THE SCOPE FOR, AND EXTENT OF, PROPRIETARY CLAIMS

Hon Mr Justice David Hayton, JCCJ

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1. Tracing principles are relevant to claims for personal relief as well as proprietary relief

It is worth noting at the outset that tracing principles are relevant to the extent not just of proprietary relief but also of personal relief in a "knowing receipt" claim against a defendant who, knowingly or unconscionably, dealt with property subject to a trust or other fiduciary duty in a manner inconsistent with such duty[1]. Thus if such property received by D when worth $1 million had become worth $4 million when knowingly dissipated by D, D will be *personally* liable for $4 million. If D still had such traceable property, then the claimant, C, would have a continuing equitable *proprietary* interest in it affording him priority over D's creditors.

As you might expect, when tracing principles are applied in the case of a claim for personal relief so that the success of the claim will not afford priority over the defendant's unsecured creditors, a judge, in assessing the evidence and drawing inferences, is more easily satisfied that property can be traced into the defendant's hands than where there is a claim for proprietary relief that will have priority over unsecured creditors of the defendant and any gratuitous transferees of the relevant property and any subsequent equitable chargees of such property. In reading cases concerned with tracing it is thus important to note whether the tracing process is in support of a claim for personal or proprietary relief. This is apparent when we later examine the approach of the Jersey Royal Court and Court of Appeal in *Federal Republic of Brazil and Municipality of Sao Paulo v Durant International Corporation and*

[1] E.g. *El Ajou v Dollar Land Holdings Ltd* [1994] 2 All ER 685

Kildare Finance Ltd (the *Sao Paulo* case)[2], but first we need to remind ourselves of tracing principles.

2. What is required to invoke the tracing principles?

Traditionally, the right to trace has been regarded as an equitable right that requires the claimant to have had an equitable interest in property or the benefit of an equitable fiduciary relationship affecting his property[3], so as then to be able to trace the property and its proceeds of sale through mixed bank accounts, traditionally regarded as impossible at common law[4]. This has led to stretching the concept of a fiduciary relationship to breaking point. It has even been suggested[5] that a thief of X's property will hold such property on constructive trust for X, even though the thief has no ownership capable of being held on trust – only a thief of cash as legal tender can become the legal owner. This absurdity avoids the greater absurdity of a distinction between the case where a thief steals a painting held by T on trust for B where tracing of the proceeds of sale through mixed bank accounts is available and where he steals a painting owned by B where, otherwise, such tracing would be unavailable.

Lords Steyn and Millett[6], however, have in *obiter dicta* made it clear that the tracing process belongs to the realm of evidence as an identification process to see if the claimant's assets can somehow be linked to assets now or formerly owned by the defendant. If they can be, it is at that point that the legal or equitable nature of the claimant's rights and the personal or proprietary nature of the relief become relevant. The doctrine of precedent, however, has caused English courts[7] to consider themselves bound to follow binding Court of Appeal authority and so stretch to the utmost the concept of a fiduciary relationship or constructive trust in order to enable invocation of the tracing process. The Jersey Court of Appeal in the *Sao Paulo* case, however, free from any binding precedent, has preferred the approach of Lords Steyn and Millett. It seems to me that other offshore jurisdictions could take the same approach but may

[2] [2012] JRC 211, strongly affirmed [2013] JCA 071
[3] *Agip (Africa) Ltd v Jackson* [1991] Ch 547, *Re Diplock* [1948] Ch 465
[4] *El Ajou v Dollar Land Holdings Ltd* [1993] 3 All ER 717
[5] *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] AC 696 at 716
[6] *Foskett v McKeown* [2001] 1 AC 1092 at 113 and 129-1340 respectively
[7] E.g. *London Allied Holdings Ltd v Lee* [2007] EWHC 2061 (Ch) at [256]-[257] and see note 3 above

cautiously rely, instead, on straining the concepts of fiduciary relationships and constructive trusts as the English courts have done.

