

***Once More unto the Breach [of a Trust]: An Analysis of the Academic Battle over Available Remedies for a Misapplication of Trust Funds***

JACK DAVIES\*

*This article canvasses recent legal developments regarding remedies available for a trustee's misapplication of trust funds. Traditionally, when faced with such a breach, a beneficiary would seek the strict remedy of falsification following the taking of a common account. This action would make the trustee in breach restore to the fund all moneys wrongfully dispersed, irrespective of whether they would have been lost had the breach not occurred. The courts would simply enforce the trustee's primary duty to account for trust property placed under their control. However, the House of Lords in Target Holdings Ltd v Redfern (A Firm) and the Supreme Court of the United Kingdom in AIB Group (UK) plc v Mark Redler & Co Solicitors have suggested, inter alia, that a but-for test of causation now applies to such claims. If the moneys would have been lost in any event, they are irrecoverable. This innovation is the primary topic of this article. After giving an overview of the trust concept, the falsification remedy and the cases, I ask whether the reasoning regarding but-for causation in Target Holdings and AIB is grounded in sound analysis. I conclude it is not, despite my view that the actual outcomes of the cases are correct. As such, I explore how the cases might be rationalised and interpreted so that the strict remedy of falsification retains its place in the law. I offer two alternative theories.*

## I INTRODUCTION

Consider a trust. One trustee, a couple of beneficiaries. The beneficiaries are legal minors, the trustee a wealthy aunt. The aunt, contrary to the trust deed but with good intentions, uses all of the trust funds to purchase an expensive painting which she thinks will appreciate in value. Over the following two days the bank the funds were held in collapses and all of the funds are lost. The beneficiaries move to seek relief. They discover the unauthorised

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\* BA/LLB(Hons). The author would like to thank Professor Peter Devonshire for his assistance, inspiration and guidance.

purchase, but the painting is gone — destroyed in a fire. Proprietary rights cannot be pursued. So, the beneficiaries look to sue for compensation, even though the trust funds would have been lost in any event. What rights do they have?

Traditionally, equity would hold the trustee to her primary duty to account. It would compel her to comply with her undertaking to abide by the trust deed. She would be required to restore to the fund her entire misapplication, even though the moneys would have been lost regardless. I venture there are good reasons for such an outcome.

However, in two decisions, *Target Holdings Ltd v Redferns (A Firm)*<sup>1</sup> and *AIB Group (UK) plc v Mark Redler & Co Solicitors*,<sup>2</sup> the House of Lords and United Kingdom Supreme Court respectively have purported to introduce what amounts to a defence of but-for causation to claims for the misapplication of trust funds. Beneficiaries are unable to recover the funds where, as here, the trustee is able to say the funds would have been lost in any event.

This change in the law lies at the heart of this article. I examine the analysis of the Lords and ask whether this change is a meritorious legal development. In the background sections, I first give an overview of the trust construct, as traditionally understood, and the onerous duties which trustees are subject to. Secondly, I examine misapplications of trust funds and how these would traditionally be remedied by falsification following the taking of a common account (what are now commonly referred to as substitutive performance claims). I stress that this remedy minimises the application of limiting principles so that trustees are required to restore all misappropriated funds, even if they would have been lost had the breach not occurred.<sup>3</sup> Thirdly, I examine *Target Holdings* and *AIB*. Emphasis is laid on those parts of the judgments which suggest that substitutive performance claims no longer have a place in the law or that a defence of but-for causation is now available to claims concerning the misapplication of trust funds.

Moving to substantive analysis, I first analyse the reasoning of the Lords in *AIB*, which draws largely on *Target Holdings*. I conclude that the strength of the reasoning, so far as it purports to disturb the place of the substitutive performance claim, is underwhelming. However, I argue the ultimate outcomes of the cases are fair and just. As such, I ask whether the cases can be rationalised on alternative grounds so substitutive performance claims may continue to have a place in the law, while the equitable outcomes in the cases are preserved. I offer two potential theories.

The first draws on dicta in *Target Holdings* and *AIB* concerning a distinction between traditional and commercial trusts. I examine the development of the trust from a purely private construct to an instrument of commerce and show how some modern instances of trusts are far removed from what the concept originally entailed. Thus, I suggest there are strong

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1 *Target Holdings Ltd v Redferns (A Firm)* [1996] 1 AC 421 (HL).

2 *AIB Group (UK) plc v Mark Redler & Co Solicitors* [2014] UKSC 58, [2015] AC 1503.

3 *Limiting principles* is used to refer to concepts such as causation and remoteness. They are typically features of the common law used to introduce a cap on potential liability.

grounds for drawing a distinction, generally along the above lines, to determine whether substitutive performance claims are available to plaintiffs. As *Target Holdings* and *AIB* concerned trusts falling under the commercial umbrella, their reasoning as to but-for causation can be limited to claims involving similar trusts. Traditional beneficiaries would still be able to make substitutive performance claims.

The second alternative draws on modern doctrine as to breach of trust which suggests, where the duty breached is merely one of skill and care, the remedies available should mirror those at common law including their limiting principles. I argue the claims in *Target Holdings* and *AIB* were, in substance, claims for breach of contract or for negligent administration of the trust. Analysed as such, the Lords' dicta as to a but-for defence would be limited to similar claims. Both of my alternatives would distinguish *Target Holdings* and *AIB* from our hypothetical beneficiaries and, accordingly, allow them to hold their aunt justly to account.

## II THE TRUST AS A LEGAL CONSTRUCT

When a settlor places property on trust they arrange “for control of the property to be separated from the right to benefit from it”.<sup>4</sup> The trustee has the legal title and everyday control of the property, while the beneficiaries take the equitable title — the right to an actual or possible benefit under the trust, pursuant to the general law and the terms of the trust deed.<sup>5</sup> I venture this is as close as one can come to a simple definition of the trust.<sup>6</sup> Legal ownership allows trustees to deal with trust property on a daily basis; however, equitable obligations bind the trustees to administer the property solely for the benefit of the beneficiaries.<sup>7</sup> The traditional trust is a “direct descendant of the medieval ‘use’” — a landholding device similar in nature to the modern trust.<sup>8</sup> And historically, from use to trust, trustees have always held significant power and control over legal title in which another has the beneficial interest.<sup>9</sup> Hence the onerous obligations (detailed shortly) which trustees are subject to.

Importantly, the trust concept has always had at its heart the control of property vested in another. Linked to this centrality of property are the two paradigmatic instances of trusts.<sup>10</sup> First, a trust over land as part of a

4 Peter Jaffey “Explaining the Trust” (2015) 131 LQR 377 at 377.

5 At 377. See this article for a seminal deconstruction of the two competing taxological theories of the English trust: the proprietary and obligational theories.

6 My definition draws on *Re Astor's Settlement Trusts* [1952] 1 Ch 534 (Ch) at 541; and *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] AC 669 (HL) at 705.

7 GE Dal Pont *Equity and Trusts in Australia* (6th ed, Lawbook & Co, Sydney, 2015) at [16.10].

8 Dal Pont, above n 7, at [16.25].

9 See *Westdeutsche*, above n 6, at 705.

10 JE Penner “Distinguishing fiduciary, trust, and accounting relationships” (2014) 8 J Eq 202 at 210.

“dynastic family settlement”.<sup>11</sup> And secondly, the more modern wealth-management trust whereby wealth is administered for private beneficiaries.<sup>12</sup>

## The Duties of Trustees and the Relationship Between the Trust and Fiduciary Doctrine

The duties of a trustee are many. In discharging their duties, trustees must obey the trust instrument and the rules of equity unless a court otherwise allows. An express trustee owes an “irreducible core”<sup>13</sup> of duties under the general law.<sup>14</sup> These are duties that cannot be modified by the trust instrument.

### 1 Fiduciary Duties in the Trust Relationship

Although the relationship of trustee and beneficiary is often described as the “archetypal fiduciary relationship”,<sup>15</sup> not all duties within a trust relationship are fiduciary.<sup>16</sup> Fiduciary duties are unified by the concept of loyalty<sup>17</sup> and are best encapsulated in two well-known tenets: the no-conflict rule and the no-profit rule.<sup>18</sup> These two tenets and other fiduciary duties are applied strictly — for example, a trustee cannot make a profit from his position even if he acts in good faith and even if the profit cannot otherwise be obtained for the beneficiaries.<sup>19</sup>

Although perhaps the typical fiduciary relationship, the trustee-beneficiary relationship is only one of many fiduciary relationships in law.<sup>20</sup> A fiduciary is a trustee only if they have vested in them a fund of property or a power of disposal over it.<sup>21</sup> Again, the trustee’s legal control over the property of another — the vesting of property in the trustee — is what makes the traditional trust such a unique concept in law. And, we will see, the control of property is central to the other duties of a trustee as well.<sup>22</sup>

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11 At 210.

12 At 210.

13 *Armitage v Nurse* [1998] Ch 241 (CA) at 253.

14 David Fox “Definition and Classification of Trusts” in John McGhee (ed) *Snell’s Equity* (33rd ed, Sweet & Maxwell, London, 2015) 571 at [21-005]. These include the duty not to act fraudulently towards his beneficiaries, to be legally accountable to them for trust assets, and to preserve the integrity of the trust fund from his own assets.

15 See, for example, *Dal Pont*, above n 7, at [4.80].

16 *Bristol and West Building Society v Mothew* [1998] Ch 1 (CA) at 16–17.

17 *Dal Pont*, above n 7, at [4.10].

18 At [4.15].

19 *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134 (HL) at 144–145. See also *Keech v Sandford* (1726) Sel Cas T King 61 at 62, (1726) 25 ER 223 (Exch) at 223.

20 Such as that of director and company. See *Dal Pont*, above n 7, beginning at [4.50] for various efforts made by Commonwealth courts to find a unifying “fiduciary principle” which delineates a fiduciary relationship from those which are not.

21 *Paragon Finance plc v D B Thakerar & Co (a firm)* [1999] 1 All ER 400 (CA) at 416.

22 I do not intend to canvass all such duties in this article.

## 2 Other Duties in the Trust Relationship

As noted above, both equity and the terms of the trust govern the trustee's duties. Thus, it has been suggested the obligation to obey the terms of the trust is the paramount duty of the trustee.<sup>23</sup> This duty is of obvious importance — the trust instrument is essentially the “charter” of the trust.<sup>24</sup> In addition, the trustee must exercise a duty of skill and care in administering the trust. Another duty of the trustee is to keep accounts and produce them to beneficiaries when required.<sup>25</sup> Indeed, in the 19th century this duty was described as a trustee's foremost:<sup>26</sup>

[T]he first and primary duty of every ... trustee having money in his hands to be received and to be paid is that an account of his receipts and payments should be kept, to be produced to those interested in the account when it is properly demanded.

