*567 Barclays Bank Ltd. Appellants v Quistclose Investments Ltd. Respondents

House of Lords

31 October 1968

[1968] 3 W.L.R. 1097

[1970] A.C. 567

Lord Reid, Lord Morris of Borth-Y-Gest, Lord Guest, Lord Pearce and Lord Wilberforce

1968 July 23, 24, 25, 29; Oct. 31

[On Appeal from Quistclose Investments Ltd. v. Rolls Razor Ltd.]

Company—Winding up—Voluntary liquidation—Loan to company for specific purpose of paying dividend—Money paid into separate account at bank—Company's liquidation before payment of dividend—Bank's claim to set off—Whether money held on trust for lender.

Banking—Multiple accounts—Company's share dividend account—payment in of sum borrowed specifically to pay dividend Bank's knowledge of condition—Company in liquidation before dividend paid—Whether sum held on trust for lender.

Trusts—Contract subject to—Bank—Loan for sole purpose of paying dividend—Non—payment of dividend—Trust attaching to loan—Lender's right to repayment—Co—existence of rights in contract and of cestui que trust in equity.

R. Ltd., who were in serious financial difficulties, having an overdraft with their bank, the appellants, of some £484,000 against a permitted limit of £250,000, commenced negotiations with X, a financier, with a view to obtaining a loan of £1,000,000, and it was suggested that such a loan might be made on condition that R. Ltd. found a sum of £209,719 8s. 6d. which was needed to meet an ordinary share dividend which R. Ltd. had declared on July 2, 1964. R. Ltd. succeeded in obtaining a loan of that sum from the respondents. The loan was made on the agreed condition that it would be used to pay the dividend. The respondents' cheque was paid into a separate account opened specially for the purpose with the appellants, who knew that the money was borrowed and who agreed with R. Ltd. that the account would only be used for the purpose of paying the dividend. Before the dividend had been paid, however, R. Ltd. went into voluntary liquidation. The respondents brought an action against R. Ltd. and the appellants claiming that the money had been held by R. Ltd. on trust to pay the dividend; that, that trust having failed, it was held on a resulting trust for the respondents, and that the appellants had had notice of the trusts and were, accordingly, constructive trustees of the money for the respondents.

Held:

(1) that arrangements of this character for the payment of a person's creditors by a third person gave rise to a relationship of a fiduciary character or trust in favour, as a primary trust, of the creditors, and, secondly, if the primary trust failed, of the third person.

Toovey v. Milne (1819) 2 B. & A. 683 and Edwards v. Glyn (1859) 2 E. & E. 29 applied.

Moseley v. Cressey's Co. (1865) L.R. 1 Eq. 405; Stewart v. Austin (1866) L.R. 3 Eq. 299 and *In re Nanwa Gold Mines Ltd. [1955] 1 W.L.R. 1080; [1955] 3 All E.R. 219* distinguished.

(2) That the fact that the transaction was one of loan giving rise to a legal action of debt did not exclude the implication of a trust enforceable in equity. That there was no difficulty in recognising the co-existence in one transaction of ****568*** legal and equitable rights and remedies; when the money was advanced, the lender acquired an equitable right to see that it was applied for the primary designated purpose. When the purpose had been carried out (that is, the debt paid) the lender had this remedy against the borrower in debt; if the primary purpose could not be carried out, the question arose if a secondary purpose (that is, repayment to the lender) had been agreed, expressly or by implication; if it had, the remedies of equity might be invoked to give effect to it, if it had not (and the money was intended to fall within the general fund of the debtor's assets) then there was the appropriate remedy of a loan. Here, there was a clear intention to create a secondary trust for the benefit of the lender, to arise if the primary trust, to pay the dividend, could not be carried out.

In re Rogers, Ex parte Holland and Hannen (1891) 8 Morr. 243 applied.

(3) That the appellants had, on the facts, accepted the money with knowledge of the circumstances which made it, in law, trust money, and could not retain it against the respondents.

Per Lord Reid: I am by no means satisfied that this House would be precluded from holding, in such circumstances as exist in this case, that notice of the trust received by the bank after they had received the money could be effective (post, p. 578B).