It is worth noting that the tracing process is not frustrated by assets moving from a jurisdiction with extensive tracing rules to jurisdictions like civil law jurisdictions ignorant of trusts and not having extensive tracing rules[8] (though perhaps having some limited proprietary subrogation rules). Equitable rights can be asserted in respect of assets situated in jurisdictions having no concept of equitable proprietary rights so long as the defendant is amenable to the jurisdiction of a court in a State where such rights can be enforced *in personam* against the defendant[9]. Moreover, the claimant's ability to trace his money or other assets is dependent on the notional exercise of a power to impose a charge over a mixed fund of money or a power to treat all or part of a particular asset as notionally owned by the claimant, not on any actual exercise of such a power. A common law court can be regarded as having a floating lasso over traceable assets as they move from jurisdiction to jurisdiction until arriving in the common law jurisdiction whereupon the lasso descends and catches the traced assets.

3. Claimant's money mixed with wrongdoer's money in bank accounts

Since we are dealing with fungible money, the starting point is that the claimant, C, has a first charge over the mixed fund and so also of any asset acquired out of it. Thus if C's money was paid into a wrongdoer, W's, account No 1 and some money thereout was paid into a No 2 account and a No 3 account, C has an equitable charge as security for his money over all the money remaining in the three accounts. This equitable charge would also extend to any asset acquired with money from any of those accounts. What, however, if such an asset had appreciated in value?

The rule is that where W wrongfully uses C's money and his own to buy an asset, C has the option, instead of claiming a charge over it, to claim a proportionate share of the asset if it has increased in value[10]. Because W is to blame for mixing up C's funds with his own he is not in a position to rebut whatever C claims. C may claim that money

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[8] *El Ajou v Dollar Land Holdings Ltd* [1993] 3 All ER 717 at 737
[9] *Webb v Webb* [1994] QB 696
[10] *Foskett v McKeown* [2001] 1 AC at 130

withdrawn from the account to pay off W's debts and living expenses was W's own money honestly and rightfully withdrawn by W, leaving the remaining money as subject to C's charge[11]. C may claim that other money that W withdrew to buy an asset that has appreciated in value was C's money rightfully withdrawn by W, as a fiduciary not allowed to profit himself, so as to buy an asset for C. C can "pick and choose" to his best advantage[12].

A problem, however, arises if the balance in W's bank account falls to nil or becomes a debit with an overdraft facility. Subsequent payments into *his own account* are presumed to be of his own money for himself and not to remedy his wrongdoing and, in any event, if the account is overdrawn will *pro tanto* discharge a debt. Thus C will have no claim against the account or in respect of assets subsequently purchased out of that account unless he can show that the money that was paid into that account *in credit* after the balance had fallen to nil represented the proceeds of sale of a traced asset of C.

Similarly, if $50,000 of C's had been paid in to W's bank account in credit but the lowest intermediate balance had been a credit of, say, $21,000, then even if $60,000 were in W's account when C claimed his $50,000 C could only claim in respect of that $21,000 lowest balance. This is often referred to as the *Roscoe v Winder* principle[13].

A further issue is whether "backwards tracing" is possible[14] where an asset is acquired using a loan and the purchaser intends to and subsequently does repay the loan using traceable funds? This can arise in conjunction with overdrafts where the rule is that money paid to discharge an overdraft is dissipated in payment of a debt. What if W has three accounts with Banks X, Y and Z respectively and has a regular overdraft facility of $100,000 with Bank Y. He has $40,000 of C's money in Bank X which he intends to transfer through Bank Y into Bank Z. On day 1 W, when utilising $1,000 of the overdraft facility with Bank Y, extends the overdraft to $41,000 by writing a cheque to pay $40,000 from Bank Y to Bank Z, knowing that he has $40,000 of C's money in Bank X

[11] *Horizon Bank International Ltd v Walsh* [2009] CA Bda 6 Civ at [89]
[12] *Foskett v McKeown* at 130-131, *Shalson v Russo* [2005] Ch 281 at [144]
[13] [1915] 1 Ch 62
[14] See M Conaglen 'Difficulties with Tracing Backwards' (2011) 127 LQR 432

which he will shortly be paying into Bank Y. He does pay it in on day 4. On the face of it, this $40,000 paid into Bank Y pays off $40,000 of the $41,000 overdraft, so that the money has been dissipated in discharging a debt. Thus tracing the $40,000 is impossible. Is backwards tracing, however, possible to trace the $40,000 paid on day 4 back to the $40,000 paid on day 1 out of Bank Y?

