COMMENT ON PROFESSOR BRYAN'S PAPER: WHAT EXACTLY IS A REMEDIAL CONSTRUCTIVE TRUST?

There is a lot to like about Professor Bryan's paper.

He has classified the characteristics of the Australian species of remedial constructive trusts in a few particular factual scenarios. I will return to two of those scenarios but begin by reminding you of some relevant recent history.

Restitutionary analysis and constructive trusts

You will have noticed that at some points he approaches the analysis using the language of part of the taxonomy of the law of restitution. In particular, in discussing the constructive trust which can operate where the victim of a theft pursues the spouse of the thief who received the money innocently, he argues for liability for an additional personal remedy subject to a defence of change of position.[1]

Once upon a time, equity lawyers sailed in the Judicature Act stream of common law and equity, relatively undisturbed by the challenge of calls for coherence between common law and equity or within the application of equitable principle. This Judicature Act stream was not like any other river. The separate waters of equity and the common law never mixed. Equity lawyers kept their boats within the separated waters of equity, knowing that if there was a fight between the rules of common law and equity, the Judicature Act declared that equity was the winner.

Then, starting in the 1960s, the restitutionists invaded. I like to think of them as a bit like the Vikings. They came without respect for the old ways. They brought a new deity. Not Odin, but unjust enrichment. Local people were converted to the new ways, starting with names like Robert Goff and Gareth Jones in England[2] and Keith Mason and John Carter in Australia.[3] They swam about in our Judicature Act stream with gay abandon, refashioning principle to their concept of unjust enrichment.

A showdown was brewing, at least in Australia. The restitutionists initially conquered and occupied the common law waters of quasi-

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[1] Pages 15 – 16.

[2] Goff & Jones, *the Law of Restitution*, London, Sweet & Maxwell, 1966.

[3] Mason & Carter, *Restitution Law in Australia*, Australia, Lexis Nexis Butterworths, 1995.

contract, in respect of services supplied under an ineffective contract. That was *Pavey & Matthews Pty Ltd v Paul* in 1987.[4] There was some push back against the restitutionary framework in a contractual setting in *Lumbers v W Cook Builders Pty Ltd (in liq)* in 2008.[5] The restitutionists were less clearly the winners in the battles over payments made under an invalid Act. That was *Roxborough v Rothmans of Pall Mall of Australia Ltd* in 2001.[6]

They looked at applying the restitutionary framework in equity by way of a constructive trust for knowing receipt of trust property. Their advances were repelled there in *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* in 2007.[7]

Over the last 30 years there have been many such battles. The champions of both sides are a little bloodied. But in the process, with the academy leading the way, the Judges have re-examined, tested, and hopefully refined a number of areas of principle, including constructive trusts.

The Grand Bazaar of constructive trusts

As lawyers, whether practising lawyers, Judges, or in the academy, we all want a rigorous, workable taxonomy for the application of legal principle to factual situations. The effect of a viable system of classification enables each of us to get the same answer when we ask the same question. This is as true of constructive trusts as it is for other areas. Instead, as Professor Bryan's paper shows, the house of constructive trusts is more like the Grand Bazaar of Istanbul.

When the application for special leave to appeal was argued in *Island Maritime Ltd v Filipowski*, Justice Gummow said that "You cannot just say estoppel. That is a house with many rooms."[8] I think it is likely that there are more rooms in the house of constructive trusts than in the house of estoppel, according to current Australian authority, at least if one accepts some of the synthesis attempted by the High Court in the area of estoppels.

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4 (1987) 162 CLR 221.
5 (2008) 232 CLR 635.
6 (2001) 208 CLR 516.
7 (2007) 230 CLR 89.
8 [2005] HCA Trans 667.

But when it comes to constructive trusts, I prefer Professor Bryan's metaphor of the stalls in the Grand Bazaar of constructive trusts to the metaphor of a house of estoppels.

A few years ago, I bought a Turkish kilim in the Grand Bazaar. I have brought it to show you. The trouble with buying a kilim in the Grand Bazaar is that there are so many stalls which seem to be selling the same thing. To the uninitiated, you can buy from any stall – it is just a matter of price.