Such accounts monitor the trustee's performance of their duties and, as will be seen, are material in assessing liability and the remedy for a breach of trust. However, the uniqueness of the trust lies in the vesting of property in the trustee. Therefore, in my view, the learned authors of *Lewin on Trusts* properly describe the duty to “preserve and safeguard the trust property” as the “overriding obligation of trustees”.<sup>27</sup> This duty is a continuing one and, like the others, is strictly applied.<sup>28</sup> If a trustee's primary duty is that of safe custody, then, by extension, an unauthorised disbursement of trust property is the primary potential breach.

### III BREACH OF TRUST AND THE PRIMACY OF THE ACCOUNTING REMEDY

A breach of trust has been described as “nothing more nor less than an act by the trustee in contravention of the duties imposed upon him by the trust or in excess of his powers”.<sup>29</sup> It can take a variety of forms — the term itself is rather amorphous. As Millett LJ said in *Armitage v Nurse*:<sup>30</sup>

23 Dal Pont, above n 7, at [22.15]; and Richard Nolan “The Duties and Discretions of Trustees” in John McGhee (ed) *Snell's Equity* (33rd ed, Sweet & Maxwell, London, 2015) 737 at [29.004].

24 Dal Pont, above n 7, at [22.15].

25 At [22.30].

26 *Wroe v Seed* (1863) 4 Giff 425 at 429, (1863) 66 ER 773 at 774–775.

27 Lynton Tucker, Nicholas Le Poidevin and James Brightwell *Lewin on Trusts* (19th ed, Sweet & Maxwell, London, 2015) at [34-001]. Another “overriding duty of a trustee is to place the trust property in a state of security”. Nolan, above n 23, at [29-004]. For a case illustrating these views see *Re Brogden* (1888) 38 Ch D 546 (Ch & CA).

28 *Jobson v Palmer* [1893] 1 Ch 71 (Ch) at 75.

29 *Re Spedding (deceased)* [1966] NZLR 447 (CA) at 463–464 per Turner J.

30 *Armitage*, above n 13, at 251.

Breaches of trust are of many different kinds. A breach of trust may be deliberate or inadvertent; it may consist of an actual misappropriation or | misapplication of the trust property or merely of an investment or other dealing which is outside the trustees' powers; it may consist of a failure to carry out a positive obligation of the trustees or merely of a want of skill and care on their part in the management of the trust property; it may be injurious to the interests of the beneficiaries or be actually to their benefit.

I focus on Millett LJ's first incarnation — a wrongful (contrary to law) or unauthorised (contrary to the trust instrument) disbursement of trust funds. This kind of breach is distinct to trustees as managers of a fund of assets equitably belonging to another.<sup>31</sup> So, how does a beneficiary seek redress for such a breach by their trustee?

Traditionally, the beneficiary would commence the action of account — an action which originated in the common law courts.<sup>32</sup> To explain the accounting mechanism, primacy is given to two seminal and recent judgments: *Libertarian Investments Ltd v Hall*,<sup>33</sup> and *Agricultural Land Management Ltd v Jackson (No 2)*.<sup>34</sup> I shy away from using the terminology of “remedy” because, as Lord Millett NPJ explains:<sup>35</sup>

... an account is not a remedy for wrong. Trustees and most fiduciaries are accounting parties, and their beneficiaries or principals do not have to prove that there has been a breach of trust or fiduciary duty in order to obtain an order for account. Once the trust or fiduciary relationship is established or conceded the beneficiary or principal is entitled to an account as of right ... the court is not granting a remedy for wrong but enforcing performance of an obligation.

The taking of an account is generally a three-step process:<sup>36</sup> first, the claimant's right to an account is established; secondly, the account is taken; and thirdly, a consequent order for relief is granted by a court.<sup>37</sup> There are two main ways in which an account can be taken: the account in common form (common account); and that on the basis of wilful default.<sup>38</sup> The differences are as follows.

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31 David Fox “Breach of Trust” in John McGhee (ed) *Snell's Equity* (33rd ed, Sweet & Maxwell, London, 2015) 765 at [30-012].

32 JD Heydon, MJ Leeming and PG Turner *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (5th ed, LexisNexis Butterworths, Australia, 2015) [MG&L] at [23-030]. For excellent histories of the action see at [26-005]; and SJ Stoljar “The Transformations of Account” (1964) 80 LQR 203.

33 *Libertarian Investments Ltd v Hall* (2013) 16 HKCFAR 681.

34 *Agricultural Land Management Ltd v Jackson (No 2)* [2014] WASC 102, (2014) 285 FLR 121.

35 *Libertarian Investments Ltd*, above n 33, at [167].

36 Steven Elliott “Personal Monetary Claims” in John McGhee (ed) *Snell's Equity* (33rd ed, Sweet & Maxwell, London, 2015) 543 at [20-014].

37 At [20-014].

38 Leaving aside for present purposes the related account of profits.

## Common Account

### 1 General Principles

The common account can be sought by a beneficiary as of right and concerns assets actually received and dealt with by the trustees.<sup>39</sup> Lord Millett NPJ explains the procedure when the common account is taken:<sup>40</sup>

Once the plaintiff has been provided with an account he can falsify and surcharge it. If the account discloses an unauthorised disbursement the plaintiff may falsify it, that is to say ask for the disbursement to be disallowed. This will produce a deficit which the defendant must make good, either *in specie* or in money. *Where the defendant is ordered to make good the deficit by the payment of money, the award is sometimes described as the payment of equitable compensation; but it is not compensation for loss but restitutionary or restorative.*

As Lord Millett NPJ explains, when granting an order to correct an unauthorised disbursement, the court is not engaged in assessing loss — the amount of loss is irrelevant. The requisite sum has been described as:<sup>41</sup>

... an equitable debt or liability in the nature of debt. It [is] a suit for the restitution of the actual money or thing, or value of the thing, of which the cheated party [has] been cheated.

Edelman J noted in *Agricultural Land Management* that such an order is, in essence, equivalent to one for specific performance — the court is enforcing the trustee’s primary duty to account.<sup>42</sup> Defendants are unable to say that the plaintiff has suffered no loss or that the amount would have been lost in any event.<sup>43</sup> Edelman J noted that it is not “a sufficient response to a disallowance, or falsification, that the disbursement would have been lost even if the trustee had acted properly”.<sup>44</sup> In short, equity resisted the application of limiting principles to such claims. It was considered equitable to compel strict compliance with the obligations trustees had voluntarily assumed.

### 2 The Strict Application of Common Account

This strictness has been the law for many years. For example, in *Magnus v Queensland National Bank*, a case concerning the liability of a custodial bank to restore funds dispersed in an unauthorised manner, the English Court of Appeal said:<sup>45</sup>

39 *Partington v Reynolds* (1858) 4 Drew 253, (1858) 62 ER 98 at 99.

40 *Libertarian Investments Ltd*, above n 33, at [168] (emphasis added).

41 *Ex parte Adamson* (1878) 8 Ch D 807 (CA) at 819.

42 *Agricultural Land Management*, above n 34, at [337].

43 At [337].

44 At [338].

45 *Magnus v Queensland National Bank* (1888) 37 Ch D 466 (CA) at 472. See also *British North American Elevator Co v Bank of BNA* (1914) 6 WWR 1444 (MBKB) at 1447. The decision was

... we are not at liberty to speculate whether the same result might not have followed whether the bank had been guilty of that default or not. The bank [has] in fact been guilty of default.

There are numerous historical examples of the principle's application.<sup>46</sup> We now come to the seminal statement of Street J in *Re Dawson*, a case concerning the extent of the liability of a trustee to repay trust funds improperly paid out.<sup>47</sup> Street J said:<sup>48</sup>

... if a breach has been committed then the trustee is liable to place the trust estate in the same position as it would have been in if no breach had been committed.

This statement appears to introduce a but-for test of causation regarding the amount due following falsification of a common account. But, as Edelman J notes, such a question is:<sup>49</sup>

... irrelevant when the duty is to replenish a distribution of unauthorised trust funds. Like instances of payment of a debt, or of specific performance, it does not matter whether the funds would have been lost in any event.

Street J's somewhat ambiguous statement can be reconciled with the preceding analysis by saying that any but-for test is "satisfied in a case where an unauthorised disbursement occurs".<sup>50</sup> There is an unauthorised disbursement — the trust fund has been wrongly diminished. End of story. Such an approach accords with the basis of falsification following a common account. The process of falsification is concerned with the beneficiary's right to compel performance of the trustee's primary duties to account and to keep proper custody of trust property — it is unconcerned with loss or a right to compensation. In sum, in accordance with the duties which the traditional trustee owes, falsification following a common account operates strictly with little or no application of limiting principles.

## Wilful Default

However, if there is an existing complaint that the trustees failed to acquire property for the trust due to an absence of due care and diligence, the

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varied in the Court of Appeal, but restored by the Privy Council in *British America Elevator Co Ltd v Bank of British North America* [1919] AC 658 (PC).

46 See, for example, *Cocker v Quayle* (1830) 1 Russ & M 535, (1830) 39 ER 206; and *Head v Gould* [1898] 2 Ch 250 (Ch) at 266. Modern applications can be seen in *Bishopsgate Investment Management Ltd (in liq) v Maxwell (No 2)* [1994] 1 All ER 261 (CA); and *Knight v Haynes Duffell Kentish & Co* [2003] EWCA Civ 223 at [38].

47 *Re Dawson (deceased)* [1966] 2 NSW 211 (SC).

48 At 215.

49 *Agricultural Land Management*, above n 34, at [344].

50 At [345].



beneficiary can ask that the account be taken on the footing of wilful default.<sup>51</sup>

If ... the account is shown to be defective because it does not include property which the defendant in breach of his duty failed to obtain for the benefit of the trust, the plaintiff can surcharge the account by asking for it to be taken on the basis of “wilful default”, that is to say on the basis that the property should be treated as if the defendant had performed his duty and obtained it for the benefit of the trust. Since *ex hypothesi* the property has not been acquired, the defendant will be ordered to make good the deficiency by the payment of money, and in this case the payment of “equitable compensation” is akin to the payment of damages as compensation for loss.

