EQUITABLE COMPENSATION FOR BREACH OF TRUST: OFF *TARGET*

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This article concerns the principles by which courts determine the quantum of equitable compensation that a trustee must pay following a breach of trust. Traditional equitable principles focused on the trustee's obligation to account for his or her stewardship of the trust property, and to restore the assets of which he or she deprived it. The Supreme Court of the United Kingdom has recently confirmed that the earlier decision in Target Holdings Ltd v Redferns *marked a shift in thinking about monetary remedies for breach of trust in England. This article addresses the question to what degree that shift towards a causal analysis represents the law in Australia, and to what degree it should do so. The argument advanced in this paper is that the underlying rationale of equity's traditional principles continues to hold good, and that the traditional principles represent the law in Australia and should continue to do so for the future.*

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I Introduction

This article concerns the principles by which courts determine the quantum of equitable compensation that a trustee must pay following a breach of trust. There is longstanding authority on this topic, although some aspects of it have been obscured to the modern eye due to inattention over many years. Those traditional principles focused on the trustee's obligation to account for his or her stewardship of the trust property, and '[t]he form of relief [was] couched in terms appropriate to require the defaulting trustee to restore to the estate the assets of which he deprived it.'[1] This accounting was 'of a more absolute nature than the common law obligation to pay damages for tort or breach of contract'[2] as it was not concerned with whether the loss was caused by or flowed from the breach.[3] These traditional principles apply to other fiduciary relationships involving the custody or control of property, beyond trusts,[4] but not necessarily to all fiduciary relationships.[5] The focus of this article is solely on custodial relationships, with a particular emphasis on trusts.

The House of Lords' decision in *Target Holdings Ltd v Redferns* ('*Target Holdings*'),[6] delivered a little over 20 years ago, appeared to mark a shift in thinking about monetary remedies for breach of trust. Lord Browne-Wilkinson suggested that the traditional principles should not be applied to commercial trusts,[7] where an award of equitable compensation is designed '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

[1] *Re Dawson; Union Fidelity Trustee Co Ltd v Perpetual Trustee Co Ltd* [1966] 2 NSWR 211, 216 (Street J).

[2] Ibid.

[3] Ibid 215. See also Justice Gummow, 'Compensation for Breach of Fiduciary Duty' in T G Youdan (ed), *Equity, Fiduciaries and Trusts* (Carswell, 1989) 57, 89.

[4] See *Bairstow v Queens Moat Houses plc* [2001] 2 BCLC 531, 548 [53] (Walker LJ); *Waxman v Waxman* (2004) 7 ITELR 162 [657]; *O'Halloran v R T Thomas & Family Pty Ltd* (1998) 45 NSWLR 262, 277 (Spigelman CJ); *Maguire v Makaronis* (1997) 188 CLR 449, 473; Charles E F Rickett, 'Equitable Compensation: Towards a Blueprint?' (2003) 25 *Sydney Law Review* 31, 32–3.

[5] See *Bairstow v Queens Moat Houses plc* [2002] BCC 91, 105 [53] (Walker LJ); *Youyang Pty Ltd v Minter Ellison Morris Fletcher* (2003) 212 CLR 484, 501 [41]–[42]; *Waxman v Waxman* [2004] 186 OAC 201 [657].

[6] [1996] AC 421.

[7] Ibid 435.

breach.'[8] The Supreme Court of the United Kingdom has now confirmed this shift in thinking in English law, in its recent judgment in *AIB Group (UK) plc v Mark Redler & Co Solicitors* ('*AIB*'),[9] declaring that 'it would be a backward step for this court to depart from Lord Browne-Wilkinson's fundamental analysis in *Target Holdings*'.[10]

The question addressed in this article is to what degree that shift towards a causal analysis represents the law in Australia, and to what degree it should do so. Heydon, Leeming and Turner have argued that 'the innovation in the *Target* decision has quite some attraction',[11] and also that it represents the law in Australia,[12] as a result of the High Court of Australia's decision in *Youyang Pty Ltd v Minter Ellison Morris Fletcher* ('*Youyang*').[13] The argument advanced in this paper is that the underlying rationale of equity's traditional principles continues to hold good, and that the law in Australia has not changed as a result of *Youyang*, so the traditional principles continue to represent the law in Australia and should continue to do so for the future.

In order to make these points, the discussion which follows provides an outline of the traditional principles applied to trustees, followed by a discussion of the extent to which *Target Holdings*, *AIB* and *Youyang* have, or have not, altered those principles. It will then be possible to address the extent to which the traditional principles continue to offer a sensible resolution to such matters.

II Traditional Equitable Principles

Equity traditionally approached a trustee's liability for a breach of trust through the mechanism of taking an account of the trust: '[t]he taking of an account is the means by which a beneficiary requires a trustee to justify his stewardship of trust property. The trustee must show what he has done with that property.'[14]

8 Ibid 439.

9 [2015] AC 1503.

10 Ibid 1527 [63] (Lord Toulson JSC).

11 J D Heydon, M J Leeming and P G Turner, *Meagher, Gummow and Lehane's Equity: Doctrines and Remedies* (LexisNexis, 5th ed, 2015) 822 [23-210].

12 Ibid 823–4 [23-215].

13 (2003) 212 CLR 484.

14 *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch) (27 July 2005) [1513] (Lewison J).

A *Accounts of Administration*

The processes by which accounts were taken can be divided into two kinds:

> One kind (… an order for an account of administration) is made where the overall administration of a business enterprise or fund or other property is to be established or accounted for. Another kind (… an order for an account of profits) is made to provide a remedy for specific equitable wrongdoing.[15]

Accounts of profits were not at issue in any of the cases under discussion here, as that form of 'accounting relates to specified gains rather than the general administration of a fund.'[16] The account of administration is the relevant form of account for the purposes of the present discussion.

Accounts of administration were further sub-divided between accounts ordered to be taken in common form and those ordered to be taken on the basis of wilful default.[17]

1 *Accounts in Common Form*

A beneficiary was entitled 'as of right' to be given an account in common form of the trustee's stewardship of the trust assets, without the beneficiary needing to prove that the trustee had committed any breach of trust.[18] The beneficiary could then object to any entry in the account which he or she considered out of place, and put the trustee to proof that the entry was justified. So, for example, in *Re Fish; Bennett v Bennett* ('*Re Fish*'),[19] the beneficiaries were unsuccessful in their argument that their trustee had acted in breach of trust continuing to operate a business, but were nonetheless 'absolutely entitled' to see the trustee's statement of account and to object to any items in those accounts which they considered out of place.[20]

The mechanisms involved in taking accounts can be traced back centuries. As Lord Hardwicke LC said:

15 *Glazier Holdings Pty Ltd v Australian Men's Health Pty Ltd [No 2]* [2001] NSWSC 6 (22 January 2001) [36] (Austin J). See also H G Hanbury, 'Forms of Account against Executors and Trustees' (1936) 52 *Law Quarterly Review* 365, 365.

16 *Glazier Holdings Pty Ltd v Australian Men's Health Pty Ltd [No 2]* [2001] NSWSC 6 (22 January 2001) [43] (Austin J).

17 See generally Heydon, Leeming and Turner, above n 11, 802 [23-030].

18 See *Libertarian Investments Ltd v Hall* (2013) 16 HKCFAR 681, 732 [167] (Lord Millett NPJ).

19 [1893] 2 Ch 413.

20 Ibid 427 (Kay LJ).

> if any of the parties can shew an omission, for which credit ought to be, that is a surcharge: or if any thing is inserted, that is a wrong charge, he is at liberty to shew it, and that is falsification …[21]

The terminology of falsification and surcharging has been described as 'arcane',[22] but the concepts remain relevant today as the mechanisms by which an account can be challenged,[23] and the traditional terminology continues to provide useful labels for the processes involved in taking accounts.[24] Where a beneficiary seeks to surcharge the common account, the beneficiary must establish that the trustee received more than the account records. If, for example, the beneficiary can show that the trustee received income from a property held in trust (such as rent on a trust property or dividends on shares held in trust) and that income was not recorded in the trust accounts, the accounts are surcharged to include that income on the debit side of the account.[25] The accounts are amended to reflect that income and the trustee is then required to hold that property on trust so that the trust fund actually contains the property which the amended accounts indicate ought to be present (or to pay equitable compensation in such amount as would enable the property to be acquired if it is no longer held). Where the beneficiary falsifies an entry contained in the accounts, he or she asserts that an entry on the credit side of the account should be struck out of the accounts as it is improper for the trustee to take credit for that entry.[26] The beneficiary need only challenge the entry and it then falls to the trustee to seek to establish that

[21] *Pit v Cholmondeley* (1754) 2 Ves Sen 565, 566; 28 ER 360, 360.

[22] *Glazier Holdings Pty Ltd v Australian Men's Health Pty Ltd [No 2]* [2001] NSWSC 6 (22 January 2001) [38] (Austin J).

[23] See, eg, *Uniform Civil Procedure Rules 2005* (NSW) r 46.7(1) concerning the need to give notice of an attempt to surcharge an account, and r 46.7(2) which concerns falsification of an account.

[24] See *Glazier Holdings Pty Ltd v Australian Men's Health Pty Ltd [No 2]* [2001] NSWSC 6 (22 January 2001) [38] (Austin J); *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch) (27 July 2005) [1513] (Lewison J).

[25] See generally Isaac Preston Cory, *A Practical Treatise on Accounts* (William Pickering, 2nd ed, 1839) 265–6. See, eg, *Wentworth v Tompson* (1859) 2 Legge 1238.

[26] Beneficiaries are not *obliged* to falsify an unauthorised disbursement, particularly if it has proven to be a beneficial investment: see *Pocock v Reddington* (1801) 5 Ves 794, 800; 31 ER 862, 865 (Sir R P Arden MR); *Libertarian Investments Ltd v Hall* (2013) 16 HKCFAR 681, 732–3 [169] (Lord Millett NPJ); *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch) (27 July 2005) [1513] (Lewison J).

the entry is correct,[27] or that the erroneous transaction has already been corrected.[28]

The precise remedy awarded following the taking of a common account depends upon what the account process throws up. As Lord Millett NPJ has said:

> an order for an account does not in itself provide the plaintiff with a remedy; it is merely the first step in a process which enables him to identify and quantify any deficit in the trust fund and seek the appropriate means by which it may be made good.[29]

Where, for example, the trustee has used trust funds to make an unauthorised investment, the disbursement can be falsified and the trustee must restore to the trust fund the sum that was wrongfully disbursed: '[t]he case must either be treated as if these investments had not been made, or had been made for [the trustee's] own benefit out of his own monies, and that he had at the same time retained monies of the testator in his hands.'[30] In contrast, where the trustee makes an unauthorised sale of trust property, the beneficiaries can falsify the disposal of that asset, and the trust accounts will then indicate that the trust fund should contain the asset. In other words, the trust accounts will then disclose 'a deficit which the defendant must make good, either in specie or in money.'[31] For example, in *Phillipson v Gatty*,[32] the trustees sold £2347, 10s 2d worth of consols for £2183, 3s 8d, and invested the proceeds in a way which was found to be in breach of trust. Rejecting an argument that the trustees only had to replace the proceeds of sale which had then been

[27] See *Bin Hadjee Mohamed Salleh Angullia v Estate and Trust Agencies (1927) Ltd* [1938] AC 624, 637; *Re Stevens; Cooke v Stevens* [1898] 1 Ch 162, 172 (Chitty LJ). Where the account is settled, as opposed to open, the onus lies on the party attacking the account to prove an error in the account: *Pit v Cholmondeley* (1754) 2 Ves Sen 565, 565–6; 28 ER 360, 360–1 (Lord Hardwicke LC); *Gething v Keighley* (1878) 9 Ch D 547, 552 (Jessel MR); Cory, above n 25, 260–1; Walter Strachan, *The Law of Trust Accounts* (Effingham Wilson, 1911) 177.