Problems also arise as to clearing of cheques. Surely, it should be possible to trace a cheque for, say, $50,000 where a cheque for $50,000 comprising C's money is cleared in W's Bank A three hours after or even a day or two after Bank A had transferred $50,000 to W's Bank B on W's instructions? Should it make any difference if, instead of W's account with Bank A having a credit in excess of the $50,000 paid out to Bank B all or part of this earlier payment had come from an overdraft facility?

Should there, indeed, be hard and fast rules as to "backwards tracing" and the "lowest intermediate balance" or should the court be more concerned with questions of evidence, not issues of fixed legal principle? According to the Jersey Court of Appeal in the *Sao Paulo* case at [50], it is simply a question of evidence depending "on the application of protean concepts of equivalence and substitution." Thus it concluded at [69] "The question in any given case is whether the plaintiff can establish a sufficient link between the asset of which he has been deprived and the asset into which he is seeking to trace." It may be that the defendant's original subjective intentions assist the court but this is merely one means of identifying a sufficient link.

The Sao Paulo case

The Royal Court, in dealing with a claim for personal and proprietary relief, found that, as a result of a wide-scale fraud, monies of the Municipality of Sao Paulo that should have been used in major construction projects were diverted in breach of fiduciary duty into the hands of Paulo Maluf (mayor of Sao Paulo) and his son, Flavio, as bribes, commissions or 'kick-backs'. Expert evidence of Brazilian law indicated that the Municipality retained a proprietary claim, no title to the stolen money having passed to the Malufs.

Via coded bank accounts and unidentified black-market currency dealers ("*doleiros*") dealing with the stolen Brazilian money, US$10,500,000 ended up held for the Malufs in a New York bank account controlled by them. The Court held that the claimant had made out a case, which in the absence any other explanation, more than justified the conclusion that the US$10,500,000 represented the Municipality's money even though there was a "black hole" or "maelstrom" created by the Malufs so that the exact route by which the funds reached their destination could not be determined. The defendants had not been able to discharge the evidential burden of displacing such conclusion by showing where the New York bank money had come from and why.

The US$10,500,000 or, at least, $7,700,000 thereout were transferred to a Jersey Bank account of Durant International and then the majority of the monies were paid into the Jersey Bank account of Kildare Finance, the wholly owned subsidiary of Durant. These companies were indirectly owned and controlled by the Malufs. Thus, the knowledge of the Malufs was attributed to those companies so as to establish both personal and proprietary liability of the two companies if the monies could be traced into the Jersey Bank accounts that had earlier been frozen to await the outcome of the trial.

The Court held that the monies could be traced into the Jersey Bank accounts. The fraudulent theft of the Municipality's money in breach of fiduciary duty sufficed to enable tracing principles to be applied. Indeed, fraud usually involves a breach of a fiduciary relationship sufficient to enable tracing principles to be applied. The Royal Court, however, strongly considered that tracing principles should be generally available, irrespective of any fiduciary relationship, as an evidential process (as suggested by Lords Steyn and Millett in *Foskett v McKeown*). They should even be available where the claimant had a legal beneficial interest in the relevant property but no equitable interest separate from the legal interest e.g. where a robber stole a person's gold bars or painting in which no separate equitable interest existed or where, as here, no equitable proprietary interest could exist under Brazilian law. The Court of Appeal endorsed this at [51], stating that the law of Jersey "does recognise tracing as a unitary concept" with no separate rules of equitable and common law tracing.

The defendants claimed that only US$7,700,000 could be traced into the Jersey Bank accounts as a result of either (a) the last three payments into the New York Bank having been made after the final payment to Durant's Jersey Bank, "backwards tracing" not being possible or (b) a claimant not being able to claim beyond the lowest intermediate credit balance in the New York Bank under the principle in *Roscoe v Winder.*

The Jersey Royal Court at [219] was not prepared to enable a sophisticated fraudster to defeat an otherwise effective tracing claim simply by manipulating the sequence in which credits and debits were made to his bank accounts, particularly where "there is no question of possible insolvency and prejudice to unsecured creditors."   "The question is simply whether there is sufficient evidence to establish a clear link between credits and debits to an account, irrespective (within a reasonable timeframe) of the order in which they occur or the state of balance in the account. It is unnecessary to posit any limitation on how, as a matter of evidence, the necessary link might be proved: it might be by means of bank documentation or by reference to the account-holder's intentions or in some other way. Nor is there any cause to diminish the effect of such a link, once recognised, by introducing the concept of a 'lowest intermediate balance rule'."