Decision of the Court of Appeal [1968] Ch. 540; [1968] 2 W.L.R. 478; [1968] 1 All E.R. 613, C.A. affirmed.

The following cases are referred to in Lord Wilberforce's opinion:

Drucker (No. 1). In re [1902] 2 K.B. 55; *[1902] 2 K.B. 237, C.A.*.
Edwards v. Glyn (1859) 2 E. &; E. 29.
Hooley, In re, Ex parte Trustee [1915] H.B.R. 181.
Moseley v. Cressey's Co. (1865) L.R. 1 Eq. 405.
Nanwa Gold Mines Ltd., In re [1955] 1 W.L.R. 1080; [1955] 3 All E. R. 219.
Rogers, In re, Ex parte Holland and Hannen (1891) 8 Morr. 243, C.A..
Stewart v. Austin (1866) L.R. 3 Eq. 299.
Toovey v. Milne (1819) 2 B. &; A. 683.

The following additional cases were cited in argument:

Clark v. Ulster Bank Ltd. [1950] N.I. 132.
Commissioner for Stamp Duties of New South Wales v. Perpetual Trustee Co. Ltd. [1943] A.C. 425; [1943] 1 All E.R. 525, P.C..
Foley v. Hill (1848) 2 H.L.Cas. 28, H.L.(E.).
Foxton v. Manchester & Liverpool District Banking Co. (1881) 44 L.T. 406.
Lister & Co. v. Stubbs (1890) 45 Ch.D. 1, C.A..
Moore v. Barthrop (1822) 1 B. &; C. 5.
Rolls Razor Ltd. v. Cox [1967] 1 Q.B. 552; [1967] 2 W.L.R. 241; [1967] 1 All E.R. 397, C.A..
Union Bank of Australia Ltd. v. Murray-Aynsley [1898] A.C. 693, P.C..
Vautin, In re [1900] 2 Q.B. 325.
Watson, In re, Ex parte Schipper (1912) 107 L.T. 783, C.A..

APPEALfrom the Court of Appeal.

This was an appeal by the appellants, Barclays Bank Ltd., from the judgments and order of the Court of Appeal (Harman, Russell and Sachs ***569*** L.JJ.) dated December 15, 1967, reversing and discharging the judgment and order of Plowman J., dated February 17, 1967, in an action brought in the matter of the trusts of a sum of £209,719 8s. 6d. paid by the respondents, Quistclose Investments Ltd., to the credit of a special dividend account in the name of Rolls Razor Ltd. with the appellants in which the respondents were plaintiffs and the defendants were Rolls Razor Ltd. ("Rolls Razor") a company in voluntary liquidation, the appellants, and by subsequent amendment) Investors Inter-Continental Fund Ltd.

In the spring of 1964, Rolls Razor were in serious financial difficulties. They had an overdraft with the appellants amounting to some £484,000, against a permitted limit of £250,000, and the appellants had informed them that they were not prepared to increase that overdraft, or, unless there were an amendment in Rolls Razor's position by the end of June, to continue to do business with them. Rolls Razor commenced negotiations with a well-known financier with a view to obtaining a loan of £1,000,000, and it was suggested that such a loan might be forthcoming provided that Rolls Razor found a sum of £209,719 8&S 6d. which was required to meet an ordinary share dividend which Rolls Razor had declared on July 2, 1964. Rolls Razor succeeded in obtaining a loan of that sum from the respondents. The loan was made on the condition "that it is used to pay the forthcoming dividend due on July 24 next," and the appellants agreed to open a special account (No. 4 ordinary dividend account) into which the money to be provided was to be paid. A letter from Rolls Razor to the bank enclosing the respondents' cheque for £209,719 8s. 6d. showed that it was agreed between Rolls Razor and the appellants that the No. 4 account would "only be used to meet the dividend due on July 24, 1964." The cheque was paid into the No. 4 account and cleared. On August 27, the dividend not having been paid, Rolls Razor went into voluntary liquidation. Quistclose brought an action against Rolls Razor and the appellants claiming that the money had been held by Rolls Razor on trust to pay the dividend; that, that trust having failed, it was held on a resulting trust for the respondents; and that the appellants had had notice of the trusts and were, accordingly, constructive trustees of the money for the respondents. Plowman J. held that, assuming that the money had been received by Rolls Razor subject to a fiduciary obligation to pay the dividend, it did not follow that, when that purpose had failed, it was thereafter held on a resulting trust for the respondents; that there was no reason to impute an intention that the money should be

repayable pursuant to some equitable obligation additional to the legal one; and that the further question whether the appellants had had notice of the trust did not, therefore, arise. He dismissed the action.