[28] See, eg, *Re Anglo-French Co-Operative Society; Ex parte Pelly* (1882) 21 ChD 492, 501 (Jessel MR), 506 (Brett LJ), 509 (Cotton LJ); *Re Brogden; Billing v Brogden* (1888) 38 Ch D 546, 557 (North J); *Re Massingberd's Settlement; Clark v Trelawney* (1890) 63 LT 296, 298 (Cotton LJ); *Re Jenkins and H E Randall & Co's Contract* [1903] 2 Ch 362, 366 (Swinfen Eady J).

[29] *Libertarian Investments Ltd v Hall* (2013) 16 HKCFAR 681, 732 [168].

[30] *Knott v Cottee* (1852) 16 Beav 77, 79–80; 51 ER 705, 706 (Romilly MR).

[31] *Libertarian Investments Ltd v Hall* (2013) 16 HKCFAR 681, 732 [168] (Lord Millett NPJ).

[32] (1848) 7 Hare 516; 68 ER 213.

wrongfully invested, Wigram V-C held that they 'must replace the stock' as the sale itself was unauthorised if made for the purpose of making the subsequent investment.[33] In most cases, the breach will be remedied by the trustee paying a sum sufficient to purchase the relevant asset back for the trust, rather than requiring the trustee to purchase the asset and return that to the trust.[34] It has, therefore, been said that a court's order that an account be taken 'proceeds, and must always proceed, upon the assumption that the party calling for it is entitled to the sum found due',[35] but this does not preclude an in specie remedy where appropriate.

2 *Accounts Founded on Wilful Default*

Where an account is taken in common form, 'the accounting party accounts only for what has actually been received and disposed of.'[36] As Sir Richard Kindersley V-C said 'the [p]laintiff … cannot charge the [d]efendant with a single farthing beyond his actual receipts'.[37] The trustee's potential liability to pay compensation is thus bounded by what has actually been received and paid out. Within that constraint, however, the beneficiaries 'can challenge the accounting party's account by asserting that more was received (in the old terminology, surcharging) or by asserting that less was disposed of (in the old terminology, falsifying).'[38]

The common account thus does not allow beneficiaries to argue that the trustee ought to have received more than he or she did receive, as that

[33] *Phillipson v Gatty* (1848) 7 Hare 516, 528; 68 ER 213, 219. See also *Earl Powlet v Herbert* (1791) 1 Ves Jun 297, 297; 30 ER 352, 352 (Lord Thurlow LC); *Kellaway v Johnson* (1842) 5 Beav 319, 324; 49 ER 601, 603 (Lord Langdale MR); *Re Massingberd's Settlement; Clark v Trelawney* (1890) 63 LT 296, 298 (Cotton LJ); *Re Dawson; Union Fidelity Trustee Co Ltd v Perpetual Trustee Co Ltd* [1966] 2 NSWR 211, 220 (Street J).

[34] See, eg, *Libertarian Investments Ltd v Hall* (2013) 16 HKCFAR 681, 732 [168] (Lord Millett NPJ).

[35] *Doss v Doss* (1846) 3 Moo Ind App 175, 197; 18 ER 464, 472 (Dr Lushington for Dr Lushington, Parke B and Lord Brougham).

[36] *Meehan v Glazier Holdings Pty Ltd* (2002) 54 NSWLR 146, 149 [13] (Giles JA).

[37] *Partington v Reynolds* (1858) 4 Drew 253, 257; 62 ER 98, 99. See also *Re Fryer; Martindale v Picquot* (1857) 3 K & J 317, 318; 69 ER 1129, 1130 (Wood V-C).

[38] *Meehan v Glazier Holdings Pty Ltd* (2002) 54 NSWLR 146, 149 [13] (Giles JA). See also *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch) (27 July 2005) [1513] (Lewison J).

argument concerns sums beyond those which the trustee actually received. In order to deal with such cases:

> There is an alternative basis for taking accounts. An order may be made for taking accounts on the basis of wilful default (sometimes the words are wilful neglect and default). Under such an order the accounting party must account not only for what has actually been received, but also for what should have been received: that is, for what would have been received if the relevant duties of the accounting party had been properly discharged. Thus in *Partington v Reynolds* … it was said that on this basis an executor or administrator must account 'not only for what he has received, but also for what he might, without his wilful neglect or default have received, although he has not received it'.[39]

An account which is conducted on the basis of wilful default thus exposes the trustee to a potentially far greater liability than a common accounting.[40] Furthermore, when accounts are taken on this basis, the trustee is subjected to a 'roving commission',[41] under which the judge (or master) can look into all aspects of the trustee's management of the trust fund and force the trustee to explain any entry, even where the beneficiaries have not pleaded anything regarding the entry.[42] In order to control this, the courts would only order an

[39] *Meehan v Glazier Holdings Pty Ltd* (2002) 54 NSWLR 146, 149–50 [14] (Giles JA). See also *Re Stevens; Cooke v Stevens* [1898] 1 Ch 162, 172 (Chitty LJ); *Armitage v Nurse* [1998] Ch 241, 252 (Millett LJ); Cory, above n 25, 260.

[40] *Meehan v Glazier Holdings Pty Ltd* (2002) 54 NSWLR 146, 150 [15] (Giles JA).

[41] *Bartlett v Barclays Bank Trust Co Ltd [No 2]* [1980] 1 Ch 539, 546 (Brightman LJ). See also *Coulthard v Disco Mix Club Ltd* [2000] 1 WLR 707, 734 (Sher QC).

[42] See *Re Stevens; Cooke v Stevens* [1897] 1 Ch 422, 432–3 (North J). Procedural rules, such as *Uniform Civil Procedure Rules 2005* (NSW) r 46.7(1), require that a beneficiary seeking to surcharge an account give 'notice of the charge, stating, so far as he or she is able, the amount that he or she seeks to charge, with brief particulars.' However, such rules as to notice and particulars are not new: see, eg, Augustine Birrell, *The Duties and Liabilities of Trustees* (Macmillan and Co, 1897) 152; Sydney Edward Williams and Frank Guthrie-Smith, *Daniell's Chancery Practice* (Stevens and Sons, 8th ed, 1914) vol 1, 919; Walter Strachan, *The Law of Trust Accounts* (Sweet and Maxwell, 2nd ed, 1937) 195; *Re Wrightson* [1908] 1 Ch 789, 799). The purpose of an accounting on the basis of wilful default 'is to discover concealed misconduct and to sort out thoroughly mismanaged estates': John McGhee (ed), *Snell's Equity* (Sweet and Maxwell, 33rd ed, 2015) 549 [20-025]. Bearing in mind the obligation to give notice and particulars only applies insofar as the plaintiff is able to do so, the roving inquiry is still possible, provided the pleadings include notice of the matters of which the plaintiff is already aware and on which he or she relies to justify the order that accounts be taken on a wilful default footing. See also *Re Stevens; Cooke v Stevens* [1897] 1 Ch 422, 432 (North J); *Mayer v Murray* (1878) 8 Ch D 424, 426–7 (Jessel MR); *Juul v Northey* [2010] NSWCA 211 (26 Au-

account to be taken in this way where the beneficiaries have proven at least one instance of the trustee having committed a breach of trust.[43] In other words, the two forms of account proceed on entirely distinct grounds. Common accounting supposes no misconduct; wilful deceit is 'entirely grounded' on misconduct.[44] The order for a common accounting was frequently referred to as 'the usual order' in order to distinguish it from 'an order founded on breach of trust'.[45] As Haddan observed:

> the general rule is, that the executor or administrator is liable for everything he has received, and no more; the assumption being, until the contrary is shown, that he has acted bona fide and to the best of his power in getting in the estate.[46]

Notwithstanding its name, an accounting on the footing of wilful default does not require conscious misconduct: '[i]t is sufficient that the trustee has been guilty of a want of ordinary prudence.'[47] But not every breach of trust constitutes wilful default.[48] Consistently with the purpose of a wilful default accounting, it must be shown 'that through breach of trust the trustee has *failed to obtain* for the trust that which would have been obtained if the trustee's duties had been discharged.'[49] Thus, for example, in *Meehan v Glazier Holdings Pty Ltd*,[50] the trustees were found to have failed, in breach of trust, to

gust 2010) [203] (McColl JA); *Grace v Grace* [2012] NSWSC 976 (23 August 2012) [217] (Brereton J).

43 See *Re Stevens; Cooke v Stevens* [1897] 1 Ch 422, 432 (North J).

44 *Partington v Reynolds* (1858) 4 Drew 253, 256; 62 ER 98, 99 (Sir Richard Kindersley V-C).

45 *Dowse v Gorton* [1891] AC 190, 202 (Lord Macnaghten).

46 Thomas Henry Haddan, *Outlines of the Administrative Jurisdiction of the Court of Chancery* (William Maxwell, 1862) 80.

47 *Armitage v Nurse* [1998] Ch 241, 252 (Millett LJ). See also *Re Chapman; Cocks v Chapman* [1896] 2 Ch 763, 776 (Lindley LJ); *Bartlett v Barclays Bank Trust Co Ltd [No 2]* [1980] 1 Ch 539, 546 (Brightman LJ); *Meehan v Glazier Holdings Pty Ltd* (2002) 54 NSWLR 146, 163 [65] (Giles JA).

48 See *Russell v Russell* (1891) 17 VLR 729, 732 (Webb J); *Re Wood; Ebert v Union Trustee Co of Australia Ltd* [1961] Qd R 375, 378 (Mansfield CJ).

49 *Meehan v Glazier Holdings Pty Ltd* (2002) 54 NSWLR 146, 163 [65] (Giles JA) (emphasis added). See also *Sleight v Lawson* (1857) 3 K & J 292, 298; 69 ER 1119, 1121–2 (Wood V-C); *Bartlett v Barclays Bank Trust Co Ltd [No 2]* [1980] 1 Ch 539, 546 (Brightman LJ); *Juul v Northey* [2010] NSWCA 211 (26 August 2010) [189] (McColl JA).

50 (2002) 54 NSWLR 146.

maintain adequate records regarding the trust.[51] However, the Court considered that this was insufficient to order that accounts be taken on a wilful default footing as there was nothing to suggest 'that something was not received by the [t]rust or otherwise lost to it' as a result of those breaches.[52] Similarly, in *Massey v Massey*,[53] where debts were admitted to exist and had not been collected, Page Wood V-C nonetheless refused to order an accounting on the basis of wilful default because the trustees indicated that the testator's widow had already collected some debts and that the others were bad and could not be recovered.[54] Without something to establish that any particular debt had not been collected which ought to have been, a wilful default accounting was inappropriate.

The distinction between common and wilful default accounts was so sharply drawn prior to the *Judicature Acts*[55] that where an account was ordered in common form, even if the accounting established that instances of wilful default had occurred, the trustees could not be charged with wilful default without a separate suit being instituted, which required the leave of the court, unless the court's original order had reserved the power to make further directions for the accounting to take place on a wilful default footing.[56] Following the *Judicature Act* reforms, however, 'the stringency of the rule has been somewhat relaxed',[57] to the point where 'under the new practice an order charging [the trustee] with wilful default may be made at any time on a proper case being made',[58] although an adequate pleading of wilful default is still necessary.[59]

[51] Ibid 163 [66] (Giles JA).

[52] Ibid.

[53] (1862) 2 J & H 728; 70 ER 1252.

[54] Ibid 735–6; 1255–6.

[55] See especially *Supreme Court of Judicature Act 1873* (Imp) 36 & 37 Vict, c 66; *Supreme Court of Judicature Act 1875* (Imp) 38 & 39 Vict, c 77.