But things are not always what they seem. Hang about for a while, and you find out that there are subtle differences in the rugs. Not only that, some kilims sold there are not from the Eastern Turkish areas or neighbouring Iraq that make Turkish kilims at all. They are fakes, masquerading as the real thing. So it is with constructive trusts. Even experienced buyers can be confused.

Now, I have mentioned those things, in this rather long winded introduction, to introduce two small points of criticism I would venture of the substantial analysis Professor Bryan has given us.

The *Black v S Freedman & Co* constructive trust

In a couple of places, Professor Bryan refers to *Black v S Freedman & Co* - a decision of the High court in 1910[9] - as authority for the imposition of a constructive trust upon a person who receives property stolen by a thief from the plaintiff. In *Black*, the plaintiff employed the defendant's husband. The husband stole his employer's money and put it in his bank account. He transferred the money to his wife's account. The question was whether the employer could get an order that the wife held her entitlement to the balance in her account on trust for the employer. The High Court said "yes".

What is sometimes overlooked about *Black* is that the husband, the thief, was in a fiduciary relationship with the employer. The reasoning of Sir Samuel Griffith expressly referred to that as a basis for the relief. Justice O'Connor, on the other hand made a general statement that a thief holds stolen property on trust for the owner.[10]

But is that right? Assume that one of you takes a shine to my possibly genuine kilim here, and nicks it. You run outside into the street, but then

9 (1910) 12 CLR 105.
10 At p 110.

realize it will be a bit of a struggle to carry it home on the bus. You come across a backpacker walking down George St and persuade them to buy it.

I later see the backpacker walking around the city and say: “Hey! That’s my possibly genuine kilim. Some lawyer just stole it from me. Give it back.” He says, in a heavy Swedish, accent: “But I just bought it from this guy for 100 Kroner.”

“Well”, I say, “that’s too bad for you. I happen to be a lawyer and our great common law says that a thief acquires no title. Nemo dat non habet – what he hasn’t got he can’t give to you. So give it here.”

Why couldn’t this Swedish backpacker say to me: “Oh no you don’t. I happen to be an equity lawyer in my spare time. If he stole it from you, then I know that the thief held it for you on trust. Justice O’Connor says so in *Black’s* case. What happened is that he sold it to me. I paid good Kroner for it. I had no reason to suspect it was stolen. Because he was a trustee for you, he had legal title and I acquired the legal title bona fide for value and without notice. So put that in your common lawyer’s pipe and smoke it.”

Who wins? Well, luckily for me, I do. Why? Because the thief did not have the legal title. He was not a trustee of my rug. Justice O’Connor’s statement taken out of its factual context in *Black* is too wide.[11]

It all gets a bit harder when we talk about money. That is because the title to money passes so readily with possession.

But in *Black*, the wife did not have legal title to the employer’s money. She had property in a chose in action, a debt her bank owed to her. The debt was the result of a deposit of funds withdrawn from her husband’s account and paid into her account. The balance in the husband’s account before the withdrawal was a debt owed to him by the bank. It had been derived by the husband depositing the stolen money into his bank account. Before the money was deposited into the husband’s account, the employer had the legal title to it. At that point, the bank acquired legal title to the employer’s money and the husband acquired the property in the debt owed to him by the bank.

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11 Lord Goff in *Lipkin Gorman v Karnale Ltd* [1991] 2 AC 548 at 572 may have fallen into the same trap.

The property in the bank's debt to the wife had thus been obtained through the husband depositing the money he stole from the employer. The reasons of Sir Samuel Griffith in *Black* show the court was following and tracing the stolen money through the husband's account and into the wife's account. That is the only rational basis for the decision.

Sir Samuel said "if the alienee is a volunteer the estate may be followed into his hands whether he had notice of the trust or not".[12] In this passage he characterises the wife's property in her bank account as equivalent to holding a legal title to property subject to a claim by the holder of a prior equitable interest. He is equating the wife's property in the debt owed to her with the title of the employer to the money before it was dealt with by the husband.