In contrast to the strict liability following falsification of an unauthorised disbursement after the taking of a common account, a surcharge on the footing of wilful default is entirely concerned with the limiting principle of causation. That is to say, the beneficiary must be able to show a causative link between the trustee’s failure to get in what he should have and the deficit in the account.

### A Modern Application of Accounting Terminology

Before turning to the two cases which comprise the focus of this article, I note Edelman J’s observation that these differences between common account and wilful default have been concealed in modern cases which speak broadly of “equitable compensation”.<sup>52</sup> Edelman J helpfully endorses the use of the “substitutive compensation” and “reparative compensation” distinction to rationalise modern claims for breach of trust.<sup>53</sup>

The former, based on the common account, describes a claim for the substituted value of the asset dissipated without authority: it demands that the trustee perform his or her duty to maintain the assets or fund. The latter, based on the account on the basis of wilful default, describes a claim for reparation for the loss suffered by breach of duty.

In my view, such an approach makes perfect sense.<sup>54</sup> As Lord Millett NPJ suggests, a substitutive performance claim is restitutionary or restorative — unconcerned with loss. Similarly, “reparative compensation” (the analogy with wilful default) accords with Lord Millett NPJ’s explanation of such an order as *compensating* the beneficiary for loss.

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51 *Libertarian Investments Ltd*, above n 33, at [170].

52 *Agricultural Land Management*, above n 34, at [348].

53 Steven Elliott “Compensation Claims against Trustees” (DPhil Thesis, University of Oxford, 2002) as cited in *Agricultural Land Management*, above n 34, at [349].

54 The action of falsification following a common account is hereinafter referred to as a *substitutive performance claim* for clarity and consistency.

#### IV TARGET HOLDINGS AND AIB

I now turn to the two cases which are the primary subject of this article: *Target Holdings* and *AIB*. Both cases concerned prima facie trusts and were congruent in outcome<sup>55</sup> — *AIB* being the progeny of *Target Holdings*.

##### *Target Holdings*

In *Target Holdings* a non-party mortgagor interposed various offshore companies between the original vendor and himself, thus enabling him to double the relevant property's purchase price. Together with an inflated valuation, he obtained an excessive mortgage advance from the plaintiff mortgagee (*Target*). The mortgagor defaulted, the property was sold and *Target* was left with a considerable loss. The defendant solicitors (*Redferns*) acted for both *Target* and the mortgagor in the mortgage transaction. *Target* discovered *Redferns* had parted with the mortgage money, which was to be held on trust until the mortgage and title deeds were obtained, without obtaining said documents. Though the documents were later acquired by *Redferns*, *Target* pleaded an unauthorised disbursement from the trust fund and sought to have the trust fund reconstituted in its entirety. Naturally, the loss would have been suffered even if the money had been paid out in an authorised way.

Lord Browne-Wilkinson delivered the sole judgment of the House of Lords. He framed the issue arising as follows:<sup>56</sup>

Is the trustee liable to compensate the beneficiary not only for losses caused by the breach but also for losses which the beneficiary would, in any event, have suffered even if there had been no such breach?

He noted, despite the payment by *Redferns* constituting a breach of trust: “*Target* had obtained exactly what it had originally intended to obtain, that is to say a loan to [the mortgagor] secured by valid charges over the property”.<sup>57</sup> Before turning to the arguments advanced, he made the preliminary observation:<sup>58</sup>

Under both systems [equity and the common law] liability is fault-based: the defendant is only liable for the consequences of the legal wrong he has done to the plaintiff and to make good the damage caused by such

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55 *Prima facie* is used merely to distinguish the trusts in question from the traditional trust described earlier. There exists, within the scope of what the courts will recognise as trusts, significant variance in attributes such as the complexity of the trust deed and the duties owed by trustees. Suffice it to say for present purposes, the trusts in *Target Holdings* and *AIB* were at the simpler end of the spectrum and definitely simpler than the trusts discussed above. This point will be developed later in this article.

56 *Target Holdings*, above n 1, at 428B.

57 At 430A.

58 At 432F.

wrong. He is not responsible for damage not caused by his wrong or to pay by way of compensation more than the loss suffered from such wrong.

Already, this statement is contrary to the premise of a claim for substitutive performance. In such a claim one is only concerned with enforcing a trustee's primary duty to account — loss is irrelevant. In the words of James Edelman, such a claim can be put colloquially as “do what you undertook to do or pay the cost of doing it”.<sup>59</sup>

Turning to the issues in the case, Target advanced two arguments in favour of its position. Argument A was that Redferns was under a continuing duty to reconstitute the trust fund by paying back into the client account the moneys paid away in breach of trust. Argument B was that, after Redferns had disbursed the funds in breach of trust, there arose an immediate right in Target to have the trust fund reconstituted regardless of later events. The former depended upon an entitlement to have the trust funds reconstituted now, whereas the latter quantified the compensation payable by reference to a right to restitution at an earlier date.

Before turning to argument A, Lord Browne-Wilkinson observed:<sup>60</sup>

The equitable rules of compensation for breach of trust have been largely developed in relation to such traditional trusts, where the only way in which all the beneficiaries' rights can be protected is to restore to the trust fund what ought to be there. In such a case the basic rule is that a trustee in breach of trust must restore or pay to the trust estate either the assets which have been lost to the estate by reason of the breach or compensation for such loss.

He then correctly noted that, if a breach of trust is still unresolved but the trust has come to an end — in that there are no active duties left for the trustee to perform under the trust deed — the court orders payment of a money sum to the beneficiary, not restitution to the trust fund.<sup>61</sup> He subsequently considered argument A. He held that even if the:<sup>62</sup>

... rules developed in relation to traditional trusts were directly applicable to such a case as this ... it is in any event wrong to lift wholesale the detailed rules developed in the context of traditional trusts and then seek to apply them to trusts of quite a different kind. In the modern world the trust has become a valuable device in commercial and financial dealings ... The depositing of money with the solicitor is but one aspect of the arrangements between the parties, such arrangement being for the most part contractual ... I have no doubt that, until the underlying commercial transaction has been completed, the solicitor can be required

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59 James Edelman “Money awards of the cost of performance” (2010) 4 J Eq 122 at 122.

60 *Target Holdings*, above n 1, at 434C.

61 At 434H–435A.

62 At 435F–436E.

to restore to client account moneys wrongly paid away. But to import into such trust an obligation to restore the trust fund once the transaction has been completed would be entirely artificial ... In my judgment, once a conveyancing transaction has been completed the client has no right to have the solicitor's client account reconstituted as a "trust fund."

The outcome of argument A is correct. If compensation needs to be made, but the trust has come to an end, the court does not order the reconstitution of the trust.<sup>63</sup> Further, to paraphrase Lord Browne-Wilkinson, ordering reconstitution of a client's trust account, when such a trust does not subsist beyond the breach for the beneficiaries, would be artificial.<sup>64</sup> There were no duties left for Redferns to perform. And there was no sound basis for Target to ask for the fund to be reconstituted. However, Lord Browne-Wilkinson's dicta as to a distinction between commercial and traditional trusts is of import and is discussed later in this article.

Turning to argument B, Lord Browne-Wilkinson noted the Court of Appeal had drawn a distinction between a breach of trust consisting of some failure in the administration of the trust and a breach where a trustee has actually paid away trust moneys.<sup>65</sup> The former would sound in reparative compensation; the latter would sound in a substitutive performance claim. With the latter, the Court of Appeal had said one stops the clock at the date the moneys are paid away — events occurring between the date of breach and the date of trial are irrelevant, save for credit subsequently received.<sup>66</sup> Such an outcome is what the traditional authorities would say is proper.

As Edelman J suggests, any matter of causation is fulfilled the moment an unauthorised disbursement is made.<sup>67</sup> However, Lord Browne-Wilkinson said:<sup>68</sup>

... the fact that there is an accrued cause of action as soon as the breach is committed does not in my judgment mean that the quantum of the compensation payable is ultimately fixed as at the date when the breach occurred.

This statement is sound — one should account for credit subsequently received. However, he then endorsed the comments of McLachlin J in *Canson Enterprises Ltd v Boughton & Co*, where she said:<sup>69</sup>

... compensation is an equitable monetary remedy which is available when the equitable remedies of restitution and account are not appropriate. ... it is essential that the losses made good are only those which, *on a common sense view of causation*, were caused by the breach.

63 *Bartlett v Barclays Bank Trust Co Ltd (No 2)* [1980] 1 Ch 515 (CA) at 545.

64 *Target Holdings*, above n 1, at 436D.

65 At 436H.

66 At 437B.

67 *Agricultural Land Management*, above n 34, at [345].

68 *Target Holdings*, above n 1, at 437D.

69 *Canson Enterprises Ltd v Boughton & Co* [1991] 3 SCR 534 at 556 as cited in *Target Holdings*, above n 1, at 438H (emphasis added).

Lord Browne-Wilkinson concluded:<sup>70</sup>

Equitable compensation for breach of trust is designed to achieve exactly what the word compensation suggests: to make good a loss in fact suffered by the beneficiaries and which, using hindsight and common sense, can be seen to have been caused by the breach.

Thus, there was no relevant loss to compensate as Target obtained precisely what it would have acquired had no breach of trust occurred (valid security for the sum advanced).<sup>71</sup>

In simple terms, Lord Browne-Wilkinson said that a trustee is only liable for loss caused by the breach. And the judgment has rightly been criticised for not addressing the accounting mechanism, let alone the distinction between substitutive and reparative compensation.<sup>72</sup> As Lord Millett correctly observed extra-judicially, a but-for test is apposite to a claim based on wilful default.<sup>73</sup> But in a substitutive performance claim, as in *Target Holdings*, the trustee is “required to account to the trust estate for the full amount of the disbursement — *not* for the amount of the loss”.<sup>74</sup>

### **The Original Criticisms and Evaluation of *Target Holdings***

A significant portion of Lord Browne-Wilkinson’s judgment stands contrary to the premise of the substitutive performance claim. He said that, whatever the breach, equity attempts to make good the loss suffered because of it — the aim is always reparative. This analysis essentially conflated the substitutive performance claim with claims for reparation for loss suffered by a trustee’s breach of duty. Lord Browne-Wilkinson was criticised accordingly by scholars in the years following the decision.<sup>75</sup>

However, despite the flaws in Lord Browne-Wilkinson’s analysis, I venture the ultimate outcome of *Target Holdings* was fair and equitable. Given the limited nature of Redfern’s trust obligations and the fact that its breach could be fairly labelled mere imprudence, to hold Redfern’s accountable for all the funds when those funds would have been lost in any event does not seem fair. Intuitively, there is a distinction between the breach faced by Target — a commercial mortgagee and a beneficiary of a very limited form of trust — and that which confronted the beneficiaries in my introductory hypothetical. I posit such factors led Lord Browne-Wilkinson to try to achieve substantive justice, albeit at the peril of orthodox principles of trust law. As the English Court of Appeal recognised several years later, “[t]he result reached by the House of Lords in *Target Holdings*

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70 At 439B.