[56] *Jones v Morrall* (1852) 2 Sim (NS) 241, 249–50; 61 ER 333, 336 (Sir Richard Kindersley V-C); *Partington v Reynolds* (1858) 4 Drew 253, 258–9; 62 ER 98, 100 (Sir Richard Kindersley V-C). See also *Robinson v Robinson* (1851) 1 De G M & G 247, 257–8; 42 ER 547, 551.

[57] Hanbury, above n 15, 366.

[58] *Job v Job* (1877) 6 Ch D 562, 564 (Jessel MR). If a wilful default accounting was sought after the judgment, the court's leave was still needed: *Laming v Gee* (1878) 10 Ch D 715, 718 (Hall V-C). See also *Re Symons; Luke v Tonkin* (1882) 21 Ch D 757, 761 (Fry J); *Smith v Armitage* (1883) 24 Ch D 727, 728–9 (Denman J); *Re Youngs; Vollum v Revett* (1885) 30 Ch D 421,

B *Relevance (and Irrelevance) of Causation*

It is now possible to address the extent to which concepts of causation do, or do not, play a role in each of these types of accounting.

Dealing first with common accounts, it is clear that causal questions do not affect the analysis of the trustee's liability to pay equitable compensation. Where the beneficiary falsifies an entry in the trustee's account, and the trustee is unable to provide the evidence necessary to justify the entry, the entry is disallowed and the disbursement is treated as if it had not happened.[60] There is no need to conduct a causal analysis as to whether the assets which were in fact disbursed would have been lost to the trust fund in some other way, as they ought still to be in the trust fund. Thus, for example, in *Magnus v Queensland National Bank* ('*Magnus*'),[61] a bank held trust property, knowing it to be such, as security for a loan. When the debt was repaid, the bank released the property on the instructions of one of the three trustees alone, Goldsmid, who later absconded with the proceeds of sale of the property and was adjudicated bankrupt.[62] The bank, when held to account, attempted to argue that it was not liable to account for the property because Goldsmid had such control over the other trustees that he would have defrauded the trust of its property in some other way, even if the bank had acted properly.[63] In other words, the argument was that the bank's breach did not cause the loss. That argument was rejected by all three judges. Lord Halsbury LC accepted the premise that Goldsmid would probably have defrauded the other trustees, but considered this irrelevant:

> once the fact is established that money belonging to this trust has got into the hands of one of the three trustees without the consent of the others, and that by the default of the bank, we are not at liberty to speculate whether the same result might not have followed whether the bank had been guilty of that default

431–2 (Cotton LJ); Sir H W Seton et al, *Forms of Judgments and Orders* (Stevens and Sons, 7th ed, 1912) vol 2, 1121.

59 See *Mayer v Murray* (1878) 8 Ch D 424, 426–7 (Jessel MR); *Juul v Northey* [2010] NSWCA 211 (26 August 2010) [203] (McColl JA); *Grace v Grace* [2012] NSWSC 976 (23 August 2012) [217] (Brereton J).

60 *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch) (27 July 2005) [1513] (Lewison J).

61 (1888) 37 Ch D 466.

62 *Ex parte Taylor; Re Goldsmid* (1886) 18 QBD 295, 297. See also *Magnus* (1887) 36 Ch D 466, 467 (Lord Halsbury LC).

63 *Magnus* (1887) 36 Ch D 466, 469–70.

> or not. … I think that the loss to the trust happened when, instead of being re-invested in the names of the three trustees, it was placed in the hands of Goldsmid alone.[64]

Cotton LJ said:

> It was urged very strongly that the negligence of the trustees was the real cause of the loss to the trust; and I agree that they were negligent. They ought to have seen that the North-Eastern stock had been put into their names. It never was. But in the view which I take of the case it is not necessary to consider that point; because, if the bank having this stock, in respect of which, the loan having been paid off, they were accountable to the trustees, paid the money arising from that property, not to the trustees, nor to any person authorized by the trustees to give a good receipt for it, they, in my opinion, must be held answerable to the trustees just as if the money was still in their hands.[65]

And Bowen LJ said:

> It will be found, I think, upon reflection, that the strength of the argument on behalf of the [a]ppellants rests upon a fallacious and misleading use of the expression, 'loss caused by the conduct of the bank'; and that the learned counsel for the [a]ppellants, in pressing home the argument that whatever the conduct of the bank may have been it did not cause the loss to the estate, was using the term in a popular and non-legal sense, and one which is not sufficient to support his proposition. When was the property of the trust lost? At the time when it first passed into unauthorized hands. … We were asked, indeed, to believe that whatever the breach of duty on the part of the bank was, it did not ultimately lead to the loss to the fund which has been sustained. That really is an illusion; it is an ocular illusion to present the case in that way. The loss occurred as soon as the money which belonged to the trust was diverted into the hands of a person who had no right to represent the trust. The proposition presented to us by the [a]ppellants, if divested of its popular and specious look, is this, that we ought not to visit those who lose trust property with the consequence of having to make it good, provided it can be shewn or surmised that, if they had made it good, somebody else would have lost it over again. Is that a tenable proposition? A man knocks me down in Pall Mall, and when I

[64] Ibid 472–3.
[65] Ibid 477.

> complain that my purse has been taken, the man says, 'Oh, but if I had handed it back again, you would have been robbed over again by somebody else in the adjoining street.' That is the argument of the learned counsel for the [a]ppellants, as soon as the proposition for which they have contended is reduced to its bare bones.[66]

These extracts are lengthy but they are important because they emphasise that, where an entry in an account is falsified on the basis that it was unauthorised, the accounting party cannot seek to argue that the loss would have been caused in a different way, even if the breach had not occurred.[67] It is suggested that the rationale underpinning this approach stems directly from the trustee's fundamental obligation to hold on to the trust property,[68] and to be able to justify what has been done with that property.[69] The trustee's underlying duty 'is properly to preserve the trust fund, to pay the income and the corpus to those who are entitled to them respectively'.[70] The basic position is, thus, that the trustee is not permitted to part with the trust property: 'the trustee cannot change the nature of the estate; as by converting money into land, or land into money, at least so as to bind and exclude the cestui que trust from remedy against the trustee personally.'[71] Trustees do, of course, frequently part with the trust property, but that is because such conduct has been authorised. As Justice Story put it, 'the trustee has no right (*unless express power is given*) to change the nature of the estate'.[72] In other words, the trustee must be able to point to a relevant power, or other justification,[73] if he

66 Ibid 477, 479–80.

67 See also *Cocker v Quayle* (1830) 1 Russ & M 535, 538; 39 ER 206, 207 (Sir John Leach MR).

68 See *A-G (UK) v Alford* (1855) 4 De G M & G 843, 851; 43 ER 373, 341 (Lord Cranworth LC).

69 *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch) (27 July 2005) [1513] (Lewison J).

70 *Low v Bouverie* [1891] 3 Ch 82, 99 (Lindley LJ).

71 Henry Ballow, *A Treatise of Equity* (John Fonblanque (ed), Small, 2nd revised ed, 1820) vol 2, 168. This proposition was stated to apply where the beneficiary is sui juris. Where that was not the case, implied powers to change the trust property might exist.

72 Justice Story, *Commentaries on Equity Jurisprudence: Third English Edition* (A E Randall (ed), Sweet and Maxwell, 3rd ed, 1920) 400 (emphasis added).

73 For example, a trustee can justify the loss of the trust property if he or she proves it was stolen without fault on the part of the trustee: *Morley v Morley* (1678) 2 Chan Cas 2; 22 ER 817; *Jones v Lewis* (1751) 2 Ves Sen 240, 241; 28 ER 155, 155; Cory, above n 25, 277.

or she seeks to justify a disposal of trust property.[74] The underlying default rule is that the trustee is expected to have the trust property in his or her control unless it was disposed of in an authorised fashion and in accordance with any relevant duties. If the trustee has disposed of an asset without authority, the falsification process enables the beneficiaries to disclaim the unauthorised entry and hold the trustee to his or her fundamental duty. If a trustee has improperly lost control of the trust asset, he or she is effectively treated as an insurer of it, in the sense that the unforeseeability of what happens to it subsequently is no defence to the trustee until the breach is repaired by the asset being recovered or replaced.[75] The accounting process disallows the unauthorised disbursement and treats the trustee as if he or she still holds the disbursed funds or asset:

> A trustee is always liable for the due application of trust funds received by him, and is accountable for all his own receipts; under the ordinary account he can only discharge himself by showing that he has paid the trust fund to the right person. … [W]hen an account is taken at the instance of the beneficiary, he will be charged, as still being in his hands, with any trust money which he cannot prove to have been properly disbursed by him …[76]

The trustee must therefore replace the wrongfully disbursed asset, or pay sufficient funds into the trust fund to enable that now to happen. The object of these rules was 'to emphasise that anything falling short in relation to the administration of trusts would not be tolerated and thereby to discourage breaches of trust.'[77]

The accounting process is thus concerned with the appropriateness of what the trustee has actually done with the trust property, rather than with deter-

[74] *Pickering v Pickering* (1839) 4 My & Cr 289, 298–9; 41 ER 113, 116 (Lord Cottenham LC). Even where not expressly included, powers of investment are commonplace in modern trust arrangements, as a result of default statutory powers: see, eg, *Trustee Act 1925* (NSW) s 14; *Trustee Act 2000* (UK) c 29, s 3.

[75] See *Caffrey v Darby* (1801) 6 Ves Jun 488, 496; 31 ER 1159, 1162 (Eldon MR); *Clough v Bond* (1838) 3 My & Cr 490, 496–7; 40 ER 1016, 1018 (Lord Cottenham LC); *Fyler v Fyler* (1841) 3 Beav 550, 568; 49 ER 216, 224 (Lord Langdale MR).

[76] *Re Windsor Steam Coal Co (1901) Ltd* [1929] 1 Ch 151, 166 (Lawrence LJ). See also *Re Anglo-French Co-Operative Society; Ex parte Pelly* (1882) 21 Ch D 492, 506 (Brett LJ); *Re Hulkes; Powell v Hulkes* (1886) 33 Ch D 552, 557 (Chitty J).

[77] Chantal Stebbings, *The Private Trustee in Victorian England* (Cambridge University Press, 2001) 172.

mining what might have been done if the trustee had acted properly. If the trustee has acted improperly, the assets which were wrongfully disposed of need to be returned so that the trust can be properly administered. In *White v Baugh*,[78] for example, the House of Lords held that a receiver who had paid money into a bank which failed was liable for the sum lost because he had placed improper restrictions on how the money could be withdrawn from the bank.[79] Lord Lyndhurst explained that it was 'altogether immaterial' that it had not been shown that those restrictions directly caused the loss to be suffered.[80] The receiver sought to avoid his liability to account for the sum that he had placed in the bank on the basis that the loss had been occasioned without any fault on his part.[81] He failed because his deposit of the funds on those terms was itself improper, irrespective of whether those terms had caused the loss of funds.[82]

The fact that the trustee had power to act in a different way, which would have brought about the same loss, is no defence for the trustee.[83] The court does not engage in speculation as to what might have been done, either by the trustee or by others. The account is concerned with the propriety, or not, of what the trustee actually did. One Irish decision suggests that this proposition should perhaps be tempered, in the sense that the accounting process should take account of what the trustee was duty-bound (rather than merely empowered) to have done, and that the trustee can set that off against the loss that has occurred.[84] However, Sir Edward Sugden LC(I) treated the case as one of mistake rather than misapplication, without explaining that difference, and acknowledged that there was no precedent for his order.[85] The case does not appear to have been followed subsequently and it seems inconsistent with the

[78] (1835) 3 Cl & Fin 44; 6 ER 1354. This was on appeal from *Salway v Salway* (1831) 2 Russ & M 215; 39 ER 376.

[79] *White v Baugh* (1835) 3 Cl & Fin 44, 64–5; 6 ER 1354, 1361–2 (Lord Lyndhurst).

[80] Ibid 65; 1362.

[81] Ibid 57; 1359 (Lord Brougham).

