ARMITAGE v. NURSEand OTHERS [1997] EWCA Civ 1279 (19th March, 1997)

IN THE SUPREME COURT OF JUDICATURE CHANF 95/1318/B
COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE HIGH COURT OF JUSTICE
CHANCERY DIVISION

Royal Courts of Justice

Wednesday, 19th March 1997

Before:

LORD JUSTICE HIRST
LORD JUSTICE MILLETT
LORD JUSTICE HUTCHISON

- - - - - - - -

PAULA RACHEL ARMITAGE

Plaintiff

-v-

(1) RICHARD NURSE
(2) DUDLEY THOMAS BOWMAN STAMMERS AND
BRIAN ARTHUR STAMMERS

(the Personal Representatives of
Arthur George Stammers, deceased)
(3) MARGARET LAMBERT McLEOD FLATMAN
(the Personal Representative of Keith
Flatman, deceased, substituted by Order
to carry on dated 20th September 1995)
(4) JEFFREY REGINALD WRIGHT

Defendants

- - - - - - - -

(Transcript of the Handed Down Judgment of Smith Bernal Reporting Limited, 180 Fleet Street, London, EC4A 2HD. Telephone No:
0171-831 3183. Shorthand Writers to the Court.)

- - - - - - - -

MR. B. WEATHERILL Q.C. (instructed by Messrs Royds Treadwell,
London, EC4) appeared on behalf of the Appellant/Plaintiff.

MR. G. HILL (instructed by Messrs Hood Vores & Allwood) appeared on behalf of the First and Fourth Defendants, instructed by Messrs Greenland Houchen on behalf of the Second Defendant and instructed by Messrs Mills & Reeve on behalf of the Third Defendant.

J U D G M E N T
(As approved by the Court)

LORD JUSTICE MILLETT:

The main questions which arise in this appeal are concerned with the true construction of a trustee exemption clause in a settlement and the legitimate scope of such clauses in English law.
The Appellant ("Paula") has brought an Action for breach of trust against the Respondents who are the trustees and the personal representatives of deceased trustees of a Settlement of which she is the principal beneficiary. The Settlement contains a trustee exemption clause (Clause 15) in very wide and general terms as well as a special and more limited exemption clause (Clause 9). Jacob J was asked to decide three preliminary questions in the Action. They may be summarised as follows:
(1) Whether Clause 15 of the Settlement operates to absolve the Respondents from liability for all or any of the breaches alleged in the Amended Statement of Claim;
(2) Whether Clause 9(a) of the Settlement operates to similar effect;
(3) Whether any of the Paula's claims in respect of breaches of trust alleged to have been committed before 15th. June 1987 are statute-barred.
The Judge decided Question (1) in the affirmative and Questions (2) and (3) in the negative. He awarded the Respondents 80% of their costs but deprived them of the right to reimburse themselves out of the trust fund to the extent of the remaining 20%.
Both parties appeal to this Court. Paula appeals against the Judge's answer to Question (1) The Respondents appeal against his answers to Questions (2) and (3) and against his order depriving them of their right to reimburse themselves for their costs out of the trust fund. We have given leave to Paula to raise a further question which was not considered by the Judge. This is whether if, as the Judge ruled, Clause 15 on its true construction exempts each of the Respondents from all liability for breach of trust other than liability for his own dishonesty, the Clause is void for repugnancy or on grounds of public policy.

The facts.
The Settlement was made on 11th. October 1984. It was the result of an application to the Court by the trustees of a Marriage Settlement made by Paula's Grandfather for the variation of the trusts of the settlement under the Variation of Trusts Act 1958. Paula's Mother was life tenant under the Marriage Settlement and Paula, who was then aged 17, was entitled in remainder. The settled property consisted largely of land which was farmed by a family company called G.W. Nurse & Co. Limited ("the Company"). The Company had farmed the land for many years and until March 1984 it had held a tenancy of the land. Paula's Mother and Grandmother were the sole directors and shareholders of the Company.
Under the terms of the variation the property subject to the trusts of the Marriage Settlement was partitioned between Paula and her Mother. Part of the land together with a sum of £230,000 was transferred to Paula's Mother absolutely free and discharged from the trusts of the Marriage Settlement. The remainder of the land ("Paula's land") together with a sum of £30,000 was allocated to Paula. Since she was under age, her share was directed to be held on the trusts of a settlement prepared for her benefit. So the Settlement came into being.
Under the trusts of the Settlement the trustees held the income upon trust to accumulate it until Paula attained 25

with power to pay it to her or to apply it for her benefit. Thereafter and until Paula attained 40 they held the income upon trust to pay it to her. The capital was held in trust for Paula at 40 with trusts over in the event of her death under that age, and with provision for transferring the capital to Paula in instalments after she had attained 25 but not 40.
The Settlement, which must be taken to have been made by Paula as well as by her Mother, appears to have been drawn by Counsel for the Marriage Settlement Trustees (Mr. P.W.E.Taylor Q.C. and Mr. Geoffrey Jaques) and approved on Paula's behalf by Junior Counsel who appeared for her guardian ad litem. It was approved on her behalf by the High Court (H.H.Judge Fitzhugh Q.C.).

The pleadings.