71 At 440G.

72 See, for example, PJ Millett “Equity’s Place in the Law of Commerce” (1998) 114 LQR 214 at 224–225.

73 At 225–226.

74 At 226 (emphasis in original).

75 See, for example, at 225.

has been generally welcomed but the route to that result has been much debated”.<sup>76</sup>

On this point, both Lord Millett and Matthew Conaglen note a just result was achievable in *Target Holdings* through proper application of the accounting principles in the substitutive performance claim rather than the insertion of a but-for test.<sup>77</sup> As the mortgage and charging documents were later acquired, such conduct was authorised and the accounts needed to reflect that.<sup>78</sup> Target had to accept the drawing of the accounts as if the funds had been released when the documents were received — the disbursement would remain unauthorised, but the authorised receipt of the documents needed to be credited against the earlier error.<sup>79</sup> An analysis along these lines would have achieved substantive justice and maintained the clear categories of breach, rather than conflate the purposes of the substitutive performance claim and those for reparation into a single purported aim of compensation.

## **AIB**

Turning to *AIB*, a detailed recount of the facts is unnecessary as they are very similar to *Target Holdings*. In short: in a mortgage transaction the defendant solicitors (Mark Redler) wrongly paid out the mortgagee’s (AIB) moneys from a trust account to the mortgagor without first redeeming an existing charge over the relevant property. Although GBP 3,300,000 was advanced in breach of trust, almost all of the loss suffered was caused by the mortgagor’s default and an erroneous valuation of the property — it would have been suffered even if the first charge had been redeemed. In contrast to *Target Holdings*, however, *AIB* never got the first-ranking charge it wanted — the equivalent of the documents eventually acquired in *Target Holdings* that would have made the accounts balance had the case engaged with those principles. Lord Toulson and Lord Reed gave judgment for the Supreme Court.

### *1 Lord Toulson’s Reasons*

Lord Toulson recognised criticism of Lord Browne-Wilkinson’s judgment as not engaging with the traditional rules governing the substitutive performance claim.<sup>80</sup> He further engaged with many of the authorities mandating a strict approach cited above.<sup>81</sup> Lord Toulson, essentially upholding Lord Browne-Wilkinson in *Target Holdings*, concluded that “[t]he basic equitable principle applicable to breach of trust ... is that the beneficiary is entitled to be compensated for any loss he would not have

76 *Bairstow v Queens Moat Houses plc* [2001] EWCA Civ 712, [2001] 2 BCLC 531 at [53] (footnotes omitted).

77 Millett, above n 72, at 227; and Matthew Conaglen “Explaining *Target Holdings v Redfern*” (2010) 4 J Eq 288 at 290.

78 Conaglen, above n 77, at 290.

79 At 290.

80 *AIB*, above n 2, at [50]–[51].

81 At [53]–[61].

suffered but for the breach”.<sup>82</sup> In my view, his conclusion was drawn on three grounds:

- (1) It is simply not right to impose a rule giving redress to a beneficiary for loss which would have been suffered even without the breach.<sup>83</sup> Such an award would be penal.<sup>84</sup> The object of a monetary remedy for breach of trust, whether it is reparative or substitutive, is to make good any loss suffered by reason of the breach (citing *Target Holdings* and *Canson Enterprises*).<sup>85</sup>
- (2) It would be a “backward step” to depart from *Target Holdings*.<sup>86</sup>
- (3) It is a “fairy [tale]” to rationalise *Target Holdings* by deeming the trust moneys as restored to the fund after the documents were acquired.<sup>87</sup>

Lord Toulson also commented on the distinction between commercial and traditional trusts discussed by Lord Browne-Wilkinson. He noted:<sup>88</sup>

... a commercial trust differs from a typical traditional trust in that it arises out of a contract rather than the transfer of property by way of gift ... [Commercial trusts] have in common that the trustee’s duties are likely to be closely defined and may be of limited duration. Lord Browne-Wilkinson did not suggest that the principles of equity differ according to the nature of the trust, but rather that the scope and purpose of the trust may vary, and this may have a bearing on the appropriate relief in the event of a breach ... [T]he terms of the contract may be highly relevant to the question of fact whether there has been a loss applying a “but for” test, that is, by reference to what the solicitors were instructed to do.

As such, Lord Toulson did ascribe some relevance to the fact that both *AIB* and *Target Holdings* concerned commercial trusts. Applying the above comments to the facts before him, he said:<sup>89</sup>

... in circumstances such as those in *Target Holdings* the extent of equitable compensation should be the same as if damages for breach of contract were sought at common law. That is not because there should be a departure in such a case from the basic equitable principles applicable to a breach of trust, whether by a solicitor or anyone else ... Rather, the fact that the trust was part of the machinery for the performance of a contract is relevant as a fact in looking at what loss the bank suffered by reason of the breach of trust ...

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82 At [73].

83 At [62].

84 At [64].

85 At [66].

86 At [63].

87 At [69].

88 At [70].

89 At [71].

## 2 Lord Reed's Reasons

Lord Reed, giving the second judgment, focused on other factors. He first discussed the *Canson Enterprises* decision in detail and Lord Browne-Wilkinson's reliance on it.<sup>90</sup> Lord Reed said that three key points can be derived from *Canson Enterprises*, the first of which is relevant for present purposes.<sup>91</sup> Lord Reed approved of McLachlin J's statement that, where a misapplication of property occurs, equity requires it to be restored.<sup>92</sup> And, where the property is gone, the court could award "compensation in lieu, with the ideal of restoring that which was lost through the breach of duty".<sup>93</sup> The conclusive principle distilled by Lord Reed from *Canson Enterprises* was: "[i]f the property cannot be restored in specie, the trustee must restore the trust fund to the position it *would have been in but for the breach*".<sup>94</sup> Critical here is reliance upon McLachlin J's judgment as holding that substitutive performance claims are still, in essence, compensatory or reparative.

Lord Reed then moved to analyse *Target Holdings*.<sup>95</sup> He noted Lord Browne-Wilkinson's observation that the court should order payment directly to the beneficiary where an unauthorised disbursement has been made but the trust no longer subsists.<sup>96</sup> "the measure of compensation is the same as if there had been an accounting and execution of the trust".<sup>97</sup>

He then turned to argument A in *Target Holdings*. Lord Reed agreed that it is artificial to order reconstitution of a client's trust account as there are no obligations left to perform under the trust.<sup>98</sup> Thus, argument A was dismissed on a procedural ground.<sup>99</sup> Moreover, if argument A succeeded, it would enable plaintiffs to recover more than they have lost. This outcome would be contrary to the basic principles of equitable compensation.<sup>100</sup> Neither an accounting nor a direct claim for compensation should allow for such a result.<sup>101</sup>

Regarding argument B, Lord Reed noted the criticism regarding the blurring of substitutive and reparative claims for compensation.<sup>102</sup> But he reiterated that Lord Browne-Wilkinson did not intend to depart from the so-called "orthodox view" that the "equitable obligation arising from a breach of trust affecting the trust fund is to restore the fund to the position it would have been in but for the breach".<sup>103</sup>

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90 At [80]–[89].

91 At [90].

92 *Canson Enterprises*, above n 69, at 546–547.

93 *AIB*, above n 2, at [85].

94 At [90] (emphasis added).

95 At [96].

96 At [99].

97 At [100].

98 At [106].

99 At [109].

100 At [107].

101 At [108].

102 At [115].

103 At [116].



Lord Reed then surveyed authorities postdating *Canson Enterprises* and *Target Holdings* — particularly those decisions which have approved, in substance, of *Canson Enterprises*.<sup>104</sup> These decisions are, currently, unnecessary to elaborate on. But they caused Lord Reed to state there is a consensus across jurisdictions that the correct approach to equitable compensation for breach of trust is as described by McLachlin J in *Canson Enterprises* and endorsed by Lord Browne-Wilkinson in *Target Holdings*.<sup>105</sup> Lord Reed concluded his judgment similarly to Lord Toulson:<sup>106</sup>

... where trust property has been misapplied, [the proper approach] is to require the trustee to restore the trust fund to the position it would have been in if the trustee had performed his obligation.

## V CRITICISM OF THE *AIB* DECISION

This part of the article evaluates the soundness of the analysis in *AIB* as to but-for causation. Lord Reed and Lord Toulson concluded that, where trust property has been misapplied, the remedy is to restore the trust fund to the position it would have been in had the breach not occurred. Several commentators have taken this to mean that *AIB* and *Target Holdings* have set a new general defence or rule that, unless a plaintiff establishes but-for causation, they will be precluded from recovering funds wrongfully dispersed.<sup>107</sup> Others more receptive to the traditional distinction between the substitutive performance claim and claims for reparation have wondered how — considering the Lords did not explicitly render the traditional accounting rules redundant — those rules might continue to operate in the post-*AIB* world.<sup>108</sup>

Clearly, the outcomes of the cases are contrary to the substitutive performance mechanism discussed above and have been asserted to constitute a “clear change in the law”.<sup>109</sup> Therefore, this first section of analysis is concerned with asking whether or not this change is grounded in sound legal reasoning. I begin with Lord Reed’s reasons and move to Lord Toulson’s.

### Lord Reed’s Judgment

Much of Lord Reed’s analysis drew on the minority judgment of McLachlin J in *Canson Enterprises*. Indeed, *Canson Enterprises* has been

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104 At [117]–[132].

105 At [133].

106 At [134].

107 See, for example, PG Turner “The New Fundamental Norm of Recovery for Losses to Express Trusts” [2015] CLJ 188 at 189; and Andreas Televantos and Lorenzo Maniscalco “Stay on target: compensation and causation in breach of trust claims” (2015) 4 Conv 348.

108 David Hayton, Paul Matthews and Charles Mitchell *Underhill and Hayton Law Relating to Trusts and Trustees* (19th ed, LexisNexis, London, 2016) at [87.42].