[82] Ibid 64; 1361–2 (Lord Lyndhurst). See also *Salway v Salway* (1831) 2 Russ & M 215, 220; 39 ER 376, 378 (Lord Brougham LC); Cory, above n 25, 278.

[83] *Cocker v Quayle* (1830) 1 Russ & M 535, 538; 39 ER 206, 207 (Sir John Leach MR). See also *Re Bell's Indenture; Bell v Hickley* [1980] 3 All ER 425, 438–9 (Vinelott J) which appears to have been based on the plaintiff's concession.

[84] *Hynes v Redington* (1844) 1 Jo & Lat 589, 600–1; 68 RR 349, 352 (Sir Edward Sugden LC).

[85] Ibid 600; 352.

clear line of authority which treats the improper application of trust funds as causing damage to the trust fund as soon as it occurs,[86] which remains so until the breach is purged by the funds being fully replaced.[87] If a trustee is, for example, obliged to invest trust funds in one particular asset but buys another, the disbursement cannot be justified and can be falsified in the accounts. In order to avoid that, the trustee must either return the misapplied funds, or use his own money to purchase the asset which should have been bought, and then treat it as a trust asset in the trust accounts. If it is not possible to do that now, that is the trustee's own fault. This approach avoids the need to draw potentially difficult distinctions between whether a trustee was obliged or merely had power to perform a mandate, particularly where that mandate was revocable.

Thus, the focus of the common accounting process is on restoring to the trust fund assets which have wrongfully been removed from it, in order to give effect to the trustee's fundamental duty to hold those assets and deal with them in accordance with the terms of the trust. It is not on attempting to determine what would have happened if the trustee had not acted in breach of trust. The process is, therefore, vastly different from that which applies where unliquidated damages are sought following a tort or a breach of contract. As the Privy Council has said, failure to appreciate that difference can lead the court into error,[88] as it is misleading to think about the trustee's liability in terms of causation. In order to distinguish it from claims for unliquidated damages, the trustee's liability was famously described by James and Baggallay LJJ as 'an equitable debt or liability in the nature of debt',[89] a view which Earl Halsbury LC agreed with in *Sharp v Jackson*.[90] Other case law denies that the trustee's liability generates a debtor–creditor relationship,[91] but

[86] See *Re Anglo-French Co-Operative Society; Ex parte Pelly* (1882) 21 Ch D 492, 506 (Brett LJ); *Devaynes v Robinson* (1857) 24 Beav 86, 95; 53 ER 289, 293 (Sir John Romilly MR).

[87] *Lander v Weston* (1855) 3 Drew 389, 394–5; 61 ER 951, 953–4 (Sir Richard Kindersley V-C).

[88] *British America Elevator Co Ltd v Bank of British North America* [1919] AC 658, 663–6 (Viscount Haldane).

[89] *Ex parte Adamson; Re Collie* (1878) 8 Ch D 807, 819.

[90] [1899] AC 419, 426. See also *Re Vassis; Ex parte Leung* (1986) 9 FCR 518, 527 (Burchett J).

[91] *Ex parte Taylor; Re Goldsmid* (1886) 18 QBD 295, 300–1 (Lord Esher MR). See also *Trustee of the Property of New, Prance & Garrard v Hunting* [1897] 1 QB 607, 616 (Vaughan Williams J); *Ex parte Stubbins; Re Wilkinson* (1881) 17 Ch D 58, 69 (James LJ); *Re Lake; Ex parte Dyer* [1901] 1 QB 710, 715 (Wright J). Most of the judgments which doubt the debt-like nature of a trustee's liability were actually decided on the basis that repayment of misapplied trust funds

whether something is a debt depends upon the purpose for which one is making that categorisation. What matters here is that a trustee's liability to replace trust funds is sufficiently distinct from a liability to pay unliquidated damages for a tort or breach of contract that it could be proven in bankruptcy in the same way a debt can be.

A causal analysis is also irrelevant where a disbursement is falsified on the basis that it was made imprudently. It is commonly thought that falsification is only concerned with situations where the entry is unauthorised, as distinct from imprudent. If the entry involves an unauthorised disbursement, then the case for falsification is straightforward, and the trustee must replace the funds.[92] But where the disbursement was within the terms of the trust but was imprudent, if all that the beneficiaries seek is the return of the amount that was disbursed,[93] they can falsify the disbursement and the trustee's imprudence means he or she will be unable to justify it.[94] In *Re Salmon; Priest v Uppleby*,[95] for example, a trustee was authorised to invest in mortgages of freehold land. He invested in mortgages of cottages in Hull, which was considered imprudent.[96] The trustee was therefore required to 'make good the loss occasioned to the trust estate by the improper investment',[97] but because the beneficiaries were not seeking to surcharge an account on a wilful default basis there was no need to establish where the fund would have stood if the trustee had acted prudently. The trustee was simply required to pay the deficiency on the mortgages. As Fry LJ put it, '[i]n some cases justice will be best done by realizing the security and making him pay the deficiency; but in some cases it may be right to make him pay at once the whole sum improperly

did not involve the kind of intention necessary for it to be set aside in bankruptcy as a voidable preference: see *Re Lake; Ex parte Dyer* [1901] 1 QB 710, 717 (Vaughan Williams LJ); *Ex parte Taylor; Re Goldsmid* (1886) 18 QBD 295, 300–1 (Lord Esher MR), 302 (Lindley LJ); *Trustee of the Property of New, Prance & Garrard v Hunting* [1897] 2 QB 19, 27 (Lord Esher MR), 29 (Smith LJ), 31 (Chitty LJ), affd *Sharp v Jackson* [1899] AC 419, 446 (Earl of Halsbury LC).

92 See *Rehden v Wesley* (1861) 29 Beav 213, 215; 54 ER 609, 609–10 (Sir John Romilly MR); *Re Salmon; Priest v Uppleby* (1889) 42 Ch D 351, 367 (Cotton LJ).

93 If the beneficiaries wish to have the amount that would have been earned if the trustee had made a prudent disbursement, they must surcharge on a wilful default footing.

94 The court may set off the loss against other gains: see, eg, *Trustee Act 1925* (NSW) s 90A.

95 (1889) 42 Ch D 351.

96 Ibid. Cotton LJ commented that 'we know the class of tenants likely to be attracted by cottage property in Hull': at 368.

97 Ibid 371 (Fry LJ).

invested, and let him take the benefit of the security.'[98] This is effectively a falsification of the imprudent disbursement,[99] requiring the trustee to return the sum that was improperly disbursed.[100]

Causation is similarly irrelevant where the beneficiaries seek to surcharge a common account. It is sometimes thought that the process of surcharging is limited in its application to wilful default accounts,[101] as they are more directly concerned with what the trust fund should contain. But that is not so. As Stuckey and Irwin said, '[a] surcharge can only charge the accounting party with moneys actually received by him, unless the accounts are being taken on the footing of wilful neglect and default'.[102] Thus, on a common account, if the trustee has received trust property which is not reflected in the trust accounts, the accounts can be surcharged to record those assets as trust property. Thus, the beneficiaries in *Re Fish* failed to establish any breach of trust but were nonetheless entitled to 'examine [the] accounts, to contest any items in them … and also, if they think fit … to surcharge any item which may be omitted in the accounts'.[103] Again, this involves no causal analysis,[104] as a surcharge in a common account amounts to no more than proof that the trustee actually did receive some property and that property ought to have been treated as part of the trust fund. The remedy will be that the trustee must for the future hold that asset for the trust, rather than for himself or herself.[105]

[98] Ibid.

[99] See, eg, *Knott v Cottee* (1852) 16 Beav 77, 79–80; 51 ER 705, 706 (Sir John Romilly MR).

[100] See also *Norris v Wright* (1851) 14 Beav 291, 308; 51 ER 298, 305 (Sir John Romilly MR); *Fry v Tapson* (1884) 28 Ch D 268, 282 (Kay J).

[101] See, eg, *Libertarian Investments Ltd v Hall* (2013) 16 HKCFAR 681, 733 (Lord Millett NPJ); Paul S Davies, 'Remedies for Breach of Trust' (2015) 78 *Modern Law Review* 681, 686 n 39; *Ultraframe (UK) Ltd v Fielding* [2005] EWHC 1638 (Ch) (27 July 2005) [1513] (Lewison J).

[102] G P Stuckey and C D Irwin, *Parker's Practice in Equity* (Lawbook Co, 2nd ed, 1949) 269. See also Williams and Guthrie-Smith, above n 42, 919; Jamie Glister, 'Breach of Trust and Consequential Loss' (2014) 8 *Journal of Equity* 235, 236.

[103] [1893] 2 Ch 413, 427 (Kay LJ); see also at 421 (Lindley LJ).

[104] Cf Jamie Glister and James Lee, *Hanbury and Martin's Modern Equity* (Sweet and Maxwell, 20th ed, 2015) 633–4 [24-008].

[105] If the asset was disposed of before the trust accounts were taken, the beneficiary can surcharge the account to establish that the asset was trust property, and then falsify the disposal of the asset (assuming it was not an authorised disbursement, such as the trustee can defend) and the trustee must restore the asset (or its current monetary equivalent) to the trust fund.

Where the account is taken on a wilful default footing, causation has a larger role to play. When an entry in the accounts is falsified, there is no substantive difference from the approach taken in a common accounting, as the analysis is the same in both cases: the entry is disallowed if the trustee is unable to justify it. Indeed, if the beneficiaries wish merely to falsify an entry in the accounts, they need only seek a common account. Wilful default accounting is really only necessary where the beneficiaries seek to argue that the trust fund would have contained other assets if the trustee had not failed, in breach of his or her duty, to obtain those other assets. This does involve some form of causal analysis, although the location of the burden of proof has proven important.

In *Re Brogden; Billing v Brogden* ('*Brogden*'),[106] Brogden covenanted to transfer, within five years of his death, £10 000 to trustees of a marriage settlement for his daughter. Two of the three trustees were sons of Brogden, who had been in business with him and who were continuing to run that business after Brogden died. The daughter's husband repeatedly pressed the other trustee, Budgett, to pursue payment of the money into the trust, but he appeared unwilling to press the point for fear of destabilising the business of his co-trustees.[107] The daughter sued, but the sons were insolvent. The claim therefore focused on Budgett's liability as the remaining solvent trustee. The Court of Appeal considered that, after five years had elapsed following Brogden's death, Budgett had been duty bound to call for payment of the sum into the daughter's trust and to take reasonable steps to enforce that payment if it were not received:[108] 'where a trustee does not do that which it is his duty to do, prima facie he is answerable for any loss occasioned thereby.'[109] Budgett argued that attempts to recover the sum due would have failed, or would have recovered less than the full sum. The Court held that Budgett must prove what would have happened if he had acted properly: '[i]t is the trustee who is seeking to excuse himself for the consequences of his breach of duty.'[110] Budgett failed to prove what he would have recovered if he had taken appropriate action, and so he was held liable for the entire sum. This approach thus

106 (1888) 38 Ch D 546.

107 Ibid 547–8 (North J).

108 Ibid 564 (Cotton LJ).

109 Ibid 567.

110 Ibid 568; see also at 572–3 (Fry LJ), 574 (Lopes LJ); *Re Stevens; Cooke v Stevens* [1898] 1 Ch 162, 171 (Chitty LJ).

involves a causal analysis — considering what would have happened but for the trustee's breach of duty — but it treats recovery of the entire debt as the prima facie loss caused by the breach and places the burden of disproving that on the trustee.

