Forgiveness after the event

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Relief under section 61 Trustee Act 1925 and its equivalents[1] - the role of reasonableness and causation

1. Any sensible (and just) system of trust law must strike a balance between on the one hand regulating trusts and disciplining errant trustees and, on the other, maintaining a system which is workable, not least *for* trustees.

2. In any talk on English trust law it is difficult to resist, or to escape, the cliché of beginning in the 19th century. Then the spread of wealth increased the incidence of the express trust as a device for holding it. Moreover, the subject matter of such trusts was now frequently property other than land with the consequence that the rôle of (such) trustees became more active and complex.

3. By the final quarter of the century, the courts were expressing their concern that there should be a ready supply of people willing to serve as trustees and, for this reason, that the duties of trustees (and their liability for breaches of them) should not be so strict as to deter those who might otherwise act.

4. Thus Lord Blackburn in *Speight v Gaunt* (1883) 9 App Cas 1 said that

> "The authorities cited by the late Master of the Rolls, I think shew that as a general rule a trustee sufficiently discharges his duty if he takes in managing trust affairs all those precautions which an ordinary prudent man of business would take in managing similar affairs of his own.
> ...
> It would be both unreasonable and inexpedient to make a trustee responsible for not being more prudent than ordinary men of business are."

and earlier, in *Barnes v Addy* (1873-74) LR 9 Ch App 244 – in the context of the employment of professional agents by trustees, the responsible use of whom the Courts have long wished to encourage – James LJ had said that

[1] The terms of various Caribbean trust laws are materially identical *eg* Cayman, BVI, Bahamas, Bermuda.

> "I have long thought, and more than once expressed my opinion from this seat, that this Court has in some cases gone to the very verge of justice in making good to *cestuis que trust* the consequences of the breaches of trust of their trustees at the expense of persons perfectly honest, but who have been, in some more or less degree, injudicious. I do not think it is for the good of *cestuis que trust*, or the good of the world, that those cases should be extended."

5. Statutory intervention was eventually recommended by Parliamentary report[2] and in section 3 of the Judicial Trustees Act 1896 was enacted the predecessor of section 61 of the Trustee Act 1925.

6. Section 61 provides as to the "Power to relieve trustee from personal liability" that

> "If it appears to the court that a trustee, whether appointed by the court or otherwise, is or may be personally liable for any breach of trust ... but has acted honestly and reasonably, and ought fairly to be excused for the breach of trust and for omitting to obtain the directions of the court in the matter in which he committed such breach, then the court may relieve him either wholly or partly from personal liability for the same."

<u>Breach of trust</u>

7. But what is a breach of trust? The 32nd Edition of Snell's Equity tells us (at 30-001) that

> "A trustee is guilty of a breach of trust if he fails to do what his duty requires, or if he does what he is not entitled to do. Breaches of trust are almost infinitely various. ...
>
> Their common feature is that the trustee wrongfully exceeds the equitable authority conferred upon him by the trust instrument or by the general law, in circumstances which may lead to a liability to make good any losses which may result."

The purpose of stating the obvious in this way is to draw attention to the sheer breadth of the concept and thus the range of possible breaches which it contemplates, from some failure to

> "exercise such care and skill as is reasonable in the circumstances"

[2] House of Commons Select Committee on the Administration of Trusts, Report (1895 HC).

– see s 1(1) of the Trustee Act 2000[3] - to breach of a strict or absolute duty in relation, for example, to permitted forms of investment.

8. Cases in which section 61 arise are rather fewer in number than they used to be and indeed the same could be said for reported cases of breach of trust generally. There is a number of possible explanations:

    a. that standards expected of trustees have relaxed;

    b. that the standard of conduct of trustees has improved;

    c. that with the rise of the professional trustee has come more widespread use of exoneration clauses.

    There is likely to be some truth in each and in the last perhaps most of all.

9. There has, however, been something of a renaissance in the jurisprudence on section 61 in the past few years, principally in the context of professional (especially solicitors') liability. As with many fields of litigation, professional liability claims come in fashions depending upon economic cycles and business "innovations" as well as the ingenuity of the lawyers who advise about them. The solicitors' context commonly relates to property transactions and the release of the principal's (usually lender's) money to third parties in breach of the trust on which the solicitor holds it.