On appeal by the respondents, the Court of Appeal reversed the decision of Plowman J. and held that in the circumstances the respondents were entitled to the sum claimed.

The facts are more fully stated in Lord Wilberforce's opinion.

E. I. Goulding Q.C. and *Allan Heyman* for the appellants.

Two questions arise for determination: (1) If a lender lends a sum of money to a borrower to be used by the borrower for a particular purpose, being a purpose of the borrower's, what right, if any, in equity, has the lender in addition to his legal rights as a creditor? (2) Notice. There are ****570*** three possibilities: (a) If the House decide that the sum in question is not trust money then the question of notice is irrelevant. (b) If there was a trust and it is held that a trust arises in favour of a lender merely because the loan is made for a particular purpose of the borrower then it is conceded that the appellants fail because the bank knew that the money was provided by someone for the purpose of paying a dividend. (c) If it is held that as between borrower and lender the money is trust money, but only because it was a condition of the loan that it should be used to pay the dividend then the appellants should succeed on the question of notice for it was never proved that a condition was attached to the loan.

(1) Equity distinguishes clearly between a debtor who owes money to a creditor and a person, whether trustee or agent, who holds some other person's money for that person's I benefit. Where equity will make one person account to another it may be because the essential relationship is a debtor and creditor relationship or a trustee-cestui que trust relationship. It is vital to make the distinction because the money may come into the hands of a third party. *Foley v. Hill (1848) 2 H.L.Cas. 28* emphasises the distinction.

Lister & Co. v. Stubbs (1890) 45 Ch.D. 1illustrates the difficulty of drawing the line between the two categories in certain circumstances. The observations of Lindley L.J., at pp. 14, 15, are adopted. The obligation of Rolls Razor to repay the respondents was not in the nature of a trust; it was a loan. It was plain to Rolls Razor and to the respondents that the loan could not be repaid before July 24, 1964. It was also plain to the respondents, at any rate, that if the dividend was not paid on that date the loan was immediately repayable on demand.

The vital distinction between the two categories is that in the trusteecestui que trust relationship the property belongs to the beneficiary. The type of case which the House has to consider is that where A lends money to B on terms that it is to be used to pay an existing creditor, C. It is emphasised that a proper analysis of the facts here shows that the relationship between Quistclose and Rolls Razor was in the field of contract and not of property. It was not the intention to make Rolls Razor an agent or servant for discharging a liability of Quistclose. Further, it is inconsistent with the conduct of the parties and the documents to state that the property in the money was to remain in Quistclose.

As to the bankruptcy cases, they fall into two categories: (i) where the debtor, perceiving that his financial position is hopeless, after an act of bankruptcy returns the money to A. (ii) Where A has not only provided money but the purpose for which it has been provided has

been carried out by payment to C but after an act of bankruptcy has been committed. The facts of the present case form a third category on which there is no reported authority. In the first category the trustee in bankruptcy seeks to recover the money from A and leave him to prove in the bankruptcy along with the general body of creditors. In the second category the trustee in bankruptcy seeks to recover the money from C.

Toovey v. Milne (1819) 2 B. & A. 683is an example of the first category. It is wrong in so far as it held that there was a specific trust but the decision is maintainable in bankruptcy law if the money paid by A to pay an existing creditor, C, was repaid to A before the receiver took the assets or C was ***571** paid. In those circumstances although the property passed to the bankrupt the ordinary rule of relation back does not apply to a creditor who lends money for the specific purpose of satisfying the debtor's creditors. Two other examples of the first category are Moore v. Barthrop (1822) 1 B. & C. 5 and Edwards v. Glyn (1859) 2 E. & E. 29. These cases were decided in the common law courts.