The decision in *Brogden* rests on the trustee's clear duty to collect the debt.[111] The same approach would apply where the trustee had a duty to make a particular investment and failed to do so.[112] Where, however, the trustee had a discretion as to which investments were to be made, and failed to exercise that discretion, the Lords Justices in *Robinson v Robinson* considered that they could not identify what the trustee ought to have done, and so were unable to hold him to his duty beyond requiring him to account for the least beneficial option available to him (the sum which ought to have been invested with interest).[113] This approach is, however, not so much concerned with the principles of trust accounting as it is with the difficulty of identifying what the trustee ought to have done, in order to hold him to that standard.[114] In *Nestle v National Westminster Bank plc* ('*Nestle*'),[115] Dillon LJ appeared to accept that the trustee's liability in *Robinson v Robinson* ought not to be measured by reference to the accident that one of the potential investments proved, with the benefit of hindsight, to have been more profitable than others.[116] But he rejected the view that this justifies holding the trustee liable only for the minimum investment value that could have been achieved.[117] In other words, the fact that a trustee has a range of possible investments to choose from should not relieve the trustee from having to pay in compensation the amount which the trust has lost as a result of him or her not having

[111] See also *Clack v Holland* (1854) 19 Beav 262, 271–2; 52 ER 350, 353–4 (Sir John Romilly MR).

[112] *Robinson v Robinson* (1851) 1 De G M & G 247, 260–1; 42 ER 547, 552 (Lord Cranworth LJ).

[113] Ibid 257–8; 551. The account here was originally taken in common form, directing 'the usual accounts': at 247; 547. However, it came on to be heard on further directions in *Robinson v Robinson*, and it was the later directions which involved, in effect, a wilful default accounting that purported to require the trustee to account for the highest value investment that could have been made. That order was reversed by the Lords Justices. See also *Partington v Reynolds* (1858) 4 Drew 253, 256; 62 ER 98, 99 (Sir Richard Kindersley V-C).

[114] See *Robinson v Robinson* (1851) 1 De G M & G 247, 259–61; 42 ER 547, 551–2 (Lord Cranworth LJ).

[115] [1993] 1 WLR 1260.

[116] Ibid 1268.

[117] Ibid; see also at 1280 (Staughton LJ).

acted in accordance with his or her duty to invest the trust fund in the way a prudent trustee would have acted.[118] This necessarily requires a hypothetical assessment of what a prudent investor would have done, in order to establish the manner in which the trustee should have acted.

Brogden and *Nestle* are both concerned with what would have happened if the trustee had complied with his duty. In *Brogden*, the duty to collect the debt was clear, but evidence was needed to establish what would have happened if the trustee had sought to do that; in *Nestle*, evidence was needed to establish what the trustee's duty required, by reference to how a prudent investor would have acted. Given that the purpose of a surcharge in a wilful default accounting is to ensure that the trust fund contains that which the trustee was duty-bound to acquire for it, it seems impossible to avoid a causal analysis of some sort in these cases.

III Modern Terminology

Before moving to consider the degree to which England and Australia may have departed from these traditional principles, two other developments merit attention.

A *Equitable Compensation*

The first is to notice that a number of the more recent cases have been pleaded and considered as claims for equitable compensation for breach of trust, rather than claims seeking an account and consequential remedies. The question this generates is whether this different form of claim requires or justifies any difference in the principles which the court applies. It is suggested that it does not.

As Heydon, Leeming and Turner identify, it seems that '[i]n the nineteenth century a more direct means of recovering loss came about when it became possible to sue for particular breaches of trust in isolation without using the equity courts' accounting procedures at all.'[119] They cite *Coppard v Allen*,[120] where Turner LJ explained that a claim could be brought against a trustee to

[118] Ibid.

[119] Heydon, Leeming and Turner, above n 11, 802 [23-030].

[120] (1864) 2 De G J & S 173, 180; 46 ER 341, 343–4.

establish a breach of trust without necessarily joining the other trustees, in contrast with the situation where an accounting was sought, in which case all trustees would need to be joined.[121] Similarly, in *Perry v Knott*, Lord Langdale MR held that beneficiaries could sue a trustee for a breach of trust without necessarily joining the other trustees, as a result of a change in the civil procedure rules which permitted suit against one of two jointly and severally liable parties without suing the other.[122] However, Beavan's notes to the decision in *Devaynes v Robinson* indicate that it would have been a mistake to assume that joinder of other trustees was unnecessary where the suit seeks to have 'trust property … brought back to be administered by the trustees, whose functions have not ceased'.[123]

In *Re Wrightson; Wrightson v Cooke* ('*Re Wrightson*'), Warrington J drew a difference between proof of wilful default on the one hand, and 'cases of breach of trust' on the other,[124] saying that '[i]n cases of breach of trust relief is given in respect of those specific breaches of trust which are proved, and in respect of those only'.[125] However, he did so in order to make the point that:

> if wilful default is alleged and if an instance is proved, then the trustees are not in a position to claim to have against them the ordinary account only, but the account must be directed on the footing of wilful default. In my judgment that rule does not apply to cases of breach of trust.[126]

While the last sentence is not especially clear, it is suggested that Warrington J was differentiating between the triggers for the two traditional forms of account, rather than between accounts and claims for equitable compensation. His Lordship's main point was to reject the proposition that proof of any breach of trust would necessarily lead to the 'roving inquiry' that a wilful

[121] Ibid 180–1; 344.

[122] (1842) 5 Beav 293, 296; 49 ER 590, 592. This decision was subsequently doubted, but only insofar as it suggested that one of several beneficiaries could sue without joining the others if the beneficiary sought recovery of their own share of the trust estate.That concern would not apply where the beneficiary is seeking reconstitution of the trust fund (effectively, in other words, an account): see *Lenaghan v Smith* (1847) 2 Ph 301, 302–3; 41 ER 958, 959 (Lord Cottenham LC).

[123] (1857) 24 Beav 86, 99; 53 ER 289, 294.

[124] [1908] 1 Ch 789, 799.

[125] Ibid 799–800.

[126] Ibid 800.

default accounting entails,[127] rather than to show a difference between claims for equitable compensation for breach of trust and claims for accounts following a breach. Indeed, his Lordship said that 'in the case of a breach of trust there is no general form of account which is substituted for the common account.'[128] In *Re Stevens; Cooke v Stevens*, Vaughan Williams LJ observed that a claim might be brought against an executor for negligent administration of the estate 'but the plaintiff would have to establish both the negligence and the damage resulting to the estate thereby'.[129] However, similarly to what has been seen in respect of *Re Wrightson*,[130] Vaughan Williams LJ also observed 'that if he would be liable in such an action, I am not sure that his liability might not be enforced by directing an inquiry in the course of taking the common account, without any substantial action for negligence.'[131]

The genesis of the distinct claim for equitable compensation for breach of trust, absent an accounting, is thus difficult to pinpoint. It seems likely that it originated in cases where the beneficiary only sought relief for a specific breach of trust, rather than seeking to scrutinise the entire trust accounts. If the beneficiary has proven the breach of trust and established its consequences, it might be sufficiently clear to the court what remedy is needed to repair that breach without needing to send the case off for an account to be taken of the trustee's management of the entire trust fund.[132] In *Kellaway v Johnson*,[133] for example, Lord Langdale MR identified a breach of trust in the sale of stock which had been held on trust and ordered that the stock be replaced with the dividends it would have earned had the trustees not disposed of it.[134] This remedy is equivalent to what would have followed from falsification of the disbursement on a common accounting, but it appears to have been done

127 Ibid 799.

128 Ibid.

129 [1898] 1 Ch 162, 177.

130 [1908] 1 Ch 789.

131 *Re Stevens; Cooke v Stevens* [1898] 1 Ch 162, 176.

132 See, eg, *Libertarian Investments Ltd v Hall* (2013) 16 HKCFAR 681, 723–6 [130]–[140] (Ribeiro PJ), 733 [174] (Lord Millett NPJ). See also *Houghton v Immer (No 155) Pty Ltd* (1997) 44 NSWLR 46, 59 (Handley JA); *Campbell v Gillespie* [1900] 1 Ch 225.

133 (1842) 5 Beav 319; 49 ER 601.

134 Ibid 324; 603.

without needing to take the accounts: '[a] more clear breach of trust was never committed.'[135]

As has been mentioned, the sharp distinction between common accounting and wilful default accounting began to break down, at least to some degree, following the judicature reforms.[136] The ability to provide a remedy which directly addresses an identified breach of trust, without unnecessary procedural obstacles being thrown in the way, seems consistent with that development. Further, even where an instance of wilful default was proven, the courts could order that an account be taken on a wilful default footing in respect of that breach alone, leaving the rest of the account to be taken on the usual basis, where there was nothing to suggest that other breaches of trust had occurred.[137] This ability to narrow the focus of a claim is also consistent with the development, from the mid-19th century, of the court's ability to give judicial advice on specific questions concerning the administration of a trust without needing to take over the entire execution of the trust, as had previously been the case through an order for general administration of the trust being made. The development of that narrower jurisdiction meant that the court no longer had to resort to taking over the entire trust in order to resolve a particular point of contention.[138] As Haddan observed, a partial administration of the personal estate of a deceased testator or intestate could be obtained without needing to seek a general administration of the estate, which limited the administration sought by the creditor or legatee to his or her own particular demand.[139] It seems likely that a similar narrowing of the trust accounting procedure led to the direct claim for equitable compensation for a breach of trust.

The importance of these observations lies in their implications for the principles that ought to apply where the claim is brought as a claim for equitable compensation for breach of trust, rather than as a claim for an account and consequential remedies. The difficulty in pinpointing its precise genesis, makes it difficult to be categorical. It is suggested, however, that if the claim for equitable compensation was simply a more direct and focused way

135 Ibid.

136 See above nn 56–8 and accompanying text.

137 *Re Tebbs; Redfern v Tebbs* [1976] 1 WLR 924, 928–30 (Slade J).

138 See *McLean v Burns Philp Trustee Co Pty Ltd* (1985) 2 NSWLR 623, 633–5 (Young J).

139 Haddan, above n 46, 54. See also *Re Blake; Jones v Blake* (1885) 29 Ch D 913, 916 (Cotton LJ).

of redressing a breach of trust without needing to go through the process of accounting because that was thought unnecessary in the instant case, the principles to be applied in determining the quantum of the remedy in such cases ought not to differ from those that would be applied in a full accounting.[140] It is important to remember that the question here is whether the remedy for a breach of trust ought to differ if the claim is brought as a claim for an account of the trust or as a claim for equitable compensation for the breach. It is not a question of concurrent liabilities under different causes of action generated by the same conduct. There is only one claim and the only question is whether the remedy for that claim differs depending on how it is brought. It is suggested that there is no reason why the result should differ simply because the plaintiff seeks equitable compensation directly rather than following the taking of an account.

B *Substitutive and Reparative Compensation*

The second recent development is the suggestion that a difference ought to be drawn between awards of equitable compensation which are substitutes for the proper performance of the trust and those which repair breaches of trust. This suggestion was developed by Steven Elliott,[141] and has been described thus:

> the remedy awarded against the trustee is an order that he pay money as a means of 'substitutively performing' his obligation to produce the missing trust property — an obligation that he could conceivably have 'specifically performed' by producing the property itself. … [O]rders of this kind are quite unlike other orders that can also be made against trustees, to pay 'reparative' compensation for losses which they cause by committing other breaches of duty, and which are brought within the accounting process by 'surcharging' the account by adding in the amount of the trustee's liability. Such an order might

[140] See also Robert Chambers, 'Liability' in Peter Birks and Arianna Pretto (eds), *Breach of Trust* (Hart Publishing, 2002) 1, 22; P G Turner, 'Measuring Equitable Compensation for Breach of Fiduciary Duty' (2014) 73 *Cambridge Law Journal* 257, 257.

[141] See Charles Mitchell, 'Equitable Compensation for Breach of Fiduciary Duty' (2013) 66 *Current Legal Problems* 307, 322 n 72.