The Amended Statement of Claim pleads a number of breaches of trust in detail. The Judge summarised them under four heads. First, Paula complains that in breach of trust the trustees appointed the Company to farm Paula's land as well as the land which had been transferred to her Mother. It is alleged that this was not merely grossly imprudent but was expressly forbidden by Clause 12 of the Settlement, inserted for fiscal reasons, which provides that no capital or income subject to the trusts of the Settlement shall in any circumstances whatsoever be paid or applied beneficially (save for full consideration) or be applied for the benefit whether directly or indirectly of Paula's Mother or Grandmother. (The Respondents, of course, plead that the Company's obligation to manage the farm constituted full consideration for the £500 a quarter which it was paid for doing so. It is not alleged that the Company's appointment had any adverse fiscal consequences.)
Secondly, it is alleged that in breach of trust the trustees failed thereafter properly to supervise the Company's management of Paula's land. Thirdly, it is alleged that the trustees failed to make proper inquiry into the reasons why the value of Paula's land apparently fell dramatically between the date on which it was valued for the purposes of the partition in 1984 and the date when it was sold in 1987. Finally, it is alleged that the trustees failed to obtain proper payment of interest in respect of a loan made to Paula's Mother.
Before us Counsel for Paula has summarised the pleadings more generally. They allege, he says, not merely a failure to distinguish between Paula's interests and those of her family but a deliberate course of conduct on the part of the trustees to disregard the interests of Paula and subordinate them to the interests of her Mother or other members of the family who were not objects of the trust; or at the very least a conscious indifference to Paula's interests.
Before analysing the pleadings in more detail, it is convenient to consider the scope Clause 15 of the Settlement.

Clause 15 of the Settlement.

Clause 15 of the Settlement is in the following terms:
"No Trustee shall be liable for any loss or damage which may happen to Paula's fund or any part thereof or the income thereof at any time or from any cause whatsoever *unless such loss or damage shall be caused by his own actual fraud* " (my emphasis).
The Clause was taken from Hallett's Conveyancing Precedents (1965 ed.). A more prolix clause to the same effect may be found in Key & Elphinstone's Conveyancing Precedents (15th.Ed.)(1953). In my judgment the meaning of the Clause is plain and unambiguous. No trustee can be made liable for loss or damage to the capital or income of the trust property caused otherwise than by his own actual fraud. "Actual fraud" means what it says. It does not mean "constructive fraud" or "equitable fraud". The word "actual" is deliberately chosen to exclude them.
Counsel for Paula submits that in a settlement the context requires the word "fraud" to be given the extended meaning which the Courts of Equity came to give it. The distinction between fraud properly so-called and other cases to which the Court of Chancery, in his own words
"undoubtedly did apply the term "fraud", although I think unfortunately"
is expounded in the speech of Viscount Haldane in Nocton v Ashburton [1914] AC 932. As he explained
"in Chancery the term "fraud" thus came to be used to describe what fell short of deceit, but imported breach of a duty to which equity had attached its sanction."

It is worthy of note that he himself used the expression "actual fraud" throughout his speech to distinguish cases of common law fraud or deceit from these other cases. Lord Dunedin did the same when he said at p. 963
"...if based on fraud, then, in accordance with the decision in Derry v Peek (1889), 14 AppCas 337, the fraud proved must be actual fraud, a mens rea, an intention to deceive."
Derry v Peek established that nothing short of a fraudulent intention in the strict sense will suffice for a case of

deceit or fraud properly so called. It requires proof of dishonesty. Nothing less will do. Gross and culpable negligence is not enough. This was confirmed in Nocton v Ashburton, which also established that dishonesty is not a necessary factor in cases of so-called equitable fraud.
In my judgment, therefore, Clause 15 is apt to exclude liability for breach of trust in the absence of a dishonest intention on the part of the trustee whose conduct is impugned. I would have added nothing further but for the confusion which appears to have been engendered in the attempt to apply the concept of actual fraud to an allegation of breach of trust.
The common law knows no generalised tort of fraud. Derry v Peek was an action for damages for deceit, that is to say, for fraudulent misrepresentation. In such a case fraud must be proved by showing that the false representation was made knowingly, that is to say, without an honest belief in its truth; or recklessly, that is to say, not caring whether it was true or false. Care needs to be taken when these concepts are applied not to a representation but to a breach of trust. Breaches of trust are of many different kinds. A breach of trust may be deliberate or inadvertent; it may consist of an actual misappropriation or misapplication of the trust property or merely of an investment or other dealing which is outside the trustees' powers; it may consist of a failure to carry out a positive obligation of the trustees or merely of a want of skill and care on their part in the management of the trust property; it may be injurious to the interests of the beneficiaries or be actually to their benefit. By consciously acting beyond their powers (as, for example, by making an investment which they know to be unauthorised) the trustees may deliberately commit a breach of trust; but if they do so in good faith and in the honest belief that they are acting in the interest of the beneficiaries their conduct is not fraudulent. So a deliberate breach of trust is not necessarily fraudulent. Hence the remark famously attributed to Selwyn LJ by Sir Nathaniel Lindley MR in the course of argument in Perrins v Bellamy [1889] 1 Ch. 797, 798:
"My old Master, the late Lord Justice Selwyn, used to say: "The main duty of a trustee is to commit judicious breaches of trust.""

The expression "actual fraud" in Clause 15 is not used to describe the common law tort of deceit. As the Judge appreciated it simply means dishonesty. I accept the formulation put forward by Mr. Hill on behalf of the Respondents which (as I have slightly modified it) is that it
"...connotes at the minimum an intention on the part of the trustee to pursue a particular course of action, either knowing that it is contrary to the interests of the beneficiaries or being recklessly indifferent whether it is contrary to their interests or not".