What happens if the wife spends the money before the employer can claim it from her on constructive trust? Assume that she was not involved in the theft and had no notice of the employer's claim before she spends it. The NSWCA decided in 2009 that the wife is only liable to a claim to the amount remaining to her credit in the bank account. That was in a case called *Heperu Pty Ltd v Belle*.[13]

Professor Bryan says that the analysis of liability in *Heperu* came down to the identification of an equitable obligation under the puzzling label of "liability as a volunteer" and was a personal liability, but only for the amount of the balance remaining after the wife spent some of the money in the account. So far, so good, although I can see no reason why the constructive trust could not have been over the property, in the sense that the court could declare that wife held her interest in the debt owed to her by the bank on trust for the employer.

This is where Professor Bryan and I part company. He takes the restitutionist's view of a species of personal liability subject to a defence of change of position. Remember the picture of the terrible Viking raiders I tried to create before. Well see him there sitting with his horned helmet on while I say this.

Professor Bryan says that there is no reason why subject to the application of a defence of change of position a personal remedy for value received, meaning the amount of the proceeds of the theft, should not be available against the wife. It sounds simple enough. But as a

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12 At p 109.

13 [2009] NSWCA 252 at [130]-[132].

matter of principle, it moves this particular species of constructive trust from its source in *Black*. The movement is away from a cause of action which is a property based following and tracing process to the identifiable remains of property stolen by a fiduciary. The movement is towards a cause of action under a general theory of a restitutionary claim which is personal, not proprietory, and subject to the taxonomy of the restitutionary framework including a change of position defence.

This is not the time or place to explore my misgivings about the usefulness of the restitutionary framework when people try to apply it as a cause of action. My point here is that to date it has not been the method by which the law in the area of constructive trusts or equity operates and I am not convinced that it is the way to go.

I would rather leave things as they are. If you can follow or trace in equity, there is a constructive trust at the end of the journey over what remains against the innocent recipient. But if you want a personal money claim go to common law in the action for money had and received, unless the claim is against a fiduciary or trustee.

That cause of action was fairly comprehensively analysed by the House of Lords in *Lipkin Gorman v Karpnale Ltd* in 1991.[14] In the result in that case, Lord Goff of Chieveley, having accepted the ability of the plaintiff to follow and trace the money into the hands of the defendant, applied the restitutionary framework of unjust enrichment and defence of change of position. This treats the tracing claim as personal, not proprietory.

The High Court has not yet done so, in a similar case, as far as I am aware, although it came close in *David Securities Pty Ltd v Commonwealth Bank of Australia* in 1992.[15]

Constructive trusts and *Lister v Stubbs*

The second small gybe I will make, in an attempt to steal a little bit of the wind from Professor Bryan's sail, is about his analysis of constructive trusts and bribes. I say gybe because on this point he is the traditionalist and I cast myself in the role of the practical modernist. I don't see why he should get to wear the fashionable horned helmet all the time.

The very use of the word bribe often supposes a fiduciary relationship. A bribe is an affront to loyalty. In many circumstances it attracts not only

[14] [1991] 2 AC 548.
[15] (1991-1992) 175 CLR 353 at 385.

civil liability, but criminal responsibility as well. There is no question that a defaulting fiduciary is liable to account for the bribe received upon a constructive trust.

The fight in this area is a small one. Is the bribe the principal's property, when received? Or is it only the measure of a personal obligation to account, at least until an order imposing a constructive trust over specific property is imposed?

As Professor Bryan acknowledges, there are forms of constructive trust that are not based in proprietory rights. The claim of a beneficiary against a person who knowingly participates in a fraudulent breach of trust is a common example. The participant is liable to account meaning pay a sum of money as a constructive trustee to restore the trust corpus, even though they received no property. It is a personal remedy. Yet it is sometimes called a constructive trust.

What is the problem with bribes? The heat in the argument comes from *Lister v Stubbs* decided in 1890.[16] Until *Mareva* orders were invented by the English commercial court in the 1970s,[17] *Lister* stood for the proposition that you can't get an interlocutory injunction to restrain a defendant dealing with his or her assets unless you have a claim to a proprietory interest in the asset.[18] The dispute in *Lister* was whether the plaintiff principal had a proprietory interest in the bribe allegedly taken by the defendant agent. The plaintiff said I do have such an interest before an order is made to account for the bribe by way of constructive trust. The Court of Appeal said "no". The point of departure was that the bribe never was the principal's property.