> be made where the trustee causes a loss by breaching his duty of care, for example.[142]

The courts definitely have drawn a distinction between claims to recover trust property that was disposed of without authority or imprudently, and claims to have the trustee add to the trust fund property that which ought to have been, but was in fact not, acquired for the trust. Traditionally, that was the distinction between the usual or common accounting order and a wilful default accounting. As Edelman J has said, the label 'substitutive compensation' is based on the common account, and the label 'reparative compensation' is based on the account on the basis of wilful default.[143] However, without understanding the principles by which common accounting and wilful default accounting have operated, the new terminology does not add to understanding, beyond emphasising that the inquiries involved in those two kinds of accounting differ. Lord Toulson indicated some willingness to engage with the new terminology in *AIB*,[144] although he also somewhat confusingly referred to a third category of 'restitutive compensation',[145] which appears to be yet another label for the remedy that the court awards following falsification of an unauthorised disbursement in an account. These new labels add little to a clear understanding of the principles.[146]

IV Substantive Change

It is now possible to assess the degree to which the recent decisions in *Target Holdings*, *AIB* and *Youyang* involve any change from the traditional approach outlined above. It is suggested that the English cases definitely change that approach, but that the position in Australia remains unchanged and should continue as such.

142 Ibid 322 (citations omitted).

143 *Agricultural Land Management Ltd v Jackson [No 2]* (2014) 48 WAR 1, 67 [349].

144 See [2015] AC 1503, 1525 [53]–[54].

145 Ibid 1525 [56], 1529 [70].

146 Indeed, insofar as the new terminology might suggest that surcharging is limited to wilful default accounts (see Mitchell, above n 141, 322), the labels would be misleading: see above nn 101–3 and accompanying text.

A *England*

In *Target Holdings*,[147] funds were paid by a mortgagee to its solicitors, the solicitors having implied authority to release the funds to the mortgagor only upon receipt of executed transfers and mortgage charges.[148] It was accepted that the funds were held by the solicitors on trust for the mortgagee in the meantime. The solicitors released £1.49 million of the funds to the mortgagor without having received the necessary mortgage charges, but these were received several days later. Subsequently, the property market fell with the result that when the mortgaged properties were sold the mortgagee recovered only £0.5 million.[149] The mortgagee sued the solicitors in negligence, but also sought summary judgment on a claim that the solicitors should reconstitute the trust fund,[150] arguing that the disbursement of £1.49 million was a breach of trust which must be repaired by restoration of the sum wrongfully paid away.

Allowing an appeal against Warner J's grant of conditional leave to defend the trust claim, Peter Gibson and Hirst LJJ ordered the solicitors to repay £1.49 million with interest, less the £0.5 million which had been received from the sale.[151] Ralph Gibson LJ dissented, holding that even where the claim is one to replace trust funds wrongfully paid away 'the requirement [to establish causation of loss] is unquestionably part of the law and it would be astonishing if it were not.'[152] Without mentioning the clear authorities to the contrary,[153] Ralph Gibson LJ considered that where 'the loss would have happened if there had been no breach, then the court can and must so hold.'[154] For the majority, Peter Gibson LJ appeared to accept that causation was also necessary, but '[w]here the breach consists in the wrongful paying away of trust moneys so that there is an immediate loss, no inquiry is necessary: the causal

147 [1996] AC 421.

148 *Target Holdings Ltd v Redferns* [1994] 1 WLR 1089, 1095 (Ralph Gibson LJ), 1101 (Peter Gibson LJ).

149 Ibid 1090.

150 Ibid 1091.

151 Ibid 1106.

152 Ibid 1099.

153 See especially above nn 63–6 and accompanying text, which appears not to have been cited in argument.

154 *Target Holdings Ltd v Redferns* [1994] 1 WLR 1089, 1100.

connection is obvious.'[155] A trustee in that situation 'comes under an immediate duty to make restitution.'[156]

The solicitors appealed to the House of Lords, where Warner J's decision was reinstated. Lord Browne-Wilkinson delivered the only reasoned speech. His Lordship's analysis was predicated on the observation that '[i]n any ordinary use of words, the breach of trust … cannot be said to have caused the actual loss ultimately suffered by [the mortgagee] unless it can be shown that, but for the breach of trust, the transaction would not have gone through'.[157] His Lordship reasoned that the traditional equitable principles concerning compensation awards for breach of trust were developed in connection with traditional trusts and that they ought not to be applied to commercial trusts,[158] although in both contexts he seemed to think that 'there does have to be some causal connection between the breach of trust and the loss to the trust estate for which compensation is recoverable, viz the fact that the loss would not have occurred but for the breach.'[159] On the assumptions that had to be made in a summary judgment application, the mortgagee obtained exactly what it would have obtained if there had been no breach of trust. As such, it could not recover compensation on a summary judgment application as the breach of trust had not been shown to have caused any loss.[160]

Lord Browne-Wilkinson's emphasis on causation in *Target Holdings* left it somewhat unclear to what degree the decision involved departure from the traditional equitable principles which have been discussed above.[161] For example, for the proposition that 'there does have to be some causal connection between the breach of trust and the loss to the trust estate'[162] Lord Browne-Wilkinson cited *Nestle*[163] and *Re Miller's Deed Trusts*.[164] Both of those

155 Ibid 1102.

156 Ibid 1104.

157 *Target Holdings* [1996] AC 421, 431.

158 Ibid 434–5. This was asserted without reference to the long history of the use of trusts in commercial contexts, see *Elders Trustee & Executor Co Ltd v E G Reeves Pty Ltd* (1987) 78 ALR 193, 229–31 (Gummow J).

159 *Target Holdings* [1996] AC 421, 434.

160 Ibid 440.

161 See Peter Birks, 'Equity in the Modern Law: An Exercise in Taxonomy' (1996) 26 *Western Australian Law Review* 1, 47.

162 *Target Holdings* [1996] AC 421, 434.

163 [1993] 1 WLR 1260.

cases concerned what would, on traditional principles, be considered an attempt to surcharge a trust account on a wilful default footing,[165] where causation would be relevant. In contrast, *Target Holdings* itself involved an attempt to falsify an unauthorised disbursement, as could have been done on a common account without any causal analysis. Lord Browne-Wilkinson's use of authorities from one context in a case concerning the other left it unclear whether he misunderstood the traditional equitable principles or was instead trying to reframe those principles along causal lines.

This confusion was compounded by the fact that the actual result in *Target Holdings* could also have been reached by the application of traditional equitable principles.[166] The unauthorised disbursement of the £1.49 million was a clear breach of trust. If the beneficiary (the mortgagee) had sought an account of the trust at that point, the trustee would have been unable to justify the disbursement of the mortgage funds, and so the entry in the accounts would have been disallowed on a falsification. The trustee would then have had to replace those funds, with interest, in order to make the trust fund accord with the re-drawn trust accounts. But accounts were not taken at that stage. By the time the claim came to court, the solicitors had received the relevant mortgage charges. At the time they did so, their authority to perform the trust by paying out the trust funds on receipt of appropriate mortgage documentation had not been revoked. As such, the entry in the accounts of the mortgage charges as a trust asset could not be falsified. Equally, the trust beneficiary could not deny the trustee's authority at that time to release the mortgage funds once it had received the necessary charges. As such, the accounts would need to reflect release of the £1.49 million at the time when the mortgage charges were received. Overall, therefore, although the original disbursement was unauthorised and could be disallowed, the subsequent receipt of the mortgage charges was authorised, at which point the trust beneficiary cannot deny to the trustee payment for any relevant expenses

[164] (1978) 75 LSG 454.

[165] See above nn 115–7 and accompanying text.

[166] See P J Millett, 'Equity's Place in the Law of Commerce' (1998) 114 *Law Quarterly Review* 214; Matthew Conaglen, 'Explaining *Target Holdings v Redferns*' (2010) 4 *Journal of Equity* 288; Peter Watts, 'Agents' Disbursal of Funds in Breach of Instructions' [2016] *Lloyd's Maritime and Commercial Law Quarterly* 118, 121, 129, 134. Cf James Edelman, 'Money Awards of the Cost of Performance' (2010) 4 *Journal of Equity* 122, 128.

associated with receipt of that asset (ie release of the mortgage funds).[167] The point is not that the original disbursement was ever authorised, but rather that the trustee's conduct subsequent to that unauthorised disbursement was itself authorised and therefore needed to be reflected in the accounts. The bottom line of the trust accounts would thus match the actual state of the trust fund, with the consequence that no compensation was payable.

However, any lack of clarity as to whether *Target Holdings* heralded a departure from traditional equitable principles has since been dispelled by the Supreme Court's decision in *AIB*.[168] The facts in *AIB* were similar to those in *Target Holdings*, although with important differences. In *AIB*, the lender agreed to lend £3.3 million against the security of a property valued at £4.5 million, but the lender insisted on its mortgage being a first charge, which required prior mortgages to be redeemed.[169] Again, the loan funds were advanced to solicitors, who released them without first obtaining the necessary first charge over the property. As a result of confusion between two mortgage accounts, £1.2 million was paid to the prior mortgagee to clear its mortgage, but this was short by £0.3 million. In consequence, that £0.3 million was paid to the borrower, instead of the prior mortgagee, along with the remaining £1.8 million.[170] A first charge could thus not be obtained, but unlike *Target Holdings,* such a charge was never obtained and the lender took a second charge. When the borrower defaulted, the lender sold the property. After paying £0.3 million to the first chargee, the lender only received around £0.87 million. The solicitors admitted negligence, but the claim in contract was limited to the £0.3 million which the lender had lost as a result of not having had a first charge: the remaining loss was brought about by market movements rather than the solicitors' negligence. The lender therefore sued for breach of trust, arguing that the entire £3.3m had been disbursed in breach

167 Similarly, where a trustee has made an unauthorised investment, liability is avoided to the extent that the unauthorised investment has been realised and invested in an authorised fashion, even if not in the original investments: see *Re Massingberd's Settlement; Clark v Trelawney* (1890) 63 LT 296 298–9 (Cotton and Fry LJJ), although the subsequent investments in that case were found also not to be within the trustees' authority. See also *Davis v Spurling* (1829) 1 Russ *&* M 64, 67–8; 39 ER 25, 26–7 (Sir John Leach MR).

168 [2015] AC 1503.

169 Ibid 1514 [2] (Lord Toulson JSC).

170 Ibid 1515 [5]–[7].

of trust, as no valid first charge had been received, and thus needed to be replaced.[171]

At first instance, HHJ Cooke held that the breach of trust lay only in paying the £0.3 million to the borrowers rather than to the first chargee; the other payments were authorised as they were partial performance of the agreement between the lender and borrower.[172] On appeal, the Court of Appeal disagreed, holding that the solicitors were not authorised to release any of the trust funds until they held documents which confirmed that the funds paid to the prior mortgagee would be used to redeem the original mortgage, thus ensuring that the lender's new mortgage would have priority.[173] Despite that conclusion, however, the Court of Appeal was of the view that the claim was limited to the consequences of that breach. Applying the causal analysis from *Target Holdings*, Patten LJ said '[h]ad the remortgage been properly completed and Barclays' charge redeemed, AIB would still have been exposed to the losses caused by the borrower's default but would have had security for an additional £300 000 odd of its loan.'[174]

This approach was upheld on appeal in the Supreme Court. Lord Toulson delivered one judgment, Lord Reed another, and the other members of the Court agreed with both judgments. Lord Toulson considered that the case raised issues regarding the inter-relationship between equitable doctrines and remedies and their common law counterparts.[175] His Lordship considered that equity's traditional approach to remedying breaches of trust 'makes it necessary to create fairy tales',[176] in the sense that accounting requires the court to treat funds as if they are still held on trust when they are not,[177] or in a case like *Target Holdings*, to treat them as having been properly disbursed at some time other than when they actually were disbursed. His Lordship considered that 'in circumstances such as those in *Target Holdings* the extent of equitable compensation should be the same as if damages for breach of

171 Ibid 1545–6 [140] (Lord Reed JSC).

172 See *AIB Group (UK) plc v Mark Redler & Co Solicitors* [2012] EWHC 35 (Ch) (23 January 2012). This was summarised in [2013] EWCA Civ 45 (8 February 2013) [10] (Patten LJ).