It is the duty of a trustee to manage the trust property and deal with it in the interests of the beneficiaries. If he acts in a way which he does not honestly believe is in their interests then he is acting dishonestly. It does not matter whether he stands or thinks he stands to gain personally from his actions. A trustee who acts with the intention of benefiting persons who are not the objects of the trust is not the less dishonest because he does not intend to benefit himself.
In my judgment Clause 15 exempts the trustee from liability for loss or damage to the trust property no matter how indolent, imprudent, lacking in diligence, negligent or wilful he may have been, so long as he has not acted dishonestly.

The permitted scope of trustee exemption clauses.

It is submitted on behalf of Paula that a trustee exemption clause which purports to exclude all liability except for actual fraud is void, either for repugnancy or as contrary to public policy. There is some academic support for the submission (notably an article by Professor Matthews in (1989) Conveyancer 42 and Hanbury and Martin's Modern Equity (14th. Ed.) pp. 473-4) that liability for gross negligence cannot be excluded, but this is not the view taken in Underhill & Hayton's Law of Trusts and Trustees (15th. Ed.) (1995) pp. 560-1 (where it appears to be taken only because the editor confusingly uses the term "gross negligence" to mean reckless indifference to the interests of the beneficiaries.) In its Consultation Paper No. 214 the Law Commission states at para. 33.41:
"Beyond this, trustees and fiduciaries cannot exempt themselves from liability for fraud, bad faith and wilful default. It is not, however, clear whether the prohibition on exclusion of liability for "fraud" in this context only prohibits the exclusion of common law fraud or extends to the much broader doctrine of equitable fraud. It is also not altogether clear whether the prohibition on the exclusion of liability for "wilful default" also prohibits exclusion of liability for gross negligence although we incline to the view that it does."

This passage calls for two comments. First, the expression wilful default is used in the cases in two senses. A trustee is said to be accountable on the footing of wilful default when he is accountable not only for money

which he has in fact received but also for money which he could with reasonable diligence have received. It is sufficient that the trustee has been guilty of a want of ordinary prudence: see, for example, Re Chapman [1896] 2 Ch 763. In the context of a trustee exclusion clause, however, such as Section 30 of the Trustee Act, 1925 it means a deliberate breach of trust: *Re* Vickery [1931] 1 h. 572. The decision has been criticised, but it is in line with earlier authority: see Lewis v Great Western Railway Co. (1877(3 QBD 195; Re Trusts of Leeds City Brewery Ltd.'s Debenture Stock Trust Deed [1925] Ch. 532n; Re City Equitable Fire Insurance Co. [1925] 1 Ch. 407. Nothing less than conscious and wilful misconduct is sufficient. The trustee must be "conscious that, in doing the act complained of or in omitting to do the act which it said he ought to have done, he is committing a breach of his duty, or is recklessly careless whether it is a breach of his duty or not " *per* Maugham J in Re Vickery (*supra*) at p. 583).

A trustee who is guilty of such conduct either consciously takes a risk that loss will result, or is recklessly indifferent whether it will or not. If the risk eventuates he is personally liable. But if he consciously takes the risk in good faith and with the best intentions, honestly believing that the risk is one which ought to be taken in the interests of the beneficiaries, there is no reason why he should not be protected by an exemption clause which excludes liability for wilful default.

Secondly, the Law Commission was considering the position of fiduciaries as well as trustees, and in such a context it is sensible to consider the exclusion of liability for so-called equitable fraud. But it makes no sense in the present context. The nature of equitable fraud may be collected from the speech of Viscount Haldane in Nocton v Ashburton and Snell's Equity (29th. Ed.) pp. 550-1. It covers breach of fiduciary duty, undue influence, abuse of confidence, unconscionable bargains, and frauds on powers. With the sole exception of the last, which is a technical doctrine in which the word "fraud" merely connotes excess of *vires*, it involves some dealing by the fiduciary with his principal and the risk that the fiduciary may have exploited his position to his own advantage. In Earl of Aylesford v Morris (1873), 8 Ch.App.484 Lord Selborne LC said at p. 491:

"Fraud does not here mean deceit or circumvention; it means an unconscientious use of the power arising out of these circumstances and conditions..."

A trustee exemption clause such as Clause 15 of the Settlement does not purport to exclude the liability of the fiduciary in such cases. Suppose, for example, that one of the Respondents had purchased Paula's land at a proper price from his fellow trustees. The sale would be liable to be set aside. Clause 15 would not prevent this. This is not because the purchasing trustee would have been guilty of equitable fraud, but because by claiming to recover the trust property (or even equitable compensation) Paula would not be suing in respect of any "loss or damage" to the trust. Her right to recover the land would not depend on proof of loss or damage. Her claim would succeed even if the sale was at an overvalue; the purchasing trustee could never obtain more than a defeasible title from such a transaction. But Clause 15 would be effective to exempt his fellow trustees from liability for making good any loss which the sale had occasioned to the trust estate so long as they had acted in good faith and in what they honestly believed was Paula's interests.

Accordingly, much of the argument before us which disputes the ability of a trustee exemption clause to exclude liability for equitable fraud or unconscionable behaviour is misplaced. But it is unnecessary to explore this further, for no such conduct is pleaded. What is pleaded is, at the very lowest, culpable and probably gross negligence. So the question reduces itself to this: can a trustee exemption clause validly exclude liability for gross negligence?