The Court of Appeal at [61] cited the Royal Court as above, having itself at [58] emphasised that "the fundamental question in any given case is whether the plaintiff can establish a sufficient link between the property of which he was originally deprived and the property into which he is seeking to trace" and at [59] having indicated that *Roscoe v Winder* turned on its particular facts in the considerable difficulties of establishing the necessary links between the property of which the plaintiff had been deprived and any credit balance in excess of the lowest intermediate balance. Like the Royal Court the Court of Appeal found sufficient links – see [66]-[69].

Thus, the claimants had a proprietary claim to the US$10,500,000 frozen in the defendants' Jersey Bank accounts, as well as the two defendants being personally liable [as constructive trustees] for such amount. The Court of Appeal upheld the award of interest at US Prime Rate plus 1% compounded with monthly rests.

The English *Relfo Ltd v Varsani*

In *Relfo Ltd v Varsani*[15] (leave to appeal granted by the Court of Appeal[16] 11 April 2013) Sales J had also taken a broad approach to tracing the payment of funds where there was a lack of evidence in a proprietary claim and a personal knowing receipt claim against the defendant. On 4 May 2004 Mr Gorecia, controlling director of Relfo, an English company, in breach of his duties to the company, caused it to pay US$890,050 to a Latvian bank account of Mirren Ltd, a BVI company, in relation to a venture with a Ukrainian businessman. On 5 May 2004 Intertrade Group LLC, a Wisconsin company, used by Ukrainian businessmen, paid $878,479.35 from its Lithuanian bank account to Mr Varani's Singaporean bank account. After deduction of a $10 banking fee $878,469.35 was credited to the Singaporean account. It just so happened that $878,479.35 was 1.3% less than $890,050. The judge found it probable that this percentage represented a handling fee for Mr Gorecia's dubious Ukrainian business associates who were used to preparing corrupt and fraudulent accounting books and records and to effecting payments which obscured the true source of monies and the purposes for which they were paid: see [59], [66] and [77]. At [77] the judge stated, "Mr Gorecia caused the Relfo/Mirren payment to be made, intending to produce the result that the funds so paid should, by means to be devised by his Ukrainian contacts, be paid on to Bimji Varsani, and it is likely that they acted so as to bring about the result which Mr Gorecia asked them to produce."

No proprietary tracing claim could lie since Relfo's liquidator had produced no evidence to show that money remained in Mr Varsani's Singaporean bank account or that payments had been made thereout to acquire particular assets. Nevertheless, a personal liability [as constructive trustee] for the traced $890,050 arose since the judge found that Mr Varsani was aware that he had received it in breach of Mr Gorecia's duty.

Conclusions

To my mind the proper approach is to regard the tracing process as an evidential one in all the circumstances. Where the claim is only a claim to monetary relief against the wrongdoer, so that the claimant will only be an unsecured creditor, the court should be

[15] [2012] EWHC 2168 (Ch)
[16] [2013] EWCA Civ

quite ready to find a sufficient link between the asset of which the claimant has been deprived and the asset into which he is seeking to trace the value of the original asset. Where the claim is to proprietary relief the court should be more cautious in ascertaining whether there is a sufficient link because the claimant will become a secured creditor, though if the wrongdoer's wealth makes this of little significance the court should still be relatively ready to hold that a sufficient link exists. Where the court will be least ready to find sufficient evidence is where the wrongdoer has granted an equitable charge for value over the claimed traced asset, which will be subject to the claimant's earlier equitable interest even if the equitable charge had no notice of it – which is very likely to be the case.

The advantage of the evidential approach, as opposed to applying allegedly fixed principles of law as to the "lowest intermediate balance" rule and as to the inadequacy of "backwards tracing", is that it allows a judge the discretionary flexibility needed to respond fairly and justly to particular circumstances.