10. This, then, is the realm of the bare [commercial] trust

> "Bare trusts arise in a number of different contexts: e.g. by the ultimate vesting of the property under a traditional trust, nominee shareholdings and, as in the present case, as but one incident of a wider commercial transaction involving agency."

[3] *Cf* the time-honoured (and sometimes still applicable) formulation of the "ordinary prudent man of business".

Per Lord Browne-Wilkinson in *Target Holdings Ltd v Redferns* [1996] AC 421 (at 436) and which was of course a case involving a solicitor's bare trust.

11. Earlier in *Target*, Lord Browne -Wilkinson had said that

> "In the modern world the trust has become a valuable device in commercial and financial dealings. The fundamental principles of equity apply as much to such trusts as they do to the traditional trusts in relation to which those principles were originally formulated. But in my judgment it is important, if the trust is not to be rendered commercially useless, to distinguish between the basic principles of trust law and those specialist rules developed in relation to traditional trusts which are applicable only to such trusts and the rationale of which has no application to trusts of quite a different kind."

(*ibid* at p 436).

12. It is not clear exactly what "traditional trusts" means but *Target Holdings Ltd v Redferns* does establish that the liability of *any* trustee in breach is

- to restore or pay to the trust estate the assets lost as a consequence of the breach of trust

or

- to pay (equitable) compensation for that loss

The precise remedial consequences of breach depend (or ought to depend) on the nature of the trust, the nature of the breach and, possibly, the nature of the obligation breached[4]. Much may also depend on whether the trust subsists; in the case of bare trusts, frequently it will not.

The technique of section 61

13. This has 3 stages:

[4] This is not the place to engage that rather "large" question arising from *Bristol & West Building Society v Mothew* [1998] Ch 1, [1997] 2 WLR 436.

a. that the trustee acted honestly and reasonably (the burden being on the trustee to show this);

b. that the trustee ought fairly to be excused for the breach of trust[5]

c. *then* the court *may* relieve him or her either wholly or partly from personal liability for the same.

The wording of the section suggests that b. and c. are distinct *viz* that even if the Court takes the view that the trustee "ought fairly to be excused for the breach" it might still decide to refuse that relief as a matter of discretion but this distinction is not easy to understand not least because striking a balance between the deservingness of the trustee and the interest of the beneficiaries might be thought to be an essential component of deciding that the trustee "ought fairly to be excused"[6] and, if so, what is left for the Court to decide as a matter of subsequent discretion?

14. Of greater significance is the recognition that a. and b. are distinct and conjunctive requirements. It is not therefore sufficient for the Court to be satisfied of the honesty and reasonableness of the trustee – although this is how many of the cases on s 61 read – it also has to be fair to excuse him or her and this requires the exercise of a discretion which takes into account more than the position of the trustee.

<u>Reasonableness</u>

15. The role (and possibly even relevance) of reasonableness depends on the duty breached.

[5] and for omitting to obtain the directions of the court in the matter in which he/she committed such breach.

[6] A proposition for which there is authority: see *Marsden v Regan* [1954] 1 WLR 423 and *Bartlett v Barclays Trust Co. (No.1)* [1980] Ch 515.

a. Where it is a strict duty then there may well be scope for the Court's concluding that, say, the trustee's misapprehension of the content or effect of a particular duty was "reasonable".

b. More difficult is a breach of the trustee's duty to "exercise such care and skill as is reasonable in the circumstances", for here *unreasonableness* might be said to be an essential ingredient of the breach. How can the trustee be unreasonable yet reasonable?

16. Perhaps there will sometimes be circumstances where it is not necessary to pass through the looking glass to resolve this "tension", where there is reasonableness and reasonableness, but the answer may more readily be found by reference to causation as a means of distinguishing between reasonableness which is relevant and reasonableness which is not.

Causation

17. Section 61 says nothing expressly about causation but in *Nationwide Building Society v Davisons* [2012] EWCA Civ 1626, [2013] PNLR 12 – another solicitor's bare trust case – Sir Andrew Morritt C said of section 61 (at §48) that

> "[it] only requires [the trustee] to have acted reasonably. That does not, in my view, predicate that he has necessarily complied with best practice in all respects. The relevant action must at least be connected with the loss for which relief is sought and the requisite standard is that of reasonableness not of perfection."