173 *AIB Group (UK) plc v Mark Redler & Co Solicitors* [2013] EWCA Civ 45 (8 February 2013) [40]–[42].

174 Ibid [46]. Nicholas Patten QC, as he then was, argued *Target Holdings* for the lender.

175 *AIB Group* [2015] AC 1503, 1514 [1], 1524 [47].

176 Ibid 1528 [69].

177 Cf *Williams v Cental Bank of Nigeria* [2014] AC 1189, 1199–200 [13] (Lord Sumption JSC).

contract were sought at common law',[178] because the release of the funds from the trust effectively brought the trust to an end and the relationship between the solicitors and their client should then only be governed by contract.[179]

Lord Toulson's decision clearly endorses the causal approach applied by Lord Browne-Wilkinson in *Target Holdings* and it marks a clear shift away from the traditional equitable principles. On traditional principles, the entire disbursement was made without authority, and unlike *Target Holdings* nothing had subsequently been done with authority which would affect the bottom line of the trust accounts. On a traditional accounting, the solicitors should replace the entire £3.3 million and would then be treated as having purchased the second charge for themselves.[180] The solicitors would then be entitled to the £0.87 million proceeds of sale received when the rights associated with that second charge were exercised, thereby offsetting their liability to that extent but no more.

Lord Reed's judgment in *AIB* was more consistent with traditional principles, but like Lord Toulson's it too necessarily confirms a change in approach. Lord Reed acknowledged that the traditional equitable response to a claim for breach of trust by misapplication of trust funds was to take an account,[181] and he expressly disavowed the idea that a trustee's liability for a breach of trust must necessarily be identical to the liability that person bears for the same conduct if it also constitutes a breach of contract or a tort.[182] Lord Reed noted that:

> The classification of claims as arising in equity or at common law generally reflects the nature of the relationship between the parties and their respective rights and obligations, and is therefore of more than merely historical significance.[183]

As his Lordship recognised, the claim for equitable compensation is a more direct route to the end achieved through an accounting, but he considered that the 'measure of compensation is therefore the same as would be payable

[178] *AIB Group* [2015] AC 1503, 1529 [71].
[179] Ibid 1529–30 [74].
[180] See above n 98 and accompanying text.
[181] *AIB Group* [2015] AC 1503, 1533 [90].
[182] Ibid 1544–5 [136]–[137].
[183] Ibid 1545 [138].

on an accounting, although the procedure is different.'[184] His Lordship also rejected any categorical distinction between commercial and non-commercial trusts, as the fundamental principles of equity apply to all trusts.[185]

Virtually all of the reasoning in Lord Reed's judgment is therefore consistent with traditional principles, but his overall disposition of the case indicates, notwithstanding his view that Lord Browne-Wilkinson had not intended to depart from the orthodox view in *Target Holdings*,[186] that *Target Holdings* must have altered the law. Like HHJ Cooke, Lord Reed considered that there was merit in the view that the breach of trust in *AIB* only amounted to the payment of £0.3 million rather than the entire £3.3 million, but he acknowledged that this had not been argued and so the Court of Appeal's view of the breach had to be applied.[187] Notwithstanding that, however, he considered that the liability was limited to £0.3 million because *Target Holdings* requires rejection of the view 'that liability does not depend on a causal link between the breach of trust and the loss'.[188] In a simple case of misapplication of trust funds, rather than a case involving a surcharge on the wilful default basis, Lord Reed's application of the causal approach associated with *Target Holdings* involves a rejection of the traditional principle recognised in cases like *Magnus*,[189] under which causation of loss is not relevant because all that is required is restoration of the assets which were wrongfully removed from the trust fund.

Unlike *Target*, where the result could be justified by the application of traditional principles (albeit that the reasoning did not apply those principles directly), the result in *AIB* cannot be justified in that way. It could only be justified on traditional principles if the trustee's authority were re-interpreted consistently with what HHJ Cooke held (and Lord Reed hinted) it to be, but that was not done. Given the authority which the trustees were found to have, the entire £3.3 million was wrongfully disbursed from the trust fund, and on traditional principles the entire £3.3 million ought to have been replaced (subject to credit for the amount received as proceeds of the second charge),

[184] Ibid 1533–4 [91]; see also at 1538 [108].

[185] Ibid 1536–7 [102].

[186] Ibid 1539–40 [116].

[187] Ibid 1545–6 [140].

[188] Ibid.

[189] (1888) 37 Ch D 466. See above nn 61–7 and accompanying text.

unless statutory relief had been granted,[190] or unless the bank's actions in arranging the second charge were somehow treated as a waiver of its rights. The latter argument would require evidence regarding the bank's knowledge of the facts which constituted the breach[191] and of the rights which it had against the trustees,[192] and deliberate action which encouraged the trustees reasonably to believe that their breaches were accepted.[193] If it were made out, such consent would prevent falsification of the disbursement,[194] but as HHJ Cooke mentioned, the evidence regarding what happened when the breach came to light was not detailed,[195] and so there seems to have been insufficient evidence to establish the facts necessary to make out that sort of argument.[196]

The combined effect of the decisions in *Target Holdings* and *AIB* is to change the law in England. It departs from the principles traditionally associated with trust accounting and replaces them with a causal analysis

190 Given the Court reached a different view on the trustees' liability, the question of relief did not arise as the trustees accepted that they were liable to pay compensation in the amount of £0.3 million: see *AIB Group (UK) plc v Mark Redler & Co Solicitors* [2013] EWCA Civ 45 (8 February 2013) [52] (Patten LJ).

191 See generally *Walker v Symonds* (1818) 3 Swans 1, 58–60, 64; 36 ER 751, 772–4 (Lord Eldon LC); *Re Pauling's Settlement Trusts; Younghusband v Coutts & Co* [1962] 1 WLR 86, 108 (Lord Wilberforce); *Spellson v George* (1992) 26 NSWLR 666, 669 (Handley JA), 673–5 (Hope AJA).

192 Heydon, Leeming and Turner, above n 11, 807–8 [37–035]-[37–040]; James Hill, *Practical Treatise on the Law Relating to Trustees* (Geo Tucker Bispham (ed), T & J W Johnson & Co, 4th American ed, 1867) 821, 823–4.

193 *Byrnes v Kendle* (2011) 243 CLR 253, 279–80 [79] (Gummow and Hayne JJ).

194 An argument of this sort might not necessarily prevent a surcharge of the account. For example, in *AIB* it might still be argued that the trust fund would have contained £0.3 million more if the trustee had acted carefully. Whether the waiver rules out such a claim will depend on what the evidence establishes as to the intention of the waiving party and as to whether it is fair in all the circumstances that such a claim could still be run: *Walker v Symonds* (1818) 3 Swans 1, 58–60, 64; 36 ER 751, 772, 733–4 (Lord Eldon LC). See also *Re Pauling's Settlement Trusts; Younghusband v Coutts & Co* [1962] 1 WLR 86, 108 (Lord Wilberforce); *Spellson v George* (1992) 26 NSWLR 666, 669 (Handley JA), 673–5 (Hope AJA).

195 See *AIB Group (UK) plc v Mark Redler & Co Solicitors* [2013] EWCA Civ 45 (8 February 2013) [4] (Patten LJ).

196 Furthermore, even if such an argument were made out on the evidence, it might potentially amount only to acceptance of the second charge in partial settlement of the claim: see *Re Lake; Ex parte Howe Trustees* [1903] 1 KB 439; cf *Thornton v Stokill* (1855) 1 Jur (NS) 751; 102 RR 906, which could still leave the possibility that the remainder of the misapplied £3.3m was to be paid in compensation. But this too would depend on the evidence as to what was intended by the lender's acceptance of the second charge.

which asks in what position the trust beneficiary would have stood had the trustee not committed the breach of trust.

B *Australia*

It remains to consider the degree to which this change in English law might have been replicated in Australia. As has been mentioned, Heydon, Leeming and Turner have argued that the decision in *Target Holdings*, which Turner has described as a 'fundamental change to the law',[197] also represents the law in Australia[198] as a result of it having been adopted by the High Court of Australia in *Youyang*.[199] It is suggested that this argument cannot be reconciled with the facts of that case and the orders which were made following the High Court's decision.

Youyang is another case on facts similar to those in *Target Holdings*, although like *AIB*, and unlike *Target Holdings*, the trustee never received the documents which it ought to have obtained before the trust funds were disbursed. Youyang agreed to subscribe for 5000 shares in E C Consolidated Capital Ltd ('ECCCL'). Youyang paid $500 000 to ECCCL's solicitors, which the solicitors held on trust for Youyang to be applied in accordance with the terms of a subscription agreement. Those terms required the solicitors to procure a negotiable bearer deposit certificate which entitled Youyang to receive $500 000 when the certificate matured 10 years later. A relatively small portion of the remaining trust funds were then to be used to meet the solicitors' expenses and the remainder was to be given to ECCCL as working capital.[200]

The solicitors disbursed $256 800 in order to purchase the deposit certificate, paid approximately $21 600 towards expenses and then released the remaining $221 600 to ECCCL.[201] ECCCL failed, and the shares were worthless. The difficulty for the solicitors lay in the fact that the certificate they took in return for the $256 800 disbursement was not a bearer certificate, but rather simply a certificate of indebtedness which 'provided Youyang with

[197] P G Turner, 'The New Fundamental Norm of Recovery for Losses to Express Trusts' (2015) 74 *Cambridge Law Journal* 188, 189.

[198] See Heydon, Leeming and Turner, above n 11, 819 [23-180].

[199] (2003) 212 CLR 484.

[200] Ibid 492 [7].

[201] Ibid 496 [20].

no security whatsoever against any insolvency of ECCCL.'[202] That indebtedness was a debt owed to ECCCL, rather than something which Youyang could call upon, and it too was dissipated by ECCCL.[203] The disbursement of $256 800 had thus been made in breach of trust, as the solicitors accepted. In turn, their failure to obtain the correct deposit certificate meant that the solicitors had not had authority to release the other funds from the trust.[204]

Youyang sought to have the trust fund replenished, but was met with an argument that the appropriate remedy was equitable compensation.[205] Relying on *Target Holdings*, Brownie AJ accepted the solicitors' argument that what Youyang lost was not the sum which was paid away in breach of trust, but the sum which would have been received if the solicitors had acted consistently with the terms of the trust.[206] His Honour thus held that 'the measure of equitable compensation, at the date of judgment, will be approximately $410 000, and that it would be inappropriate to award any sum by way of interest, since this amount will represent the value at the date of judgment of $500 000 on 24 September 2003.'[207] In the Court of Appeal, Handley JA and Young CJ in Eq applied *Target Holdings*,[208] and concluded that the solicitors' breach of trust had caused no loss at all, because Youyang had consented to the certificate of indebtedness being changed in a way which permitted ECCCL to dissipate the funds.[209] On that basis, no award of equitable compensation ought to have been made. Hodgson JA agreed that the initial breach (in paying for the wrong certificate) caused no loss,[210] but his Honour found that the subsequent release of the remaining $221 600 to ECCCL did cause loss as those funds would still have been held in trust if they had not been

202 Ibid 496 [22].

203 *Youyang Pty Ltd v Alexander* [2000] NSWSC 698 (20 July 2000) [19] (Brownie AJ).

204 *Youyang* (2003) 212 CLR 484, 498 [32].

205 Ibid [28].

206 Ibid.

207 Ibid [29]. That date is when the bearer deposit certificate, had it been obtained, would have matured and produced the $500 000 yield for the investor.