4. Tracing against Innocent donees

This last point leads to a reconsideration of the orthodox rules as to tracing assets in the hands of *innocent* volunteers where the same rules apparently apply as in the case of a wrongdoing fiduciary, "F", or a "wicked" volunteer, "W", who is aware that he has wrongfully received fiduciary property. Thus, if F sells fiduciary property and uses the proceeds to buy an apartment for himself, the apartment can be traced and recovered. If F then gratuitously transfers the apartment to W it can still be recovered from W, not being a bona fide purchaser of a legal interest for value without notice. If W then sells it and uses the proceeds to buy Whizzo Ltd shares, which double in value, these shares can be recovered.

The orthodox view is that the position is the same if W had been an innocent volunteer, V, on the basis that the claimants have a *continuing* proprietary interest in all traceable substitutions[17]. The problem with this is that a proprietary right must relate to a specific thing and cannot be detached from that thing and re-attached to a different new thing:

[17] *Foskett v McKeown* [2001] 1 AC 102 at 108-109, 127-128

the right to the earlier thing is not the same right as the right to the new thing[18]. Under the doctrine of overreaching, however, there can be an authorised detaching of a right to a specific asset and an attaching the right to its proceeds of sale and then to an asset purchased with the proceeds of sale.

There is thus another view[19] that, while the claim against V is proprietary so far as concerns the apartment that he received from F, once V has sold the apartment believing it and its proceeds of sale to be his, he is entitled to deal with the proceeds and spend or invest them as he sees fit, taking advantage of his own skills and experience. His only obligation upon learning of F's wrongdoing is to pay over the proceeds of sale of the apartment as a liability for unjust enrichment.

V's position is distinguished from the position of F and W. F and W both knew that they were wrongfully dealing with fiduciary property that was not their own. Thus, they were holding it and any substitutes acquired with proceeds of sale for the benefit of the claimants. As fiduciaries owing a duty of loyalty to act in the claimants' best interests, not their own interests, they could not deny that the claimant's interests in the original property had been duly overreached into authorised acquisitions derived from that property. In stark contrast, V never knew he was holding fiduciary property and was fully entitled to believe it was his own to use as he wished. Thus, when he sold it, whatever he bought became fully his own, though from the date he became aware that he had sold property that beneficially belonged to the claimants he becomes personally liable for an amount equivalent to the proceeds of sale to prevent his being unjustly enriched.

5. Constructive trusts of bribes and secret commissions

In *FHR European Ventures LLP v Mankarious and Cedar Capital Partners LLC*[20] the English Court of Appeal had the opportunity to consider the "highly controversial" judgment of Lord Neuberger MR, delivering the English Court of Appeal judgment, in

[18] P Birks, 'Tracing, Property, and Unjust Enrichment', (2002) 54 CLP 231 at 244-245
[19] Underhill & Hayton, *Law of Trusts and Trustees,* 18th ed (2010) 90.06-90.10
[20] [2013] EWCA Civ 17

Sinclair Investments (UK) Ltd v Versailles Trade Finance Ltd[21]. Lord Neuberger was happy to consider himself bound by the Court of Appeal in *Lister v Stubbs*[22] which had held that bribes received by a fiduciary from a third party are not held on a proprietary constructive trust, occasioning merely a personal monetary liability. He did not apply the contrary decision of the Privy Council in *Att-Gen of Hong Kong* v *Reid*[23] which had expressly disapproved *Lister*.

His basis for this [at 88] was that English case law established that “a beneficiary of a fiduciary’s duties cannot claim a proprietary interest, but is entitled to an equitable account, in respect of any money or asset acquired by a fiduciary in breach of his duties to the beneficiary, unless the asset or money is or has been beneficially the property of the beneficiary or the trustee acquired the asset or money by *taking advantage of an opportunity or right which was properly that of the beneficiary*.”