109 *MG&L*, above n 32, at [23-210].

acknowledged as the “intellectual roots” of the purported new rule in *Target Holdings* and *AIB*.<sup>110</sup> Therefore, it pays to first discuss *Canson Enterprises*.

*Canson Enterprises* concerned a breach of fiduciary duty by the defendant solicitors who acted for the plaintiff developers in a purchase of land. The solicitors did not disclose a third party was making a secret profit on the transaction. The development was not a success and the developers sought to recover all of their losses from the development from the solicitors.<sup>111</sup> At the time, the law regarding recovery for loss suffered through breach of fiduciary duty was somewhat unsettled in Canada. Instinctively, the substantive justice of the case warranted a clear application of some form of limiting principle. However, the case did not concern a breach of trust and, so, when Lord Browne-Wilkinson first applied McLachlin J’s test of common sense causation to what would traditionally have been a claim for substitutive performance, he was rightly criticised for drawing inappropriately from a case far removed from the accounting paradigm as regards a misapplication of trust property.<sup>112</sup>

In all fairness to Lord Reed, he did appreciate this distinction. But he relied on further dicta of McLachlin J to say that, when one has suffered a misapplication of trust property, and the property cannot be restored, the court awards “compensation in lieu, with the ideal of restoring that which was lost through the breach of duty”.<sup>113</sup>

McLachlin J did not engage with the traditional authorities cited above<sup>114</sup> and she addressed the matter in a rather perfunctory way. Such analysis is perfectly understandable. *Canson Enterprises* did not concern a breach of trust. But it was suspect for Lord Reed to rely on McLachlin J’s analysis as providing the intellectual cornerstone of his judgment when she never engaged with the principles of the substitutive performance claim. The problem is compounded because McLachlin J, in stating a but-for causation test applies to what are properly analysed as substitutive performance claims, relied solely on a Melbourne University Law Review article by Ian Davidson.<sup>115</sup> While that article explored claims for equitable compensation for breach of fiduciary duty, Davidson expressly did not engage with the principles governing breach by a misapplication of trust funds. Davidson was clear and said on the article’s first page:<sup>116</sup>

The well known equitable remedies where property held in a fiduciary capacity is misapplied will not be discussed. Attention will be directed to the much less certain position where a breach of other equitable obligations causes financial loss.

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110 At [23-210].

111 The developers tried to link their loss from the failure of the actual development to the failure to disclose the secret profit.

112 See Peter Birks “Equity in the Modern Law: An Exercise in Taxonomy” (1996) 26 UWALR 1 at 36–37.

113 *AIB*, above n 2, at [85].

114 Aside from mentioning en passant *Ex parte Adamson*, above n 41.

115 Ian E Davidson “The Equitable Remedy of Compensation” (1982) 13 MULR 349 quoted in *Canson Enterprises*, above n 69, at 548.

116 At 349 (footnotes omitted).

For such a clear change in the law to have occurred, something more was warranted than reliance on *Canson Enterprises* and McLachlin J's ill-conceived analysis as to breach of trust. Particularly when the majority judgment, given by La Forest J, explicitly rejected analogising equitable compensation for breach of fiduciary duty with a misapplication of trust funds. He was quite clear:<sup>117</sup>

There is a sharp divide between a situation where a person has *control* of property which in the view of the court *belongs* to another, and one where a person is under a fiduciary duty to perform an obligation where equity's concern is simply that the duty be performed honestly and in accordance with the undertaking the fiduciary has taken on. In the case of a trust relationship, the trustee's obligation is to hold the *res* or object of the trust for his *cestui que trust*, and on breach the concern of equity is that it be restored to the *cestui que trust* or if that cannot be done to afford compensation for what the object would be worth. In the case of a mere breach of duty, the concern of equity is to ascertain the loss resulting from the breach of the particular duty.

The other major point made by Lord Reed was that there is a “measure of consensus across a number of common law jurisdictions” that the correct approach “to the assessment of equitable compensation for breach of trust is as described by McLachlin J in *Canson Enterprises*”.<sup>118</sup> Lord Reed cited myriad cases for this controversial proposition.<sup>119</sup> The distinguished list of authorities proves unsatisfactory throughout. The majority of the cases did not even involve trusts, let alone a misapplication of trust property — neither did they engage with the principles governing substitutive performance claims described above.<sup>120</sup> Granted, in some of the other cases there is obiter which endorses *Target Holdings* as applicable to what would traditionally have been viewed as substitutive performance claims. Yet, similarly, two of these did not involve a trust, let alone engage with the traditional authorities.<sup>121</sup> Furthermore, although there are supportive dicta in *Bank of New Zealand v New Zealand Guardian Trust Co Ltd*, that case did not engage with the traditional authorities on substitutive performance claims.<sup>122</sup> The same goes for *Youyang Pty Ltd v Minter Ellison Morris Fletcher*.<sup>123</sup> And although in *Libertarian Investments* Ribeiro PJ suggested in obiter that

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117 At 578 (emphasis in original, footnotes omitted).

118 *AIB*, above n 2, at [133].

119 At [117]–[132].

120 *Amaltal Corp Ltd v Maruha Corp* [2007] NZSC 40, [2007] 3 NZLR 192; *Premium Real Estate Ltd v Stevens* [2009] NZSC 15, [2009] 2 NZLR 384; *Bristol and West Building Society*, above n 16; *FBI Foods Ltd v Cadbury Schweppes Inc* [1999] 1 SCR 142; *Hodgkinson v Simms* [1994] 3 SCR 377; *KM v HM* [1992] 3 SCR 6; *Breen v Williams* (1996) 186 CLR 71; *Pilmer v Duke Group Ltd (in liq)* [2001] HCA 31, (2001) 207 CLR 165; and *FHR European Ventures LLP v Cedar Capital Partners LLC* [2014] UKSC 45, [2015] AC 250.

121 *Maguire v Makaronis* (1997) 188 CLR 449; and *Thanakharn Kasikorn Thai Chamkat (Mahachon) v Akai Holdings Ltd (No 2)* (2010) 13 HKCFAR 479.

122 *Bank of New Zealand v New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 664 (CA) [*Guardian Trust*] at 679 and 687.

123 *Youyang Pty Ltd v Minter Ellison Morris Fletcher* [2003] HCA 15, (2003) 212 CLR 484. I query also whether this case is compatible with the reasoning in *AIB*. See Paul S Davies “Compensatory Remedies for Breach of Trust” (2016) 2 CJCL 65 at 82.

*Target Holdings* applied to claims for the misapplication of trust moneys,<sup>124</sup> again, he did not engage with the traditional authorities. There is also an obvious divide between his words and Lord Millett NPJ's judgment, quoted above, which shows how the substitutive performance claim cuts out but-for causation as it is commonly applied. In short, Lord Reed's survey of authorities is far from convincing so far as it purports to show an informed consensus across jurisdictions as to how claims for misapplied trust property should be treated.<sup>125</sup>

### Lord Toulson's Judgment

Turning to Lord Toulson's judgment — leaving aside his comments regarding commercial factors (which on his reasoning are only relevant as far as they assist in applying a but-for test) — I venture it is also unsatisfactory. First, a monetary award which reflects loss that would have been suffered in any event is not penal. It simply enforces a trustee's primary duty to account. All the court is saying is *do what you undertook to do*. The trustee must have assumed such duties voluntarily. A substitutive performance claim, although in personam against the trustee, finds its genesis in the existence of in rem rights — rights subjected to near-complete control by the relevant trustee.<sup>126</sup> This analysis links back to the uniqueness of the trust lying in the trustee's everyday control over the property of another. Why then is it harsh to hold a trustee to their bargain of maintaining safe custody? Lord Toulson does not provide a satisfactory answer, merely an assertion.<sup>127</sup>

Secondly, Lord Toulson's objection to fairy tales does not withstand scrutiny. His rejection here was in response to a submission from AIB that the proper solution to *Target Holdings* was to treat the moneys wrongly paid out as restored to the client account and then properly applied after the requisite documents were obtained.<sup>128</sup> Presumably, this submission was premised on Lord Millett's first appraisal of the case.<sup>129</sup> However, in my view, the submission misread Lord Millett's article. What Lord Millett is actually saying is that, as the disbursement was originally unauthorised, equity would treat the amount as *still in the client account* — it was dispensed without authority and, thus, the nominal account would deem the amount to still be there. But, since the documents were later obtained, equity would deem the money still there to have been properly dispensed. Granted, the process does have a touch of the ethereal. A more straightforward analysis can be proffered: as the documents were eventually acquired within

124 *Libertarian Investments Ltd*, above n 33, at [87].

125 See Davies "Compensatory Remedies", above n 123, at 79–80.

126 Charles EF Rickett "Equitable Compensation: Towards a Blueprint?" (2003) 25 Syd LR 31 at 47–48.

127 Further, on this analysis, all debt claims, even those brought at common law, would be penal. See Paul S Davies "Remedies for Breach of Trust" (2015) 78 MLR 681 at 685.

128 *AIB*, above n 2, at [69].

129 Millett, above n 72, at 227.

the solicitors' authority, their receipt could not be falsified.<sup>130</sup> Thus, it is ultimately a matter of crediting the authorised receipt against the unauthorised debit. Simple accounting, not fairy tales.

Lastly, there is nothing in the notion that it would be a backward step to depart from, or at least revise, *Target Holdings*. The House of Lords has said that overruling itself or — by extension — revising its own previous decisions, where such decisions impede the proper development of principle, “will promote and not impair the certainty of the law”.<sup>131</sup> Precedent that is bad precedent should be seen as no precedent at all. *Target Holdings* deserved to be revised and the reasoning of the Supreme Court in *AIB* is unsatisfactory and unconvincing. Indeed, jurists and scholars, such as William Gummow, have argued it was decided per incuriam.<sup>132</sup> These scholars would have had Mark Redler pay all GBP 3,300,000 subject to any credit subsequently received on the sale of the property.

However, no matter how principled the positions of Gummow and others might be in regard to their endorsement of the substitutive performance claim, having the solicitors in *AIB* repay all of the money wrongfully paid out seems intuitively unjust. Together with the factors mentioned in connection with *Target Holdings*, because the trusts in both were purely ancillary to a contractual agreement, the justice lay in claims similar to those available at common law.<sup>133</sup>

To summarise at this stage, both cases are unsatisfactory in their analysis regarding the proper response to a misapplication of trust funds, despite their outcomes being, in my view, correct. Detailed above, there are compelling reasons for the rigour of the substitutive performance claim. These reasons include the inherent vulnerability of beneficiaries in a traditional trust situation and the uniqueness of the trust construct as regards the vesting of property in someone which equitably belongs to another. However, these factors were minimised in both cases to the extent that it was fair not to apply the mechanism of the substitutive performance claim.