It is a bold submission that a clause taken from one standard precedent book and to the same effect as a clause found in another, included in a settlement drawn by Chancery Counsel acting for an infant settlor and approved by the Court on her behalf, should be so repugnant to the trusts or contrary to public policy that it is liable to be set aside at her suit. But the submission has been made and we must consider it. In my judgment it is without foundation.

There can be no question of the clause being repugnant to the trust. In Wilkins v Hogg ((1861) 31 L.J.Ch. 41 at p.42 Lord Westbury LC challenged counsel to cite a case where an indemnity clause protecting the trustee from his ordinary duty had been held so repugnant as to be rejected. Counsel was unable to do so. No such case has occurred in England or Scotland since.

I accept the submission made on behalf of Paula that there is an irreducible core of obligations owed by the trustees to the beneficiaries and enforceable by them which is fundamental to the concept of a trust. If the beneficiaries have no rights enforceable against the trustees there are no trusts. But I do not accept the further submission that these core obligations include the duties of skill and care, prudence and diligence. The duty of the trustees to perform the trusts honestly and in good faith for the benefit of the beneficiaries is the minimum necessary to give substance to the trusts, but in my opinion it is sufficient. As Mr. Hill pertinently pointed out in

his able argument, a trustee who relied on the presence of a trustee exemption clause to justify what he proposed to do would thereby lose its protection: he would be acting recklessly in the proper sense of the term.
It is, of course, far too late to suggest that the exclusion in a contract of liability for ordinary negligence or want of care is contrary to public policy. What is true of a contract must be equally true of a settlement. It would be very surprising if our law drew the line between liability for ordinary negligence and liability for gross negligence. In this respect English law differs from civil law systems, for it has always drawn a sharp distinction between negligence, however gross, on the one hand and fraud, bad faith and wilful misconduct on the other. The doctrine of the common law is that
"gross negligence may be evidence of mala fides, but is not the same thing"

per Lord Denman CJ in Goodman v Harvey (1836) 4 A&E 870.
But while we regard the difference between fraud on the one hand and mere negligence, however gross, on the other as a difference in kind, we regard the difference between negligence and gross negligence as merely one of degree. English lawyers have always had a healthy disrespect for the latter distinction. In Hinton v Dibber (1842) 2 QB 646 Lord Denman doubted whether any intelligible distinction exists; while in Grill v General Iron Screw Collier Co. (1866), 35 LJCP 321,330 Willes J famously observed that gross negligence is ordinary negligence with a vituperative epithet. But civilian systems draw the line in a different place. The doctrine is *culpa lata dolo aequiparetur;* and although the maxim itself is not Roman the principle is classical. There is no room for the maxim in the common law; it is not mentioned in Broom's Legal Maxims.
The submission that it is contrary to public policy to exclude the liability of a trustee for gross negligence is not supported by any English or Scottish authority. The cases relied on are the English cases of Wilkins v Hogg (supra) and Pass v Dundas 1880), 43 LT 665; and the Scottish cases of Knox v Mackinnon (1888), 13 App. CAS. 753 and Rae v Meek (1889), 14 App.Cas 558; ; Wyman v Paterson [1900] AC 271; and Clarke v Clarke's Trustees [1925] SC 693. These cases, together with two other Scottish cases Seton v Dawson (1841) 4 D 310 13 and Carruthers v Carruthers [1896]AC. 659 and cases from the Commonwealth and America, were reviewed by the Jersey Court of Appeal in Midland Bank Trustee (Jersey) Limited v Federated Pension Services Limited [1996] Pensions Law Reports 179 in a masterly judgment delivered by Sir Godfray Le Quesne QC.
In Wilkins v Hogg Lord Westbury LC accepted that no exemption clause could absolve a trustee from liability for knowingly participating in a fraudulent breach of trust by his co-trustee. But subject thereto he was clearly of opinion that a settlor could by appropriate words limit the scope of the trustee's liability in any way he chose. The decision was followed in Pass v Dundas, where the relevant clause was held to absolve the trustee from liability. In the course of his judgment Bacon V.-C. stated the law in the terms in which counsel for the unsuccessful beneficiaries had stated it, viz. that the clause protected the trustee from liability unless gross negligence was established; but this was plainly *obiter.*
Each of the Scottish cases contains *dicta*, especially in the speeches of the Scottish members of the House of Lords, which have been taken by academic writers to indicate that no trustee exemption clause in a Scottish settlement could exonerate a trustee from his own *culpa lata* . But in fact all the cases were merely decisions on the true construction of the particular clauses under consideration, which were in common form at the time. In Knox v Mackinnon, for example, it was unnecessary to consider the exemption clause since the transaction in question was outside its scope. Lord Watson, nevertheless, speaking of "a clause conceived *in these or similar terms",* said that it was the settled law of Scotland that " *such a clause"* was ineffectual to protect a trustee against the consequences of *culpa lata,* or gross negligence on his part, and added that *"clauses of this kind"* did not protect against positive breaches of duty" (my emphasis). In Seton v Dawson the judges who were in the majority spoke to the same effect both of "the protecting clause which occurs in this particular deed" and of "the usual clauses framed for the same object." In Rae v Meek Lord Herschell pointed out that the clause in question was a common one found in many trust deeds and did not come before the court for construction for the first time. He said that its effect had been considered in Seton v Dawson and adopted the passage in Lord Watson's speech in Knox v Mackinnon to which I have already referred. In Carruthers v Carruthers the House was concerned with a standard trustee exemption clause which was to be treated as inserted into the trust deed. Their Lordships held that the terms of such a clause would not exempt trustees from liability for *culpa lata.* Wyman v Paterson was not a case of negligence at all, but of a plain failure to perform a positive obligation. It turned on the true construction of the particular clause under consideration. In Clarke v Clarke's Trustees Lord President Clyde held that the clause in question did not protect the trustees from the consequence of their negligence. He added:
"It is difficult to imagine that any clause of indemnity in a trust settlement could be capable of being construed to mean that the trustees might with impunity neglect to execute their duty as trustees, in other words, that they were licensed to perform their duty carelessly. There is at any rate no such clause in this settlement."