18. This approach was elaborated by the Court of Appeal earlier this year in *Santander UK plc v RA Legal Solicitors* [2014] EWCA Civ 183. As to the role of causation, the parties adopted predictable positions:

a. the defendant solicitor contending for a strict causal connection between the conduct which amounted to breach of trust and the loss

b. the lender arguing for a broader approach based on wider-ranging criticisms of the solicitor's conduct.

19. Briggs LJ analysed the question in this way:

> "There are, I think, competing policy issues which affect this question. On the one hand, the court should be slow to gloss the general words of a statute, all the more so where it confers a broad discretion." [§23]

Nonetheless

> "It is in my view clear that a strict causation test casts the net too narrowly for the purpose of identifying relevant conduct." [§24]
>
> "Furthermore, it is also too restrictive to apply a 'but for' test which disregards conduct, however unreasonable, on the basis that even if the solicitor had acted reasonably in that respect, the fraud, and therefore the loss, would still have occurred.
> ...
> In my judgment it would not be appropriate to exclude as irrelevant, conduct which consisted of a departure from best or reasonable practice which increased the risk of loss caused by fraud, even if the court concludes that the fraudster would nonetheless have achieved his goal if the solicitor had acted reasonably." [§25]

But

> "it seems to me that some element of causative connection will usually have to be shown, and that conduct (even if unreasonable) which is completely irrelevant or immaterial to the loss will usually fall outside the court's purview under section 61" [§28]

And

> "I would, finally, caution against an over-mechanistic application of the requirement to show the necessary connection between the conduct complained of and the lender's loss. There may be highly unreasonable conduct which lies at the fringe of materiality in terms of causation, and only slightly unreasonable conduct which goes to the heart of a causation analysis. It would be wrong in my view to allow this purely mechanistic application of a causation-based test for the identification of relevant conduct to exclude the former from any consideration under section 61 ." [§29]

20. On the facts, the defendant had done just too many things wrong and the Court of Appeal therefore overturned the conclusion of the trial judge (Andrew Smith J) that relief should be granted.

21. Asking "what difference the relevant conduct made?" makes sense of the reasonable/unreasonable conundrum in the cases where it arises and, more generally, aligns the application of section 61 with the consequential approach to remedy for breach of trust which emerges from *Target Holdings Limited v Redferns*.

22. On the other hand, *if* in the first place a trustee is only liable to remedy what his or her conduct has *caused* then of what is there to be relieved of liability under section 61?

Section 1157 of the Companies Act 2006

23. This provides as to "Power of court to grant relief in certain cases**"** that

> (1) If in proceedings for negligence, default, breach of duty or breach of trust against–
>
> (a) an officer of a company, or
> (b) a person employed by a company as auditor (whether he is or is not an officer of the company), it appears to the court hearing the case that the officer or person is or may be liable but that he acted honestly and reasonably, and that having regard to all the circumstances of the case (including those connected with his appointment) he ought fairly to be excused, the court may relieve him, either wholly or in part, from his liability on such terms as it thinks fit.

Clearly the terms of section 1157 bear some similarity to section 61 but they are more widely drawn. They do not, however, contemplate actions which are not brought by or on behalf of the company.[7]

[7] *Customs & Excise Commissioners v hedon Akpha Ltd* [1981] 1 QB 818, CA.

24. The Court of Appeal in *Santander* had something to say about this too. At first instance, the judge had construed section 61 in part by reference to authorities on the application of section 1157[8] and which led him conclude that only "pervasive and compelling" negligence would preclude a trustee from relief under section 61.

25. The Court of Appeal said this was wrong. As Hoffman LJ had put it in *Re D'Jan of London Ltd* [1993] BCC 646

> "It may seem odd that a person found to have been guilty of negligence, which involves failing to take reasonable care, can ever satisfy a court that he acted reasonably. Nevertheless, the section clearly contemplates that he may do so."

As Briggs LJ put it in *Santander*:

> "section [1157] appears to contemplate that a company officer or auditor may have acted honestly and reasonably, even though negligent, whereas section 61 contemplates no such thing in relation to trustees."

It was therefore wrong to equate the two provisions:

> "I consider that the test of reasonableness rather than perfection identified in the Davisons case is amply sufficient for comparable cases under section 61 , and calls for no further elaboration."

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[8] Or rather section 727 of the Companies Act 1985 as it then was.