How then can the outcomes of both cases be rationalised such that the substitutive performance claim might live on in England and the new general rule not supplant orthodoxy in other common law jurisdictions? As noted, critics suggest that *Target Holdings* can be rationalised via traditional accounting principles. That is to say, the substitutive performance claim would have required Target to account for credit subsequently received. However, the dicta as to but-for causation in *Target Holdings* was endorsed and applied in *AIB*. In that case, AIB never received the equivalent of the

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130 Conaglen, above n 77, at 290.

131 See, for example, *Jones v Secretary of State for Social Services* [1972] AC 944 (HL) at 966.

132 See, for example, William Gummow “Three cases of misapplication of a solicitor’s trust account” (2015) 41 Aust Bar Rev 5; Nicholas A Tiverios and Clare McKay “Orthodoxy lost: The (ir)relevance of causation in quantifying breach of trust claims” (2016) 90 ALJ 231; and Charles Mitchell “Stewardship of property and liability to account” (2014) 3 Conv 215.

133 Michael Furness and Judith Bryant “Equitable compensation — clarity at last?” (2015) 21 T&T 1027 at [44].

documents that would have made the accounts balance in *Target Holdings*. As such, that reasoning is spent. And alternative analysis must be considered.

## VI DISTINGUISHING BETWEEN TYPES OF TRUST

I now discuss the distinction between commercial and traditional trusts, which was first mentioned by Lord Browne-Wilkinson in *Target Holdings*. I ask whether a distinction might be drawn, generally along those lines, to delineate what remedies are available in equity for a misapplication of trust funds. On this analysis, the outcomes and reasoning of *Target Holdings* and *AIB* would be confined to their facts and those of analogous cases. The cases can be confined on the ground that it is inappropriate to allow plaintiffs a claim of substitutive performance for a misapplication of funds from a trust so removed from the paradigmatic instances of trusts and devoid of many of the interests the strict doctrines developed to protect. This section explores this distinction.

### Equity's Intrusion into the Sphere of Commerce

Around the turn of the 20th century, the judges of England expressed a marked disapproval for the doctrines of equity to infiltrate the commercial world. As noted, the trust developed in order to protect land interests and to manage wealth in respect of private individuals. And naturally wishing to protect the vulnerability attaching to traditional beneficiaries, equity developed its strict and rigorous responses to breaches of trust. These doctrines — the onerous obligations imposed on trustees and the extensive rights bestowed on beneficiaries — were anathema to the commercial sphere. This is because, in the commercial sphere, parties were seen as needing to know immediately where they stood as regards a legal wrong and needing to have the freedom to commit, for example, efficient breaches of contract. In *The New Zealand and Australian Land Co v Watson*, Bramwell LJ said:<sup>134</sup>

Now I do not desire to find fault with the various intricacies and doctrines connected with trusts, but I should be very sorry to see them introduced into commercial transactions, and an agent in a commercial case turned into a trustee with all the troubles that attend that relation. I think there is no ground for holding that these defendants have any fiduciary character towards the plaintiffs.

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134 *The New Zealand and Australian Land Co v Watson* (1881) 7 QBD 374 (CA) at 382. See also *Henry v Hammond* [1913] 2 KB 515 (KB) at 521; and *Manchester Trust v Furness* [1895] 2 QB 539 (CA) at 545.

These observations show an understanding of equity as a rather distinct body of law — resplendent with unique rules, functions and remedies. The courts were reluctant to see the trust become a mechanism — useful or otherwise — for promoting commerce and assisting commercial transactions. Yet that is exactly what the trust has become.

As early as 1951 the English Judiciary expounded that:<sup>135</sup>

... the truth is that, as the principles of equity permeate the complications of modern life, the nature and variety of trusts ever grow, and it is perhaps rash to think of some conception of a trust having certain characteristic attributes ...

From then on, the trust has acquired only more commercial relevance. As noted by Lord Millett, “[t]he picture of the trustee or fiduciary as an old friend of the family who has gratuitously volunteered his services is long obsolete.”<sup>136</sup> Notably, a trust was recognised in the context of a loan arrangement between two commercial parties. There, the House of Lords said the intention to create a trust was evidenced by the lender’s clear indication to the borrower that the loan was to be used solely to pay a dividend and that the loan monies were to be left in a separate account.<sup>137</sup>

But trusts have not only been implied in commercial law. The express trust has also permeated commercial life. Take the pension trust for example.<sup>138</sup> This trust arises from contracts of employment providing for deferred compensation to be paid in retirement. The trust has also assumed prominence in other commercial situations.<sup>139</sup>

It is clear many of these commercial trusts bear similarity to the traditional trust discussed earlier. The only difference is that they arise in a commercial context rather than a purely private one. For example, the trustees of a pension trust will owe duties above and beyond the “irreducible core” of obligations set down in *Armitage*.<sup>140</sup> They will likely owe significant management duties as well. The trust mechanism here allows for a variety of beneficiaries’ interests to be managed for a specific purpose. Thus, it is clear that the trust can be a useful instrument for dealings in the world of commerce, despite what the courts may have said 100 years ago. And so, consistent with this trend, in both *Target Holdings* and *AIB*, neither party in either case disputed that the funds were held on trust of a type common in commercial transactions.

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135 *Re A Solicitor* [1952] 1 Ch 328 (Ch) at 332 per Roxburgh J.

136 Millett, above n 72, at 216.

137 See *Barclays Bank Ltd v Quistclose Investments Ltd* [1970] AC 567 (HL).

138 See Jamie Glistler and James Lee *Hanbury and Martin Modern Equity* (20th ed, Sweet & Maxwell, London, 2015) ch 17.

139 See generally Glistler and Lee, above n 138, at ch 3; and John H Langbein “The Secret Life of the Trust: The Trust as an Instrument of Commerce” (1997) 107 Yale LJ 165.

140 *Armitage*, above n 13, at 253.

## Bare Trusts in the Commercial Sphere

The trusts in those cases were not only commercial — they were also a species of bare trust. A bare trust arises where the trustee has no duties to perform and must deal with the trust property in accordance with the beneficiary's instructions.<sup>141</sup> Contrast this with a special, typical or traditional trust where the trustee has a wide variety of duties in respect of the trust property. Generally, a bare trust will arise where the beneficiary is absolutely entitled to the trust property and the beneficiary is, thus, entitled to call for a conveyance of the property at any time.<sup>142</sup> A bare trustee into whose name an absolute owner transfers property is sometimes called a "nominee".<sup>143</sup> Thus, Gary Watt has noted that many modern bare trustees are "in essence commercial agents (such as solicitors taking possession of purchase monies in the course of a conveyancing transaction)".<sup>144</sup> And so it was with the trusts in *AIB* and *Target Holdings*.

## A Wrongful Importation of Doctrine

The willingness of the courts to embrace the trust as part of the commercial world has resulted in some unsatisfactory developments. As the trust has moved into areas originally the domain of the common law, commercial arrangements far removed from the traditional trust paradigm have been upheld as trusts. As seen with the pension trust, the trust structure and the strict duties of trustees can, on occasion, make themselves useful instruments of commerce. However, even though some aspects of trust doctrine may find use in the business world, it is difficult to rationalise the other strict and unique aspects of the trust concept to the commercial sphere. In contrast to the strict duties owed by trustees to their beneficiaries:<sup>145</sup>

[I]n negligence and contract the parties are taken to be independent and equal actors, concerned primarily with their own self-interest. Consequently the law seeks a balance between enforcing obligations by awarding compensation and preserving optimum freedom for those involved in the relationship in question, communal or otherwise.

In giving effect to arrangements that are nominally trusts, and which make use of some facets of trust doctrine, the courts have looked over other aspects of these arrangements inimical to the trust concept. These other aspects are more readily applied to the spheres of negligence and contract law described by McLachlin J above. For example, one could point to, as regards the conveyancing accounts in *Target Holdings* and *AIB*: the lack of substantive custodial duties owed; the relevant duties being imposed by a contract; and the fund being a mere part of a larger transaction. Arguably, as

141 *Re Cunningham and Frayling* [1891] 2 Ch 567 (Ch) at 571–572.

142 Pursuant to the rule in *Saunders v Vautier* (1841) 4 Beav 115, 49 ER 282.

143 See *Ingram v Inland Revenue Commissioners* [2000] 1 AC 293 (HL).

144 Gary Watt "Contributory Fault and Breach of Trust" (2005) 5 OUCJLJ 205 at 214.

145 *Canson Enterprises*, above n 69, at 543.



these and similar arrangements are so removed from the trust concept, they should not be treated as trusts.

A prime example of this development is *Citibank NA v MBIA Assurance SA*.<sup>146</sup> Citibank was a trustee of debt notes issued to securitise Eurotunnel debt. The issuer covenanted with the noteholders, inter alia, to pay certain sums due on the notes. The noteholders were not of equal standing in terms of credit risk. Holders of the senior notes had the additional benefit of a guarantee given by MBIA. In order to protect its position as guarantor, MBIA was given, in the trust deed, the right to give Citibank instructions concerning Citibank's exercise of powers and discretions as trustee. Citibank had to obey such instructions and the deed provided that Citibank need not have regard to the interests of the noteholders when acting on MBIA's instructions. The deed also contained an extensive exemption clause absolving Citibank of all liability to the noteholders when acting on MBIA's instructions. The noteholders' position was that Citibank was not bound to act on MBIA's instructions if doing so would conflict with its natural duties as trustee. The Court of Appeal upheld the Chancery Division's decision that MBIA, indeed, had the relevant power and that Citibank was bound to follow its instructions. Naturally, as Alexander Trukhtanov says:<sup>147</sup>

The duties and liabilities that the office of trustee carries were liable to be circumvented by an instruction of MBIA; that instruction had the effect, by virtue of express provisions of the trust instrument, of removing the trustee's duty to act in the interests of the beneficiaries.