It is not easy to know what to make of this (save that it was *obiter)*. Sir Godfray Le Quesne QC read the passage as directed to the construction of the indemnity clauses common in Scottish settlements at the time. I do not so read it. I tend to think that the Lord President was saying that it was difficult to conceive of a settlor permitting the inclusion of a clause which would have the effect stated. But I agree with Sir Godfray that the Lord President was emphasising the need to exclude liability for negligence by clear and unambiguous words, and was not purporting to exclude the possibility of such a clause on the grounds of public policy.
I agree with the conclusion of the Jersey Court of Appeal that all these cases are concerned with the true construction of the particular clauses under consideration or of similar clauses in standard form in the Nineteenth Century. None of them deals with the much wider form of clause which has become common in the present century, and none of them is authority for the proposition that it is contrary to public policy to exclude liability for gross negligence by an appropriate clause clearly worded to have that effect.
At the same time it must be acknowledged that the view is widely held that these clauses have gone too far, and that trustees who charge for their services and who, as professional men, would not dream of excluding liability for ordinary professional negligence, should not be able to rely on a trustee exemption clause excluding liability for gross negligence. Jersey introduced a law in 1989 which denies effect to a trustee exemption clause which purports to absolve a trustee from liability for his own "fraud, wilful misconduct or gross negligence." The subject is presently under consideration in this country by the Trust Law Committee under the chairmanship of Sir John Vinelott. If clauses such as Clause 15 of the Settlement are to be denied effect, then in my opinion this should be done by Parliament which will have the advantage of wide consultation with interested bodies and the advice of the Trust Law Committee.

Do the pleadings allege fraud ?
The position which I have reached so far, therefore, is that the Respondents are absolved by Clause 15 of the Settlement from liability for all loss or damage to the trust estate except loss or damage caused by their own dishonesty or the dishonesty of their deceased. The question which then arises is: does the Amended Statement of Claim allege dishonesty?
In opening the appeal Counsel for Paula expressly disclaimed any intention to allege dishonesty. He did the same before the Judge. I would not myself hold him to this concession, from which he later resiled, because I think that he may have understood the word "dishonesty" more narrowly than is justified. I take his concession to mean only that it is not intended to allege that any of the trustees acted for their own personal benefit.
The general principle is well known. Fraud must be distinctly alleged and as distinctly proved: Davy v Garrett (1878), 7 Ch.D. 473 at p. 489 *per* Thesiger LJ. It is not necessary to use the word "fraud" or "dishonesty" if the facts which make the conduct complained of fraudulent are pleaded; but if the facts pleaded are consistent with innocence, then it is not open to the Court to find fraud. As Buckley LJ said in Belmont Finance Ltd. v Williams Furniture Ltd. [1979[Ch. 250 at p. 258:
"An allegation of dishonesty must be pleaded clearly and with particularity. That is laid down by the rules: and it is a well-recognised rule of practice. This does not import that the word "fraud" or the word "dishonesty" must be used....The facts alleged may sufficiently demonstrate that dishonesty is allegedly involved, but where the facts are complicated this may not be so clear, and in such a case it is incumbent upon the pleader to make it clear when dishonesty is alleged. If he uses language which is equivocal, rendering it doubtful whether he is in fact relying on the alleged dishonesty of the transaction, this will be fatal; the allegation of its dishonesty will not have been pleaded with sufficient clarity."

That case is authority for the proposition that an allegation that the defendant "knew or ought to have known" is not a clear and unequivocal allegation of actual knowledge and will not support a finding of fraud. It is not treated as making two alternative allegations, ie. an allegation (i) that the defendant actually knew with an alternative allegation (ii) that he ought to have known; but rather a single allegation that he ought to have known (and may even have known - though it is not necessary to allege this).
Before turning to the pleadings I would add one thing more. In order to allege fraud it is not sufficient to sprinkle a pleading with words like "wilfully" and "recklessly" (but not "fraudulently" or "dishonestly"). This may still leave it in doubt whether the words are being used in a technical sense or merely to give colour by way of pejorative emphasis to the complaint.
I shall now consider the detailed allegations in the Amended Statement of Claim.
(1).The appointment of the Company. This is dealt with in Paragraphs 7 and 8. The substance of the complaint is that the appointment was ill-advised and that the trustees ought to have known this. It is not alleged that they had any improper object in making the appointment. Despite the repeated use of the words "in reckless and wilful breach of trust" the complaints to which they relate are complaints of omission. They are consistent with honest