208 *Youyang Pty Ltd v Minter Ellison* [2001] NSWCA 198 (25 June 2001) [16] (Handley JA), [76]–[78], [97] (Young CJ in Eq).

209 Ibid [18] (Handley JA), [79] (Young CJ in Eq).

210 Ibid [29].

wrongfully paid away.[211] On that basis, he would have ordered compensation in that sum plus interest.

On further appeal, the High Court unanimously held that the entire $500 000 had been misapplied in breach of trust, as the initial payment of $256 800 had not been made in return for the correct bearer deposit certificate and authority to make the remaining payments had been conditioned on that certificate first having been received.[212] The Court awarded compensation in the sum of the entire $500 000 together with interest.[213] Some elements of the reasoning in the Court's judgment suggest that it was adopting the thinking in *Target Holdings*, but it is suggested that the result is inconsistent with that thinking. The Court did quote from Lord Browne-Wilkinson's speech in *Target Holdings*,[214] and suggested that the case 'raise[d] considerations having an affinity with those which determined the outcome in *Target Holdings*.'[215] The Court also accepted Youyang's submission that 'it would not have suffered the loss of $500 000 but for the breaches of trust by Minters',[216] which might be read as adopting a causal analysis of the sort deployed in *Target Holdings*. Ultimately, the Court distinguished *Target Holdings* on the basis that, unlike *Target Holdings*, the correct bearer deposit certificate had never been obtained by the trustee in *Youyang*.[217]

However, it is suggested that these references to *Target Holdings* were made because the Court had to respond to the arguments which were presented,[218] which focused on the applicability or otherwise of the decision in *Target Holdings*, and because the lower courts in the case had also concentrated on that decision. In *Youyang*, the Court also cited the decision in *Magnus*,[219] for

211 Ibid [34].

212 *Youyang* (2003) 212 CLR 484, 498 [32].

213 Ibid 509 [71].

214 Ibid 499 [35], 504 [50].

215 Ibid 502 [44]. In *Australian Special Opportunity Fund LP v Equity Trustees Wealth Services Ltd* [2015] NSWCA 225 (11 August 2015) [160] (Bathurst CJ), this was taken to mean that 'so far as a claim is based on a breach of trust, it is necessary to prove that the breach caused the loss.'

216 *Youyang* (2003) 212 CLR 484, 504 [51].

217 Ibid 503 [48].

218 Ibid 487; Transcript of Proceedings, *Youyang Pty Ltd v Minter Ellison Morris Fletcher* [2002] HCATrans 577 (13 November 2012) 2341, 4416 (Jackson QC), 3179, 3932, 4023 (Bathurst QC).

219 (1888) 37 Ch D 466. See above nn 61–6 and accompanying text.

the proposition that events subsequent to the breach were not relevant to the trustee's liability unless they involved acquisition of the correct bearer deposit certificate.[220] The result in *Youyang* is not consistent with the sort of causal analysis which *Target Holdings* suggested and which *AIB* has now confirmed is the law in England, because if the trustees had acted properly they would have received a bearer deposit certificate which would only have entitled Youyang to receive $500 000 on 24 September 2003, not on 24 September 1993. As Handley JA said, the point of the deposit certificate in the overall investment scheme was that the investor 'hoped to derive profits from this investment but if the worst came to the worst it would get back its original investment, without interest, when the bearer certificate of deposit matured.'[221] In other words, on the causal analysis required under *Target Holdings*, there was no justification for Youyang receiving interest until its entitlement to the $500 000 crystallised in 2003. On that causal analysis, the award made by Brownie AJ was correct, and yet the High Court set that aside and awarded the entire $500 000 plus interest from 24 September 1993. That decision is consistent with traditional equitable principles, and is not consistent with *Target Holdings*. It is, in effect, a straightforward falsification of the unauthorised disbursement,[222] consistent with the *Magnus* decision to which the High Court referred.

The High Court did note in *Youyang* that '[t]his is not a case of providing a remedy to restore or replenish funds thereafter to be held on trusts yet to be fully performed',[223] which might also be thought to support the view that the court was adopting the thinking in *Target Holdings*. But the Court's statement here is simply a reflection of the fact that the usual remedy of reconstituting the trust so that it could be properly performed was impossible here, given the investment could not now possibly be made (ECCCL having already failed). That does not mean that the traditional principles are applied differently. It simply means that the trust accounts indicate what should now be held on

220 *Youyang* (2003) 212 CLR 484, 507 [63].

221 *Youyang Pty Ltd v Minter Ellison* [2001] NSWCA (25 June 2001) 198 [2]. See also *Youyang Pty Ltd v Alexander* [2000] NSWSC 698 (20 July 2000) [4] (Brownie AJ).

222 See also Jamie Glister, 'Breach of Trust and Conversion in a Falling Market' [2014] *Lloyd's Maritime and Commercial Law Quarterly* 511, 526.

223 (2003) 212 CLR 484, 499 [37].

bare trust for the beneficiary.[224] It makes sense, in that situation, for the compensation to be paid direct to the beneficiary, because if the ordinary course were followed, and the compensation paid back into the trust fund, those funds would be held at the beneficiary's direction;[225] it is obvious, given the beneficiary is seeking the funds, that the beneficiary would then simply direct that the funds be paid to him or her. The fact that something is done directly where traditional principles would suggest a less direct route does not mean that the traditional principles have ceased to govern. In this regard, it is noteworthy that less than a year after it decided *Youyang*, the High Court dealt with another claim coming out of the ECCCL investment debacle, and referred to the claim for breach of trust as 'restitutionary or restorative, in the sense used by Street J in *Re Dawson* … and recently exemplified in *Youyang*.'[226]

For these reasons, it is suggested that Australian law has not adopted the decision in *Target Holdings*, and continues to follow the traditional equitable principles discussed earlier. It may do so through the mechanism of a direct claim for equitable compensation for breach of trust, as in *Youyang*, without going through the formal process of taking accounts, but that does not affect the fundamental principles which determine the quantum of compensation payable.

V Conclusions

The decisions in *Target Holdings* and *AIB* changed the way in which trustees are held accountable for breaches of trust in England. Contrary to the traditional equitable principles, trustees in England can now argue that no compensation is payable following a breach of trust if the breach did not cause any loss, in the sense that the loss would have been suffered even if the trustee

224 Where a trustee's disbursement empties the trust of assets, the trust normally terminates. But where that disbursement was wrongful, the trust is kept alive for the purpose of enabling the beneficiaries to sue to have the fund reconstituted and properly administered: see *Johns v Johns* [2004] 3 NZLR 202, 219–20 [60]–[63] (Tipping J for Gault, Tipping and Glazebrook JJ); David Hayton, Paul Matthews and Charles Mitchell, *Underhill and Hayton's Law of Trusts and Trustees* (LexisNexis, 18th ed, 2010) 414 [21.4].

225 See *Elder's Trustee & Executor Co Ltd v Higgins* (1963) 113 CLR 426, 447 (Dixon CJ, McTiernan and Windeyer JJ).

226 *Alexander v Perpetual Trustees WA Ltd* (2004) 216 CLR 109, 126–7 [44] (Gleeson CJ, Gummow and Hayne JJ).

had not acted in breach. While considerations of that sort are consistent with the traditional approach where a trustee's account is surcharged on a wilful default footing, that is because the surcharge involves arguing that the trustee, had they acted in accordance with their duty, would have received more than he or she did, which requires some consideration of what would have happened if the duty had been complied with. On the other hand, the reasoning (albeit not the result) in *Target Holdings* and the decision in *AIB*, are inconsistent with longstanding authority regarding the falsification of unauthorised disbursements in trust accounts. The traditional approach is to require the trustee to restore those assets to the trust estate, irrespective of what might have happened if they had not been wrongfully removed in the first place. In place of that approach, English courts are now instructed to determine what would have happened if the trustee had complied with its duty.

It has been argued that this recent English innovation has not, contrary to the view presented by others, been adopted by the High Court of Australia in *Youyang*. Nor should the English approach be adopted in Australia. The underpinning rationale of the traditional approach to falsification is to hold the trustee up to its duty,[227] to maintain the trust assets and only to dissipate them in accordance with the terms of the trust. The concern with the English approach is that it undermines the strength of that duty.[228] The point is highlighted in something Gummow J said during argument in *Youyang*:

> It is just as if I go along to my solicitors, I put the solicitors in funds to complete the purchase of Blackacre, there is authority to pay out Blackacre, the proceeds to the vendor — that does not happen, they are paid somewhere else — and I go back to the solicitor and say, 'Where is my money?'[229]

That passage is not binding authority, but it well expresses the underpinning rationale for the traditional approach to falsification of an account: the trustee

[227] *Youyang* (2003) 212 CLR 484, 500 [39].

[228] There is thus some irony in the fact that Heydon, Leeming and Turner support the application of the *Target Holdings* approach, given they argue against adopting common law notions of causation in respect of claims for breach of equitable duties of care precisely because '[t]he institution of the trust would be undesirably weakened' if that approach were followed: see Heydon, Leeming and Turner, above n 11, 839 [23-370].

[229] Transcript of Proceedings, *Youyang Pty Ltd v Minter Ellison Morris Fletcher* [2002] HCATrans 577 (13 November 2012) 1431–5 (Gummow J).

should return the misapplied funds, and should not be permitted to argue about what loss might have been suffered if Blackacre had actually been acquired. If property is held in trust, with authority to use it in a specific way, the falsification process holds the trustee up to his or her duty to use the funds in that way and in that way alone. A trustee who has not complied with his or her duty cannot argue that the funds would have been lost in any event, through some other cause. In that way, the claim is very different from a claim for unliquidated damages following a breach of contract or a tort, but that is because the underlying principles and expectations of the parties are different. Trustees are held to a high standard, and are expected to abide by the terms of their trust.[230] The traditional principles for calculating liability for failure to do so are designed to hold trustees to those duties.

It is also important to bear in mind that while this approach may seem harsh, it is not unrealistically so. The facts of *AIB* illustrate this, given the Supreme Court's decision was clearly influenced by what it considered to be the commercial reality of the situation, in the sense that once the funds had been released the lender no longer had any commercial interest in the trust.[231] But that does disservice to the fact that the solicitors accepted that they had acted in breach of trust by releasing the funds to the wrong parties. It was not a difficult matter for the solicitors, as trustees, to identify the correct parties to whom payments should have been made by getting a formal redemption statement from the prior lender. Furthermore, even after that had not happened, the solicitors did not dispute their responsibility to pay compensation in the amount of £0.3 million, on the basis that they ought to have been paid to clear the prior charge. If the solicitors had simply applied that sum in redeeming the first charge which had priority over the lender's second charge, the second charge would then have acquired priority and the solicitors would have had no further liability as they would then, as in *Target Holdings*, have met the conditions for release of the trust funds. That would not have been difficult. Further, even where a trustee does not take these relatively straightforward steps, it can of course seek the beneficiary's consent to waive the breach, or judicial advice regarding a proposal to repair the breach,[232] or, failing all else, judicial relief from liability.[233] The availability of

230 See *Youyang* (2003) 212 CLR 484, 498 [32], 500 [39].

231 See *AIB* [2015] AC 1503, 1529–30 [74].

232 See, eg, *Trustee Act 1925* (NSW) s 63. See also *Robinson v Robinson* (1876) IR 10 Eq 189.

these various mechanisms means that it is neither unrealistic nor uncommercial to require a trustee who has failed to employ them to account in accordance with equity's traditional principles.

[233] See, eg, *Trustee Act 1925* (NSW) s 85. See also Charles Mitchell, 'Stewardship of Property and Liability to Account' [2014] *Conveyancer and Property Lawyer* 215, 227. This is not to say that such relief would necessarily be forthcoming, given it comes at a price to the beneficiaries: see *Santander UK plc v RA Legal Solicitors* [2014] EWCA Civ 183 (24 February 2014) [34] (Briggs LJ).