I consider there is a very strong argument the Court of Appeal's decision had the effect of reducing Citibank's obligations below the *Armitage* "irreducible core".<sup>148</sup> Arden LJ said that was not so because Citibank continued to have an obligation of good faith and it retained certain discretions under the trust deed not fettered by MBIA's powers.<sup>149</sup> However, as Trukhtanov points out:<sup>150</sup>

In effect, there [was] no longer a meaningful trust for the note-holders since MBIA controls all the important powers concerning the subject-matter of the trust. ... The commercial position in which Citibank, MBIA and the note-holders found themselves is difficult to translate in terms of traditional trust concepts.

This case shows clearly a willingness on the part of the courts to uphold trusts which are far removed from the traditional trust concept and where alternative (non-trust) rationales should be used to explain the relevant arrangement. Similarly, when upholding the fund in *Target Holdings* as a trust, Lord Browne-Wilkinson denied Target strict relief so that the "trust is

146 *Citibank NA v MBIA Assurance SA* [2007] EWCA Civ 11, [2007] 1 All ER (Comm) 475.

147 Alexander Trukhtanov "The Irreducible Core of Trust Obligations" (2007) 123 LQR 342 at 343.

148 *Armitage*, above n 13, at 253.

149 *Citibank NA*, above n 146, at [82].

150 Trukhtanov, above n 147, at 345.

not to be rendered commercially useless”.<sup>151</sup> But, in wishing to avoid the injustice in importing strict trust doctrines into a commercial context, he also laid down what has been shown to be an unsatisfactory rule of causation of purportedly general application. What again did Lord Toulson say in *AIB* about the commercial context of a trust as regards remedies? Only that “the terms of the contract [creating the trust] may be highly relevant to the question of whether there has been a loss applying a ‘but for’ test”.<sup>152</sup> Thus, in applying the trust rationale to a commercial bargain overlaid by a contract, the general trust principles which would act fairly when correctly applied to traditional trusts were erroneously diluted.

So, if one endorses the applicability of substitutive performance claims, how does one reconcile that strict approach to, for example, the *Citibank NA* type of trust? I suggest one cannot. These are trusts far removed from the traditional trust paradigm with beneficiaries having little vulnerability. In applying these strict doctrines one would be doing a substantive injustice — a fact I believe Gummow and others have overlooked. To quote Patrick Parkinson, the rules developed in relation to the “traditional trust created by a settlor transferring money or assets gratuitously to trustees [are] not readily conceptualised within the law of bargains”.<sup>153</sup> And perhaps that is what many of these purported trusts should be labelled: bargains. I propose that is a far more apt word than “trust” to describe the facts of *Citibank NA*. After all, why not just call a spade a spade? Such may be an option. Thus, in scenarios like *Citibank NA*, the courts should arguably invalidate such arrangements on the basis that, among other things, the *Armitage* core has been reduced. As Peter Devonshire writes:<sup>154</sup>

If effect is given to [contractual] terms that [abridge] the fundamentals of a trust or a general fiduciary relationship, then it must be recognised that, irrespective of form, a different legal construct is involved.

This analysis would render trust-based remedies unavailable. However, it would be hard to apply to conveyancing accounts, such as that in *AIB*, where the *Armitage* obligations are still present. The alternative reasoning is to recognise that the rules of equity should be of different application to different trusts.

### **A Dividing Line between Commercial and Traditional Trusts?**

This distinction, since proposed by Lord Browne-Wilkinson, has generally not been supported in the literature and has been labelled *unprincipled*.<sup>155</sup> William Gummow, for example, states it is wrong to say a “commercial

151 *Target Holdings*, above n 1, at 435H. See also Edelman “Money awards”, above n 59, at 127.

152 *AIB*, above n 2, at [70].

153 Patrick Parkinson “Reconceptualising the Express Trust” (2002) 61 CLJ 657 at 681.

154 Peter Devonshire “Account of Profits for Breach of Fiduciary Duty” (2010) 32 Syd LR 389 at 394.

155 See, for example, Edelman “Money awards”, above n 59, at 128; Gummow “Three cases”, above n 132, at 11; and Penner, above n 10, at 225–226.

context” can displace the operation of the law of trusts governing the solicitor-client relationship.<sup>156</sup> However, I propose it is not necessarily unprincipled to say that in relation to some trusts (if one upholds the arrangement as a trust), the availability of a substitutive performance claim may be denied. Such an outcome is not unworkable. And neither would the analysis be confined to a blunt dichotomy of traditional and commercial trusts as perhaps it seemed following *Target Holdings*.<sup>157</sup> The support this notion has received in literature recognises that the distinction is not so blunt, nor would Lord Browne-Wilkinson have intended it to be. As Sir Anthony Mason has stated:<sup>158</sup>

... parties from time to time structure their commercial arrangements in such a way as to generate an equitable interest or an equity. But ... the importation of equity is so inimical to the interests of commerce as to amount to an important policy consideration which is influencing the shape of English law as it affects commercial transactions between commercial parties standing at arm’s-length. ... Some modification is essential if trusts and equitable relationships are to be of utility to commerce.

Thus, the question of whether the strict remedies are available would not merely inquire into whether a trust was traditional or commercial. It would constitute a larger taxonomical inquiry as to what duties are owed under the trust and the degree of similarity to the traditional trust paradigm. Lord Browne-Wilkinson’s words properly interpreted, in my view, are that there will be some instances of trusteeship far removed from the traditional trust paradigm and undeserving of the traditional strict remedies. And these instances are inherently more likely to arise in a commercial setting. As Katy Barnett has noted, with commercial trusts where limited duties are owed or where the trust only subsists for a short period of time as part of a larger transaction, “the substitutive concerns are not the same” as with a traditional trust.<sup>159</sup> It would reek of unfairness in such contexts for a beneficiary to be indemnified for events occurring long after the breach and where other third parties are more closely linked to the loss.<sup>160</sup> The distinction is perhaps best put by Richard Nolan:<sup>161</sup>

One might say those engaged in commerce, who vest property in a nominee so that the nominee can deal with it on behalf of the beneficial owner, should not necessarily be able to look to the nominee as, in effect, a guarantor of the integrity of the fund. ... the law is not so wrong to treat the arrangement as being in substance, if not in form, more akin to agency than to other instances of trusteeship, so that the duties of a nominee are more like those of an agent than those of an active trustee.

156 Gummow “Three cases”, above n 132, at 11.

157 See Edelman “Money awards”, above n 59, at 127.

158 Anthony Mason “Equity’s Role in the Twentieth Century” (1997) 8 KCLJ 1 at 7–8.

159 Katy Barnett “Equitable compensation and remoteness: not so remote from the common law after all” (2014) 38 UWAL Rev 48 at 74.

160 At 74.

161 Richard Nolan “A Targeted Degree of Liability” [1996] LMCLQ 161 at 162.

The rejoinder of Tiverios and McKay would be that, “by including a trust instrument as part of their relationship, the parties may have intended to benefit from the additional protection afforded by traditional trust rules”.<sup>162</sup> I contend this point is unconvincing. The better view is that of Peter Watts who states, at least in regard to scenarios such as *Target Holdings* and *AIB*, that the usefulness of the trust mechanism derives from the beneficiary’s potential rights against parties other than the nominee if a breach were to occur.<sup>163</sup> The other alternative is that the trust has pervaded commerce to an extent that such arrangements are entered into merely as a matter of routine. Regardless, in contexts where limited duties are owed, or where a trust subsists as a cog in a larger transactional machine, it is difficult to hold that parties intended the substitutive performance claim to be available when such was intended to vindicate the onerous duties owed under traditional trusts.

As to the criticisms that such a distinction is unprincipled, I would say the opposite. If one recognises the substitutive performance doctrine arose in the context of the traditional trust — reflecting the dynamics of such a relationship — it is principled to limit the doctrine to those instances when the trust concept has developed far beyond its original parameters.<sup>164</sup> Rather, it is unprincipled to apply the strict doctrines without regard to the wider context in which they are operating. As the learned authors of *Underhill and Hayton Law Relating to Trusts and Trustees* write:<sup>165</sup>

... [*AIB*] concerned a [bare trust in a commercial transaction] and this made it appropriate to depart from the rules applicable to traditional trusts which were not within the reasonable commercial expectations of the parties.

By importing limiting principles to certain trusts, equity can be seen to maintain its traditional flexibility and discretionary nature. It will lead to fair outcomes like that which the Lords tried to achieve. But why should the original equitable principles, which are justly applied to traditional trusts, be disturbed from their proper application? To do so is to replace one inequity with another.

On the foregoing analysis, to rationalise *AIB* its dicta as to but-for causation should be confined to scenarios where the dynamics of the traditional trust relationship have been abridged. If the case is rationalised as such, then the substitutive performance remedy would still be available to beneficiaries of a traditional trust, but unavailable to those in circumstances such as *AIB*’s. As *AIB* and *Target* could only seek a reparative claim, the analysis in *AIB* as to causation can be limited to such.

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162 Tiverios and McKay, above n 132, at 241.

163 Peter Watts “Agents’ Disbursal of Funds in Breach of Instructions” [2016] LMCLQ 118 at 122.

164 This analysis can be analogised to that concerning the flexibility of the fiduciary principle.. See Devonshire, above n 154, at 390.

165 Hayton, Matthews and Mitchell, above n 108, at [87.36].

## VII A MORE SUBTLE EXAMINATION OF THE RELEVANT BREACH OR DUTY

This final section proposes a potentially less ambiguous way of rationalising the cases. Even though the foregoing analysis is sound in principle, it would be hard to set down a bright-line test centred on the category of trust as to when substitutive performance claims are available. And lawyers love bright-line tests. Regarding academic commentary, ambiguity has permeated the rationalisations of *AIB* by those supportive of substitutive performance claims maintaining a place in the law. The leading text most supportive of such, *Underhill and Hayton Law Relating to Trusts and Trustees*, says that:<sup>166</sup>

... [*Target Holdings* and *AIB*] create an exception to [the] basic principles. This exception requires claims for the reconstitution of depleted trust funds to be treated as though they were not substitutive performance claims but reparation claims in cases where the trust has been exhausted and the trust fund has become absolutely vested in possession and/or where money has been paid out of a bare trust arising as an incident of a wider commercial transaction.

Thus, the learned authors would limit the application of the two cases to essentially their exact facts. This analysis cannot be correct. First, there are too many dicta in the cases supporting a wider application, rather than the cases having been decided on their own facts. Secondly, if there was a typical wrongful payout from a bare trust in a traditional context which depleted the fund, surely that would be deserving of the strict application of a substitutive performance claim, even if the requisite amount was paid directly to the beneficiary.<sup>167</sup>

### Premise

In this section I propose that the cases can also be rationalised by applying the modern doctrine as to breach of trust — supported by the Lords in *AIB*.<sup>168</sup> This doctrine says that, when determining the appropriate remedy for a breach of trust, one looks to see what duty has been breached by the trustee.<sup>169</sup> In particular, as noted above, not all duties owed by a trustee are fiduciary.<sup>170</sup>

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166 At [87.31].