incompetence. If proved, they support a finding of negligence, even of gross negligence; but not of fraud.
(2). The failure to supervise the Company. This is dealt with in Paragraph 9 of the Amended Statement of Claim. The substance of the allegations in Paragraph 9.1(1)-(5) and (8)-(11) is neglect of duty. The complaints are complaints of omission. They are consistent with honest incompetence. At best the charge is one of indolence, at worst of negligence.
Paragraph 9. 1(6) stands on a different footing. It alleges that the trustees "consciously determined" to limit the income of Paula's fund to £15,000 "and/or to allow [the Company] to buy equipment or to build up its capital." This is supported by particulars which refer to a note by one of the trustees (unfortunately now dead) which appears to show that the trustees considered that it was undesirable that Paula's fund should have too much income. I am satisfied that, considered by itself, the subparagraph does not sufficiently allege fraud. It is equivocal. It is unclear whether it is alleged that the trustees had an improper purpose or what that purpose was. In particular, it does not distinctly allege (though it may hint) that the trustees deliberately decided to limit the income of Paula's fund in order to benefit the Company or its shareholders (who were not objects of the trust); nor do I understand how the one was capable of achieving the other, given the nature of the contractual arrangements with the Company. The note referred to in the particulars plainly calls for an explanation, but it is not inconsistent with honesty. I can think of several possible explanations, all innocent and plausible.
In any case Paragraph 9.1(6) cannot support an independent allegation of breach of trust, since the note was apparently never acted on. It was written in connection with a contemplated transaction which in the event did not proceed, and in respect of which it is not alleged that failure to carry the transaction into effect was the fault of the trustees let alone amounted to a breach of trust on their part. At the most, therefore, the subparagraph could provide particulars of the matters relied on in support of an allegation of improper purpose made elsewhere.
Paragraph 9.1(7) complains that the trustees wrongly delegated certain of their powers to the Company. If such delegation was not authorised it constituted a breach of trust. But in the absence of an averment that the trustees delegated their powers in the knowledge that this would result in a misapplication of trust money and that it did so, this is not a charge of fraud.
The several complaints in Paragraph 9.1 (including Paragraph 9.1(6) are summarised in Paragraph 9.11(A) in terms which confirm that they are allegations of neglect of duty only, not allegations of fraud. Paragraphs 9.2 contains the allegation that the trustees were guilty of "reckless and wilful breach of trust" but in its context this is a meaningless incantation. The purpose of Paragraphs 9.2 and 9.2A is to allege that the trustees' failure to supervise the Company or to manage Paula's land properly caused loss to the trust fund.
(3) The value of Paula's land. This is dealt with by Paragraph 11. Paula's land was sold in 1987 for £299,000, ie. £175,000 less than the value assigned to it at the time of the partition. It was sold on the basis of professional advice and to a purchaser at arms-length, and it is not alleged that the sale was at an undervalue. The complaint is only that the trustees failed to inquire into the reasons for the apparent decline in the value of Paula's land, said to be all the more surprising given that the land appropriated to Paula's Mother (which was sold at the same time) had appreciated in value; and failed to investigate the possibility that they might have a cause of action against the valuers who had valued Paula's land at the time of the partition, or against the Company for the negligent management of Paula's land. These are charges of negligence, not fraud; and this is confirmed by the terms in which the complaints are summarised in Paragraph 11.6.
(4) Payment of interest. This is dealt with in Paragraphs 12 and 13. In order to assist Paula's Mother, the trustees agreed to purchase from her the house where Paula lived with her. The agreement was, it appears, subject to contract, and in the event Paula's Mother did not proceed. In the meantime, however, the trustees raised £200,000 from the capital of the Settlement and used it to pay off a legal charge which the bank had over the house, taking a deposit of the title deeds by way of security. In due course the house was sold, and the trustees were paid the sum of £200,000 with simple interest at 8% during the 16 month period of the loan. It is alleged that the transaction constituted a breach of trust, but the only relief claimed in respect of it is in respect of an alleged deficiency of interest. It is not alleged that 8% was below the commercial rate of interest properly chargeable in respect of the loan.
In the absence of Clause 15 the trustees would, I apprehend, be liable to account on the footing of wilful default (which in this context, it will be remembered, means lack of due diligence) for the difference between simple interest at 8% and compound interest at a commercial rate (if higher). Clause 15 exonerates the trustees from any liability to account on the footing of wilful default unless they have been dishonest. It is not alleged that the trustees deliberately undercharged or acted dishonestly in not obtaining a higher rate or compound interest. The pleading is consistent with innocence. It does not amount to a charge of fraud.
(5) The subordination of Paula's interests to those of her Mother. This appears only in Paragraph 9.3. So far as material it reads as follows:

"It is averred that *in the premises* [the trustees] pursued a policy...which failed and neglected to give paramount consideration to the best interests of Paula and instead...pursued a policy *designed* to benefit [Paula's Mother and Grandmother] who were not objects of the trust" (my emphasis).

In my judgment this pleading is embarrassing. It is difficult to know whether it alleges fraud or not. If the word "designed" means "intended" then it does. But the word may mean merely "calculated" (in the sense of "likely"). If it were merely a matter of construing the Paragraph, I would be inclined to think that the word should be taken in its latter signification, so as not to involve a charge of fraud. I would say this for two reasons. First, the words "in the premises" show that Paragraph 9.3 does not contain a new allegation but rather a summary of the effect of the allegations previously made in Paragraph 9; and nothing in the earlier parts of the Paragraph (not even Paragraph 9.6) amounts to a charge of fraud. Secondly, the first part of Paragraph 9.3 alleges only that the trustees pursued a policy which was objectionable because it failed in fact to give paramount consideration to Paula's interests, not that it was their chosen policy not to do so. That is not a charge of fraud. Given the ambiguity in the word "designed", I would give it the meaning which makes the second part of the Paragraph mirror the first. Accordingly I read the Paragraph as alleging nothing more than a failure on the part of the trustees to distinguish properly between Paula's interests and those of her Mother and Grandmother. That is not a charge of fraud.
But it is not just a question of construction. The pleading is clearly equivocal. Without amendment it cannot support a finding of fraud.