The Full Court of the Federal Court in *Grimaldi v Chameleon Mining No 2* in 2012[19] refused to follow *Lister*. They said that the constructive trust in this setting is discretionary and therefore imposed at judgment and not before. That statement follows from *Muschinski v Dodds.*[20] They also said that it is well accepted that a constructive trust ought not to be imposed if there are other lesser orders capable of doing full justice. That statement follows from *John Alexander's Clubs Pty Ltd v White City Tennis Club Ltd.*[21]

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[16] (1890) 45 Ch D 1.
[17] *Mareva Compannia Naviera SA v International Bulkcarriers SA* [1975] 2 Lloyd's Rep 509.
[18] *Jackson v Sterling Industries Ltd* (1987) 162 CLR 612 at 618.
[19] (2012) 287 ALR 22.
[20] (1985) 160 CLR 583 at 623.
[21] (2010) 241 CLR 1 at [128].

Professor Bryan's dissatisfaction with these points resides in his view that this constructive trust is or should be a true trust. It should follow, he says, that where the trust targets identifiable property in a bribe the plaintiff has an entitlement to an order and should not be subject to discretion that the relief is only a lien or subject to the interests of creditors in insolvency.

In the end, this must be another way of saying that this constructive trust is more institutional than remedial and the plaintiff has a proprietory interest in the targeted property at some point before the making of the order. That is the traditionalist's view, as I call it.

I cant agree about this in the case of the bribe, as well in some other cases, such as the profits made by a defaulting fiduciary. In my view, this trust is necessarily remedial. The reason for the trust is to hold the defaulting fiduciary to the required standard of loyalty, not that the plaintiff has a proprietory interest in the ill gotten gains before judgment.

Avoiding intractable problems

I have to concede that there is a taxonomical clarity in being able to say that constructive trusts are like other trusts in most circumstances. But there are also problems with that approach, even in categories of case where the plaintiff asserts a proprietory interest, which a remedial constructive trust approach avoids.

An example I would give is *Carl Zeiss Stifftung v Herbert Smith No 2*, a 1969 decision of the Court of Appeal of England and Wales.[22] That case came out of the cold war. After the division of Germany, there were two Carl Zeiss lens manufacturing companies. One was the East German organization. The other was the West German organization. In 1964, the East German organisation claimed against the West German one that all the assets of the West German organization were held on trust for the East German organization. Then they sued the solicitors for the West German organization claiming that the fees received in acting for their clients were part of the trust property. It was alleged that the solicitors received that money with notice of the trust because they had notice of the claim.

The Court of Appeal dismissed the claim against the solicitors. It said that the solicitors could not have the requisite notice before the liability of

22 (1969) 2 Ch 276.

the West German organization to the plaintiff was established. The case may have been treated as a claim under the first limb of the rule in *Barnes v Addy*, [23] although even that is debatable. That has always struck me as an uncomfortable process of reasoning, because the notice requirement seems to have been placed at a fairly high level – and that is inconsistent with some other cases about the knowledge requirement under the first limb of the rule in *Barnes v Addy*.[24]

But if it is accepted that the claim is not simply a following claim, and that the species of constructive trust that is in play is a remedial trust some of the problems go away, starting with the proposition that the plaintiff's equity did not give an immediate proprietory interest in the West German organisation's assets in the hands of their solicitors.

The other point to keep in mind is that although a plaintiff who claims a remedial constructive trust risks getting less favourable relief because other relief may do, or because another person's interest may have to be considered, the practical problem created by *Lister* that by the time the claim is established the ill gotten gains will have disappeared is answered in the present day by the availability of a freezing order.

I hope that, like me, Professor Bryan's paper has got your equity lawyers' brains going. It is only by engaging in analysis at this level of principle and comparison, that we can see both the strengths and pitfalls of the different methodologies. It is also only by this level of rigour that the Australian remedial trust will emerge as both an intellectually and practically satisfying solution to what Professor Bryan rightly describes as some intractable problems.

His paper is, in my view, a valuable contribution to that work in progress.

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23 (1870) 9 Ch App 244 at 251.

24 See *Farah constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89 at [122]-[129], where the High Court said nothing much about the ongoing legal argument as to the extent of the knowledge required, notwithstanding that the point was left unclear in *Consul Development Pty Ltd v DPC Estates Ltd* (1974-1975) 132 CLR 373 at 411-414.