If a bribe is received in England by an English resident exploiting his English fiduciary relationship and proceedings are brought in England, the English courts (other than the Supreme Court) must apply English law[24] and follow *Lister* v *Stubbs* in preference to *Reid.* Offshore jurisdictions having the Privy Council as their final court and dealing with a bribe received by a local resident from exploiting a local fiduciary relationship would need, however, to apply their local law with *Reid* as binding authority unless, perhaps, convinced that its reasoning was wholly unreliable in light of *Sinclair.* This, however, is certainly not the case when one examines the attitude to *Sinclair* of the Court of Appeal in *FHR Ventures.*

Indeed, in a case where it is English law that applies to a resident who received a bribe in England from exploitation of an English fiduciary obligation but who then became resident in an offshore jurisdiction, so that proceedings are taken against him there, it

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[21] [2011] EWCA Civ 347
[22] (1890) 45 Ch D 1
[23] [1994] 1 AC 324
[24] Whether because an English personal obligation arises from English wrongdoing or a trust of English property arises as a response to a breach of the fiduciary ’no profit, no conflict’ obligation. [In the case of an express trust governed by English law, tracing is a crucial step for bringing a substantive action within the law of property, so that the identification process will be governed by English law rather than the lex fori otherwise concerned with evidential matters: Dicey*,* Morris & Collins, *Conflict of Laws* 15th ed (2012) at 7.016]

would seem that in applying English law it is open to the offshore court to be persuaded not to follow *Sinclair* on the basis that it is likely that the Supreme Court would reject *Sinclair* and prefer *Reid*, taking account of the critical views in *FHR Ventures.*

In *FHR Ventures* the Court of Appeal distinguished *Sinclair* in holding that a secret commission was held on a proprietary constructive trust. Etherton C at [102] pointed out that in *Sinclair* the fraudster was the principal shareholder of Co A which had a subsidiary Co B. The fraudster then set up Co X to receive money for investment which was diverted to Co B and enabled Co A shares to appreciate very significantly, so the fraudster sold some of them and used the proceeds to buy a London house for £9million. In respect of this house, Lord Neuberger had rejected the proprietary tracing claim of the assignee of the victims' rights after examining the bribe and secret commission cases. However, the Co A shares had belonged to the fraudster before he perpetrated his fraudulent scheme, so was it not inevitable that he could not be regarded as having received them as a secret commission?

The Court of Appeal thus focused upon Lord Neuberger's phraseology that permitted a proprietary interest to be claimed where a fiduciary took advantage of "an opportunity which was properly that of the beneficiary" or of "opportunities beneficially owned by the claimant". The Court was then able to expand upon this phraseology so as to hold at [59] (Lewison LJ), [74] (Pill LJ) and [111] (Etherton C) that a contractual right to a €10 million secret commission and then the money paid pursuant to that contract was held by the defendants on a proprietary constructive trust for the claimant. The Court made clear that it was time the position was fully reviewed by the Supreme Court since *Sinclair* is out of line with courts in Australia, Canada, Singapore and the USA which have, like the Privy Council, held bribes to be subject to a proprietary constructive trust.

The Court was very critical at [57] per Lewison LJ and at [84] per Etherton C of Lord Neuberger's phrases "an opportunity which was properly that of the beneficiary" at [88] and "opportunities beneficially owned by the claimant" at [89]. The judges pointed out that these dicta had been uttered in ignorance of *Bhullar v Bhullar*[25] in which the Court

[25] [2003] EWCA Civ 424

of Appeal had decisively rejected the notion that it was necessary to identify some form of beneficial ownership of the opportunity itself. As Etherton C stated at [84] "Opportunities are not a species of property capable of being held on trust." Nevertheless, a contract, a species of property, coming into existence as the result of an exploitation of an opportunity in breach of the fundamental fiduciary "no profit, no conflict" rule can be held on trust such that the traceable product of the contract will be held on constructive trust.

Cedar Capital LLC was owned by Mankarious. While Cedar was advising the claimants in relation to the possible purchase by them of the Monte Carlo Grand Hotel, it entered for a limited period into an exclusive brokerage agreement with the hotel owners. Under the agreement Cedar was to receive a €10 million fee from the owners for introducing prospective purchasers who then entered into negotiations with the hotel owners and purchased the hotel. This fee was to be paid within five days of the hotel owners receiving the purchase price. In the agreement Cedar also agreed "it shall disclose its appointment hereunder" to the prospective purchasers.