Question 1.
I am of opinion that, as at present drawn, the Amended Statement of Claim does not allege dishonesty or any breach of trust for which the trustees are not absolved from liability by Clause 15. Accordingly I would answer Question 1 in the affirmative as the Judge answered it.

Clause 9(a) of the Settlement.

Clause 9(a) of the Settlement reads as follows:
"...the Trustees...shall have power to carry on or join or assist in carrying on or directing any business of farming...with power for that purpose ...to employ or engage... any managers or agents ...and to delegate all or any of the powers vested in them in relation to the business... *And the Trustees shall be free from all responsibility and be fully indemnified out of Paula's fund in respect of any loss arising in relation to the business"* (my emphasis)."

In the absence of the Clause the trustees would have no power to carry on a farming business, whether themselves or through an agent. If they did so, however prudently, they would commit a breach of trust. The Clause confers the necessary powers. The Judge rightly held that the concluding words of the Clause confer upon the trustees a consequential exemption from liability for trading losses incurred in the carrying on of the farming business. It does not exonerate them from liability for imprudently investing in a farming business yielding poor returns or from failing to ensure that the business is properly managed.
Question 2.
Accordingly I would answer Question 2 in the negative as the Judge answered it.
Limitation.
Section 21(1)(a) of the Limitation Act 1980 provides:
"No period of limitation prescribed by this Act shall apply to an action by a beneficiary under a trust, being an action-
(a) in respect of any fraud or fraudulent breach of trust to which the trustee was a party or privy"

Section 21(3) provides:

"Subject to the preceding provisions of this section, an action by beneficiary....in respect of any breach of trust...shall not be brought after the expiration of six years from the date on which the right of action accrued.

"For the purposes of this subsection, the right of action shall not be treated as having accrued to any beneficiary entitled to a future interest in the trust property until the interest fell into possession."

Two questions have been argued. The first is whether Section 21(1)(a) is limited to cases of fraud or fraudulent

breach of trust properly so called, that is to say to cases involving dishonesty. The Judge held that it is. In my judgment he was plainly right for the reasons which he gave. I have explained the meaning of the word fraud in a trustee exemption clause, and there is no reason to ascribe a different meaning to the word where it appears in Section 21(1)(a) of the Limitation Act 1980. Moreover, the meaning of the subsection is not free from authority. Its predecessor (Section 26 of the Limitation Act 1939) was held "to mean what it says" and to be limited to cases where fraud was an ingredient of the wrong: see Beaman v A.R.T.S. [1949] *per* Lord Greene MR at p. 538. The meaning of the words "fraud" and "fraudulent" in Section 21(1)(a) is not distorted by the meaning of the expression "concealed fraud" formerly used in Section of the 1939 Act and which was given a very special meaning but has been replaced in the 1980 Act by the more accurate expression "deliberate concealment". The result is that in the absence of deliberate concealment liability for an honest breach of trust is statute-barred after six years, but liability for a dishonest breach of trust endures without limitation of time.

The second question is whether Paula had a present interest while she was under the age of 25 or whether she had only a future interest which fell into possession when she attained that age. The Judge held that she had merely a future interest. In my judgment he was right. Until Paula attained 25 the trustees held the trust fund upon trust to accumulate the income with power instead to pay it to Paula or to apply it for her benefit. She had no present right to capital or income but only the right to require the trustees to consider from time to time whether to accumulate the income or to exercise their power to pay or apply it for her benefit. That, in my judgment, is not an interest in possession. Paula was, of course, a beneficiary and as such was entitled to see the trust documents. The Respondents submit that this was sufficient to give her an interest in possession within the meaning of the Section, and cite Leedale v Lewis [1982] 3 All ER 808 in support.

In my judgment that case does not assist the Respondents. As Lord Wilberforce pointed out at p. 816

“The word “interest” is one of uncertain meaning and it remains to be decided on the terms of the applicable statute which, or possibly what other, meaning the word may bear.”

The statutory language and context in that case compelled the conclusion that an object of a discretionary trust of capital and income had an interest in settled property. A-G v Heywood (1887), 19 QBD 326 was to similar effect. That decision was approved in Gartside v IRC [1968] AC 553 where, however, a different conclusion was reached because of the different context in which the word “interest” was used.

The meaning of the word must, therefore, be ascertained from the context in which it appears. As the tax cases show, the evident policy of a taxing Act may sometimes make it necessary that an object of a discretionary trust or power should be treated as having an interest and sometimes it may show the contrary. The question thus depends upon identifying the legislative purpose which Section 23 is intended to achieve.

The Respondents submit that the policy to which Section 23 of the Limitation Act 1980 gives effect is that it would be unfair to bar a plaintiff from bringing a claim unless and until he is of full age and entitled to see the trust documents and so has the means of discovering the injury to his beneficial interest. The difficulty with this argument, in my judgment, is that it proves too much. Every beneficiary is entitled to see the trust accounts, whether his interest is in possession or not. The rationale of Section 23 appears to me to be different. It is not that a beneficiary with a future interest has not the means of discovery, but that he should not be compelled to litigate (at considerable personal expense) in respect of an injury to an interest which he may never live to enjoy. Similar reasoning would apply to exclude a person who is merely the object of a discretionary trust or power which may never be exercised in his favour.

Question 3.

Accordingly, I would answer Question 3 also in the negative, as did the Judge.