167 See *AIB*, above n 2, at [108].

168 At [55] and [59]–[60].

169 At [59]–[60].

170 *Bristol and West Building Society*, above n 16, at 17–18 per Millett LJ. Prior to enunciating this rule, Millett LJ endorsed the comments of Ipp J in *Permanent Building Society (in liq) v Wheeler*. See *Permanent Building Society (in liq) v Wheeler* (1994) 11 WAR 187 (SC) at 237 and 239. But see *Clough v Bond* (1838) 3 My & Cr 491, 40 ER 1016.

Although the remedy which equity makes available for breach of the equitable duty of skill and care is equitable compensation rather than damages, this is merely the product of history and in this context is in my opinion a distinction without a difference. Equitable compensation for breach of the duty of skill and care resembles common law damages in that it is awarded by way of compensation to the plaintiff for his loss. There is no reason in principle why the common law rules of causation, remoteness of damage and measure of damages should not be applied by analogy in such a case. It should not be confused with equitable compensation for breach of fiduciary duty [or with a misapplication of trust funds which would normally sound in a substitutive performance claim] ... The nature of the obligation determines the nature of the breach.

This doctrine has since become orthodox in England and New Zealand.<sup>171</sup>

In applying this analysis to the cases, I stress that both Redferns and Mark Redler committed a breach of trust when performing their one key duty under the trust instrument — to release the funds in accordance with the beneficiaries' instructions. They were given a direction by the beneficiaries to pay out and, while assumedly well-intentioned, did not do so in accordance with the instructions. They performed their duties negligently. Or, on a different view, they breached their instructions — they committed a breach of contract. Analysed this way, the claims in both cases were analogous to common law claims — the breaches are readily conceptualised as claims for negligent breaches of an equitable duty of care or for breach of contract. As Geoffrey Vos says:<sup>172</sup>

... where true equitable remedies lie, true equitable principles should be applied. Where a claim is framed in equity, even though it is exactly analogous to a common law claim, then the same rules of causation must apply to both.

In my view, it is intuitive that a strict substitutive performance claim was unsuitable to the wrongs committed. Neither Redferns nor Mark Redler had any substantive custodial duties that, when breached, would traditionally attract the vigour of trust analysis. In both cases, there was an absence of hefty trust obligations — the parties in breach only had to pay out when they were told to. Neither scenario called for a strict trust-based response, and framing a claim based on misapplication of the trust funds was opportunistic. On this hypothesis, having regard to the duty breached, AIB and Target should have been limited to a claim for breach of contract; or, given the trust context, for negligent breach of trust. But how does one rationalise this analysis with the current categories of breach which hold that damage to a trust fund will attract the most vigorous of equitable remedies?

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171 See, for example, *Guardian Trust*, above n 122, at 687; and *Novoship (UK) Ltd v Mikhaylyuk* [2014] EWCA Civ 908, [2015] QB 499 at [106]. But see *Youyang Pty Ltd v Minter Ellison Morris Fletcher*, above n 123, at [39].

172 A current Lord Justice of Appeal. Geoffrey Vos "Linking Chains of Causation: An Examination of New Approaches to Causation in Equity and the Common Law" (2001) 60 CLJ 337 at 345.

## Surveying the Literature

Writing shortly after *Target Holdings* was decided, Raymond Davern suggested “the contractual terms are sufficient in law to determine how a bare trust may be terminated”.<sup>173</sup> He appears to suggest, however, that this analysis would only apply to a direction to pay out and bring a bare trust to an end. Taking a more expansive approach, Davern’s analysis could apply to all trusts regulated by contracts. Where a breach has occurred, contract would trump trust law if appropriate. This analysis could apply to scenarios, such as in *Royal Brunei Airlines Sdn Bhd v Tan*, where all relevant trust obligations were essentially to pay funds out periodically in accordance with the underlying contract.<sup>174</sup> However, I venture there is no compelling reason for limiting the analysis to those trusts regulated by contracts. The reply is as the Lords gave in *AIB* — there is nothing, per se, in a trust arising from a contract. To take a wider view:<sup>175</sup>

There is a world of difference between a trustee’s failure to do only what he is authorised and obliged to do (when there is an unauthorised entry in the accounts that can be falsified) and his failure to exercise the requisite degree of care in performing his undertaken functions (so the relevant entry in the accounts cannot be deleted, the accounts, instead, having to be surcharged with the amount needed to make reparation for the relevant loss) ... [there is a] practical logic [in] not treating negligent conduct as unauthorised conduct and of the merits of distinguishing between strict liability for doing what is not authorised to be done ... and liability for negligently doing what is authorised to be done ...

Hayton makes a compelling case for rationalising some breaches which are in form a misapplication of funds, yet in substance a breach of a duty of care, as the latter.

Granted, this way of rationalising *Target Holdings* and *AIB* is likely to have its critics. It would involve something of a reimagining of the current categories of breach and the remedies that attach to each.<sup>176</sup> For example, both Gummow and Mitchell are strident in their shared belief that a dispersal of trust funds must sound in a substitutive performance claim.<sup>177</sup> But again, they are not recognising the substantive justice in the cases. If the cases are to be rationalised in a way that preserves substitutive performance claims in England, a rationalisation along these lines should be endorsed. If the law has reached a stage where it must choose between substitutive performance claims, or having every wrongful disbursement categorised as the most severe breach, the justice lies with the former.

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173 Raymond Davern “The Problem with Bare Trusts in Contractual Contexts: A Simple and Orthodox Solution” (1997) 8 KCLJ 86 at 95.

174 *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 (PC).

175 David Hayton “Unique Rules for the Unique Institution, the Trust” in Simone Degeling and James Edelman (eds) *Equity in Commercial Law* (Lawbook Co, Sydney, 2005) 279 at 290 and 292.

176 See Tipping J’s outline in *Guardian Trust*, above n 122, at 686–687.

177 Gummow “Three cases”, above n 132, at 10; and Mitchell “Stewardship of property”, above n 132, at 216.

This solution has also received some support in the case law. Several years after it was decided, Robert Walker LJ distinguished the facts in *Target Holdings* from those before him:<sup>178</sup>

... whereas the trust in *Target Holdings* was ... simply an aspect of a wider commercial transaction involving agency, the fiduciary obligations undertaken in this case ... involved heavy and continuing responsibilities for the stewardship of the company's assets. ... [T]his is a wholly different case from *Target Holdings*, in which ... the solicitors were shown to have done no more than to have acted imprudently in disbursing their client's funds before they obtained their client's security.

As Robert Walker LJ's analysis suggests, a realistic appraisal of circumstances is needed in this area. Where claims are properly considered in the common law sphere, despite operating in a trust context, courts should be cautious in applying a strict trust rationale to the question of remedy. Where substantive justice lies in applying limiting principles (such as in *Target Holdings* and *AIB*) rigorous trust doctrine — more relevantly applicable to traditional express trusts — is likely to be wrongfully diluted. That is what equity should strive to avoid here.

Thus, upon examining the substance of the claims in *Target Holdings* and *AIB*, it is evident that they should have been again limited to claims for reparation. Viewed in this way, the analysis as to causation would be limited to claims which are properly analysed as a breach of an equitable duty of care and not to substantive misapplications of trust funds.

## VIII CONCLUSION: LOOKING TO THE FUTURE

To conclude, despite their outcomes being correct, both *Target Holdings* and *AIB* are unsatisfactory in their analysis as to causation and recoverable loss for a misapplication of trust funds. The disregard for meritorious and long-established equitable principles is not grounded in sound reasoning and respect for such principles was lost on the Lords' quest to achieve substantive justice. Thus, I have sought to present two alternative ways in which the cases might be interpreted so that substitutive performance claims might live on in the law.

If *Target Holdings* and *AIB* are not rationalised along one of the two bases advanced in this article, the modernists (PG Turner and others) win out. The alternative is to concede that there is a general defence of causation applicable to claims for breach of trust and that substitutive performance claims no longer exist as part of the law.<sup>179</sup>

178 *Bairstow*, above n 76, at [53]–[54]. See also *Youyang Pty Ltd v Minter Ellison* [2001] NSWCA 198 at [97] per Young CJ in Eq.

179 PG Turner “The New Fundamental Norm”, above n 107, at 189; *MG&L*, above n 32, at [23-180]; *Televantos and Maniscalco*, above n 107, at 351; Davies “Remedies for Breach of Trust”, above n 127, at 693; and David Wright “Another wrong step: equitable compensation following a breach of trust” (2015) 21 T&T 825 at 842.



But, as I have shown, that is the least desirable outcome. The substitutive performance claim was never engaged with by the Lords on a satisfactory basis. Furthermore, as noted by Ruo Yu Tan, when applied in contexts and to breaches it was originally applied to, the result is a just one.<sup>180</sup> Lusina Ho, despite supporting the reasoning of both cases, also recognises this issue.<sup>181</sup>

... it is true that as compared to the traditional mechanism of falsification, the doctrine of causation has the potential of exonerating a trustee when equity might not wish to do so.

Perhaps most tellingly, Lord Toulson himself recognised there might be an exception to the general rule premised on fraud.<sup>182</sup> But an exception for actual fraud would run counter to the historical objectives of the substitutive performance claim<sup>183</sup> — it did not aim to punish fraud, but to sanction unauthorised conduct by trustees. Lord Toulson's acknowledgement that the substitutive performance claim can work justice in certain contexts underscores the weakness of the Lords' reasoning. Hopefully, in time, the Supreme Court will venture once more unto the breach of a trust and recognise this.

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180 Ruo Yu Tan “Substitutive performance claims for breach of trust: final nail in the coffin? *AIB Group (UK) Plc v Mark Redler & Co Solicitors* [2014] UKSC 58” (2015) 21 T&T 565 at 569. See also Furness and Bryant, above n 133, at [45].

181 Lusina Ho “Equitable Compensation on the Road to Damascus?” (2015) 131 LQR 213 at 217.

182 *AIB*, above n 2, at [62].

183 See comments of Somers J in *Aquaculture Corp v New Zealand Green Mussel Co Ltd* [1990] 3 NZLR 299 (CA) at 302.