These prospective purchasers, however, were not made aware of Cedar's commission entitlement when Cedar on their behalf negotiated with the hotel owners to obtain the lowest possible purchase price. Simon J thus held there had been insufficient disclosure for Cedar to succeed in its defence that the claimants had given their fully informed consent to Cedar's contractual right to €10 million after the claimants had bought the hotel for €211.5 million.

Applying *Sinclair,* Simon J held that there was no constructive trust of the €10 million, only a personal liability to account to the claimants for such sum. On appeal, the claimants succeeded in their claim that there was a proprietary constructive trust.

Sir Terence Etherton, the Chancellor of the High Court, pointed out that the effect of *Sinclair* is that there are three categories of benefits received by a fiduciary in breach of the fiduciary 'no profit, no conflict' duty, only the first two giving rise to a constructive trust:

(1) where the benefit is or was an asset belonging beneficially to the principal e.g. any benefit obtained by misappropriating or misapplying the principal’s property;

(2) where the benefit was obtained by the fiduciary taking advantage of an opportunity which was properly that of the principal;

(3) all other cases where a benefit was obtained, covering situations like those in *Sinclair* and also in *Att-Gen of Hong Kong v Reid* if the facts had occurred in England.

The Court of Appeal held that Cedar’s contractual right to receive the secret commission (and thus the actual receipt thereof) was not a category 1 benefit, even though the fact that, under the agreement, the commission was to be paid by the hotel owners to Cedar within five working days of the receipt of the purchase price from the purchasers raised a strong inference that Cedar’s commission was in a practical sense paid out of moneys received from the purchasers. Nevertheless, on payment of the purchase price to the hotel owners in return for the hotel, the full legal beneficial title to the money passed to the owners and the purchasers were divested of all interest in the money paid over. Thus, it could only be the hotel owners’ moneys, not the purchasers’ that had passed to Cedar by way of the €10 million commission payment: see [30] and [33] (and [67] and [105]).

The Court, however, found that Cedar held the benefit of the commission contract on a constructive trust for the claimants as a category 2 benefit as refined, the benefit having been obtained by the fiduciary, in breach of the ‘no profit, no conflict’ rule, taking advantage of an opportunity in which his principal was interested. Thus it could be traced into the €10 million receipt. This was the result of examining three classes of cases where a benefit, wrongly obtained by a fiduciary by misusing the opportunity presented by his relationship with his principal, had been found to be held on constructive trust, even though the benefit had been acquired by the fiduciary’s own assets or efforts and had come from a third party – and whether or not, if there had been no breach of fiduciary duty, the benefit could have or would have been obtained by the principal.

The three classes of cases giving rise to a category 2 proprietary constructive trust are as follows, the Court of Appeal relying in particular on the third class.

(1) Cases where the principal had actually instructed the agent to acquire or to negotiate the acquisition of property for him, but the agent purported to acquire the targeted property on his own behalf – or joint venture cases where one stole a march on the other by acquiring property exclusively for himself.

(2) Cases where the fiduciary was not specifically charged with acquiring particular property for his principal, but the fiduciary acquired property which would have been of interest to the principal if the fiduciary had disclosed, as he ought, the possibility to his principal. *Bhullar* was this type of case, where two directors discovered that property adjoining their company's property was available to be purchased by them in a company that they incorporated for this purpose. Jonathan Parker LJ stated, "Where a fiduciary has exploited a commercial opportunity for his own benefit, the relevant question is not whether the party to whom the duty is owed had some kind of beneficial interest in the opportunity; in my judgment that would be too formalistic and restrictive in approach. Rather the question is simply whether the fiduciary's exploitation of the opportunity is such as to attract the application of the rule." The rule is that "no fiduciary shall be allowed to enter into any engagements in which he has, or can have, a personal interest conflicting, or which may possibly conflict, with the interests of those whom he is bound to protect." The Court of Appeal endorsed asking the question whether the fiduciary's exploitation of the opportunity was such as to attract the rule and answered it in the affirmative in the circumstances before it.

Phipps v Boardman[26] was a similar type of case where the trust fund comprised a minority shareholding in a private company. No more shares could be acquired unless, upon application under s 57 of the Trustee Act 1925, the court authorised this. The solicitor to the trust, with the help of a beneficiary who attended company meetings with him, thought that a majority holding should be acquired

[26] [1967] 2 AC 46

and the company business reorganised. With what they thought was informed consent from trustees, who did not want to be involved in any such business dealings, they proceeded to acquire the remaining shares and reorganise the company's business to the advantage of the trust fund and of themselves by increasing the value of the shares in the company.