Costs.

The Judge awarded the Respondents 80% of their costs, depriving them of the remaining 20% because they were unsuccessful on two of the points which had been argued. After hearing further argument, he directed that the Respondents should not be at liberty to reimburse themselves out of the trust fund to the extent of that 20%. He considered that the Respondents were defending themselves and, having taken points which cost money and in respect of which they were unsuccessful, ought to bear those costs themselves.

The Judge recognised that there was long-standing authority to the contrary, but held that it was displaced by the terms of RSC Order 62 Rule 6.2. That Rule entitles a trustee to recoup his costs out of the trust fund and authorises the Court to order otherwise

"only on the ground that he has acted unreasonably or, in the case of a trustee or personal representative has in substance acted for his own benefit rather than for the benefit of the fund."

The Respondents cross-appeal from the Judge's ruling which, they claim, deprives them of their legal rights. They submit that trustees are entitled to a lien over the trust fund for their costs, and that this lien extends to the

costs of litigation, including the costs of defending themselves against a charge of breach of trust: see Turner v Hancock (1882), 20 Ch.D. 303; Re Spurling's Will Trusts [1966] 1 WLR 920. The lien is only lost by misconduct.

But the principle is in my opinion overstated. Trustees are entitled to a lien on the trust fund for the costs of *successfully* defending themselves against an action for breach of trust. That was the position in Re Spurling's Will Trusts as it was in Walters v Woodbridge 7 Ch.D. 504 which it followed. But on what principle can one justify their right to recoup themselves out of the trust fund for the costs of *unsuccessfully* defending themselves against such an action? It offends all sense of justice. The Respondents rely on Turner v Hancock and submit that that was just such a case; but I do not think that it was. The action was an action for an account. On taking the accounts it was found that a sum was due from the trustee and not to him as he contended. It was therefore a case in which the trustee was unsuccessful; but it was not a case in which he was found to be guilty of misconduct or breach of trust. In the course of his judgment Sir George Jessel MR said at p. 304;

"These rights can be lost or curtailed by such inequitable conduct on the part of a mortgagee or trustee as may amount to a violation or culpable neglect of his duty under the contract...It is not the course of the court in modern times to discourage persons from becoming trustees by inflicting costs upon them if they have done their duty, or even if they have committed an innocent breach of trust."

As Ungoed-Thomas J pointed out in Re Spurling's Will Trusts, it is not enough to deprive trustees of their right to recoup their costs out of the trust fund that the claim is a claim to recover money from them for the benefit of the trust. If the trustees succeed, then the claim was not well founded, and they cannot be denied their right of recoupment. I would add that even if the claim succeeds, yet they may not have so conducted themselves as to lose their right of recoupment.

In the present case the Judge deprived the Respondents of 20% of their costs because they had put forward arguments on which they had been unsuccessful. That was a proper exercise of his discretion. But he also deprived them of their right to recoup themselves out of the trust fund to the extent of that 20% on the ground that the claim was a hostile claim against them personally for breach of trust. In my opinion that was not a sufficient ground for denying them their contractual rights. As things stood at the conclusion of the Judge's judgment, he had held that the Respondents were absolved by Clause 15 from liability in respect of all the claims for breach of trust pleaded against them, with the result that the greater part of the Action was bound to fail (there is a claim to an account in respect of a separate matter which is not particularly contentious and which would survive). Accordingly, unless the pleadings were amended, the Action would be dismissed without any inquiry into the trustees' conduct. This would not provide any basis for depriving the Respondents of their rights. Accordingly, I would set aside this part of the Judge's order.

Amendment of the pleadings.

At the conclusion of Belmont Finance Ltd. v Williams Furniture Ltd.(*supra*) this Court granted the unsuccessful respondent leave to amend the pleadings. No such application is before us. Nevertheless I think that Paula should be given the opportunity to re-amend the Amended Statement of Claim if so advised. I express no view on whether there is material which would justify Counsel in advising such a course; and I would not wish to encourage it. They will no doubt bear in mind that at the material time the trustees of the settlement consisted of one professional man and two distant relatives; and that a charge of fraud against independent professional trustees is, in the absence of some financial or other incentive, inherently implausible.

The possibility of amendment affects the order for costs which ought to be substituted for the order which the Judge made. In my judgment, the Respondents should have the right to recoup themselves out of the trust fund but only if and when the Action against them is discontinued or dismissed. If the Action is repleaded and succeeds against any of them, then the unsuccessful Respondents should not recoup themselves out of the trust fund without the leave of the Court given after trial of the Action.

Conclusion.

It is our view that Paule should be given the maximum opportunity to see the trusts documents and to investigate the manner in which the trustees managed the affairs of the trust. We would wish to hear Counsel as to the terms of any order which we should make in this respect, in particular as to the appropriate tribunal to entertain such an application (whether the Master or the Judge in Chambers), the imposition of any time limits, and whether, prior to such application, Paula should have the right to have the trust documents produced to her: see Re Londonderry Settlement [1964] Ch. 594.

Subject thereto, the appeal and cross-appeal will be dismissed. The Order of the Judge refusing the Respondents liberty to recoup their costs out of the trust fund will be set aside and an Order in the terms indicated above substituted.

LORD JUSTICE HUTCHISON: I agree.

LORD JUSTICE HIRST: I also agree.

Orders: appeal and cross appeal dismissed; respondents to receive 80% of costs in the Court of Appeal; order made under section 18 of the Legal Aid Act; appellant's contribution assessed at nil

- - - - - - -
