallant

[1986] Fam 106

A husband and wife purchased a house in the husband's sole name. They then divorced and the husband sold the house to his ex-wife and her new boyfriend at a discount to reflect the divorce settlement to the ex-wife. The unmarried couple bought the house with an express clause in the conveyance as follows:

"... the purchasers shall hold the property upon trust to sell the same with power to postpone the sale thereof and shall hold the net proceeds of sale and net rents and profits thereof until sale upon trust for themselves as joint tenants".

When the couple later separated the wife tried to claim a greater share in the property to reflect her ex-husband's discount of the price.

Judgment:

The court held that the express declaration was a declaration of a trust that the property was held in equal shares and should be followed. The property should be sold and proceeds of sale divided equally.

This principle has been followed in Hong Kong.

Chen Tek Yee v Chan Moon Shing

(HCA 954/2010, [2015] HKEC 735)

Ms Chen cohabited with Chan Senior for some decades. The couple had no children together but Ms Chen's daughters also lived with the couple from the 1970s. Chan was some years older than Ms Chen and for the last few years of his life he lived in an old people's home. Chan died in 2009. In 1980 Chan and Ms Chen bought a flat as joint tenants. Chan had been offered a favourable price to purchase the property and paid a small amount towards it. Ms Chen provided most of the purchase price and she and her daughters paid the mortgage instalments and other outgoings in respect of the property. On a number of occasions Chan assured Ms Chen and her daughters that they would be able to live in the property for the rest of their lives. However, unknown to Ms Chen, Chan executed an assignment severing the joint tenancy and assigning to his son, Chan junior, his 50 per cent share in the property. Chan junior then sold his share at auction to Ng at a substantial discount to the market value. By then, Ms Chen had learned of the severance and she began proceedings against Chan junior seeking a declaration that she and her daughters were entitled to sole and exclusive occupation of the property to the exclusion of Chan junior for the rest of their lives. The auction particulars made it clear that the sale was subject to these proceedings. Ng had visited the property and spoken to Ms Chen. Ms Chen and the daughters now sought declarations that: Chan Senior, Chan junior and Ng (in turn) held Chan's 50 per cent share on trust for Ms Chen; the Property was subject to the Contractual Licence; and that Ms Chen and her daughters were entitled to sole and exclusive occupation of the Property to the exclusion of Chan, Ng or their successors in title.

Judgment:

The court considered the whole course of conduct between Chan and Ms Chen to determine whether the presumption of joint beneficial ownership was rebutted. The fact that Ms Chen had made more financial contribution to the purchase price and paid the mortgage instalments did not rebut the presumption of equality. The court was satisfied that the presumption of equality reflected the parties' intentions in the purchase of the property as a "family residence and permanent home for the family".⁷⁸ The purchase of the Property "reflected a joint or shared commitment by both Ms Chen and [Chan] notwithstanding their unequal financial contributions".⁷⁹

Thus the couple had equal beneficial interests but Chan's repeated assurances to Ms Chen and the daughters affected his conscience and they had acted to their detriment to the extent that a constructive trust arose in their favour. This trust also bound Chan Junior and Ng, the latter because he had agreed to take the property subject to the proceedings and had purchased it at a substantial discount. Thus Ms Chen and her daughters were entitled to sole and exclusive occupation of the Property during their lifetimes.

The parties are free to vary their equal beneficial interest after purchase but such agreement should be evidenced in writing to comply with the formalities in s.5 of the CPO. Therefore

⁷⁸ (HCA 954/2010, [2015] HKEC 735), [75].

⁷⁹ *Ibid.*, [77].