A beneficiary with a five eighteenths interest in the trust's minority shareholding claimed a declaration that he was entitled to five eighteenths of the shares acquired by the defendants. As the Chancellor stated at [91], Wilberforce J made the claimed declaration that five eighteenths of the shares owned by the defendants were held on constructive trust for the claimant beneficiary and ordered an account of the profits made by the defendants so that the defendants, as desired by the claimant, could simply account to the claimant for such profits rather than convey the shares to the claimant in return for being reimbursed the cost of the shares. The House of Lords upheld the orders of Wilberforce J making plain that there had been a proprietary constructive trust, though Lord Neuberger without the benefit of a detailed examination had considered that the question of a proprietary constructive trust had not arisen.

(3) Cases where the fiduciary was held to be a trustee of a profit made in breach of fiduciary duty, even though the principal did, in fact, obtain the target property. In *Tyrell v Bank of London*[27] Tyrell was the Bank's solicitor and secretary. The Bank was offered the opportunity to buy certain property on part of which stood the Hall of Commerce, in which it was interested, though it was not then in a position to buy it. Tyrell subsequently entered into a contractual arrangement with Read who had a contract to buy the property from the mortgagee. The arrangement was for Tyrell and Read to be jointly interested in Read's contract. The Bank then agreed with Read to buy the Hall of Commerce part from him and paid him the purchase money. The House of Lords held that Tyrell held the benefit of his contract with Read on trust for the Bank so far as concerned the Hall of Commerce part of the land, so that Tyrell held the traceable profit on trust

[27] (1862) 10 HLC 26

for the Bank. Similarly, see *Fawcett v Whitehouse*[28] where Fawcett, on behalf of himself and two partners, acquired an underlease of ironworks from a lessee who was finding it an unprofitable business and so paid Fawcett £12,000 to clinch the deal: Lord Lyndhurst LC held that Fawcett held two thirds of the £12,000 on trust for his two partners.

Thus Cedar's exploitation of the opportunity to make a large commission for itself in breach of the "no profit, no conflict" rule in helping the claimants acquire the Grand Hotel was such as to require it to hold the benefit of its commission contract and then the commission itself on constructive trust for the claimants.

6. Powers of revocation and personal powers to appoint to self

Although a power to make oneself owner of property does not make one owner of the property until the power is exercised, such a power is tantamount to ownership according to the Privy Council in *FONU v Merrill Lynch Bank and Trust Company (Cayman) Ltd* [2011] UKPC 17. Thus, to assist a judgment creditor satisfy its judgment, a court by way of equitable execution can appoint a receiver in respect not just of the judgment debtor's property but also of his power of revocation.

In this case the settlor had reserved to himself a power of revocation and a judgment creditor wanted to satisfy the settlor's debt out of the settled property, which would be available to satisfy debts as the settlor's own beneficial property if the power were exercised. Could the court order the settlor to execute an instrument that would directly revoke his trust (with a court official being authorised to execute on his behalf if he refused). If not, could the revocation be obtained indirectly by the court by way of equitable execution ordering the settlor to execute an instrument to delegate his power of revocation to a receiver for the creditor who would then revoke the settlement (with a court official or the receiver being authorised to execute the delegation instrument if the settlor refused)?

[28] (1829) 1 Russ & M 132

An English High Court Family Division case, *Field v Field* [2003] 1 FLR 376 precluded the direct approach, so although the Privy Council doubted the correctness of *Field,* it chose to take the indirect approach to achieve the same result.

Note that the reasoning of the Privy Council will extend beyond a settlor's power of revocation to a settlor's power to appoint to himself and others and to any debtor having a personal power of appointment exercisable in his own favour (including a power to add himself to a class of objects of a personal power of appointment held by him). Any consent, however, required to the exercise of a power of revocation or of appointment to oneself will prevent the position of the donee of the power being tantamount to ownership unless and until the consent has been given, as Upjohn J accepted in *Re Triffitt's Settlement* [1958] Ch 852.

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