The following cases were decided under the bankruptcy jurisdiction of the High Court: In re Rogers, Ex parte Holland & Hannen (1891) 8 Morr. 243 is the first example of the second category. The breadth of the reasoning in this case is too wide. Further examples of this second category are *In re Drucker (No. 1) [1902] 2 K.B. 55*, 237; In re Watson, Ex parte Schipper (1912) 107 L.T. 783and In re Hooley, Ex parte Trustee [1915] H.B.R. 181.

In the appellants' submission the bankruptcy cases are distinguishable. They do not cover the facts of the present case and should not be extended. They are an anomaly and an exception to the proposition that the concept of a loan cannot coexist with that of a trust. The present case comes within the principle established by Moseley v. Cressey's Co. (1865) L.R. 1 Eq. 405; Stewart v. Austin (1866) L.R. 3 Eq. 299and *In re Nanwa Gold Mines Ltd. [1955] 1 W.L.R. 1080*, namely, that if A pays money to B to pay to C for a particular purpose the money in the hands of B is not impressed with a trust. The appellants support the judgment of Plowman J. *[1967] Ch. 910*.

As to the decision of the Court of Appeal and the judgment of Harman L.J. [1968] Ch. 540, 548 et seq., the money must have become the property of Rolls Razor, for it is said that the liquidation of the company made it illegal to pay the dividend; this shows that the money must have been the company's, that is, Rolls Razor's money. Reliance is placed on *Rolls Razor Ltd. v. Cox [1967] 1 Q.B. 552*.

The fact that this money, if retained, is a "windfall" for the bank, as Harman and Russell L.JJ. put it, cannot be a guide in coming to a correct conclusion on the law on this question. It would not have been surprising that if this sum had been paid into a bank to which Rolls Razor was not indebted that the liquidator should prevail over the claim of Quistclose in circumstances where Rolls Razor were in grave financial difficulties and yet were being loaned money to pay a very large dividend on the previous year's trading profits.

As to the judgment of Sachs L.J. (at p. 568C), the appellants do not suggest that equitable remedies cannot exist alongside common law rights, but the existence of equitable remedies per se does not impute the concept of a trust.

(2)Notice Where a bank receives funds from a company to be placed in a separate account, that fact by itself does not put the bank on inquiry concerning the rights of third parties: see *Union Bank of Australia v. Murray-Aynsley [1898] A.C. 693*. For a helpful review of the authorities on the subject of notice: see Clark v. Ulster Bank Ltd. [1950] N.I.

132.

The House is not concerned here with any abstract duty on the part of a banker to question the purpose for which an account is opened but merely with what the appellant bank knew at the date when the cheque was received ***572*** and with what it had agreed to do. In these circumstances the question of notice is in a narrow compass.

If it was enough to know that the money paid to Rolls Razor was for the purpose of paying a dividend the appellants would fail since it would appear from answer to an interrogatory administered to the bank in the course of the proceedings that the bank did know that the money was paid for the payment of dividends. If that be sufficient to impress the money with a trust then there was notice for present purposes.

The Court of Appeal, however, held that a trust arose because it was a condition of the loan that it should only be used to pay the dividend declared on July 2, 1964. That the bank had notice of such a condition is inferred from a number of circumstances of which the bank admitted having knowledge. But that is not a legitimate inference to draw when it is seen that Quistclose obtained leave from the court to administer an interrogatory to the bank in which the express question was asked of the manager of its city branch and when the respondents elect not to use the answer given, which was, "I do not know."

Generally, the strength of the case against the appellants is based on a group of bankruptcy cases which are little known to the general body of practitioners and are not mentioned in the books on trusts. It is pertinent to consider how far they go. Suppose a farmer approaches his bank manager and requests an overdraft of £1,000 in order to purchase a tractor. The request is granted and subsequently the farmer goes bankrupt and it is discovered that the money was used to buy a motor car. In these circumstances the bank could take the car and have a considerable advantage over the general body of creditors. Now let it be supposed that the overdraft is refused but the next day the farmer returns to the bank and informs the manager that he proposes to pay in a cheque to pay for the tractor as his brother will lend him the money for that purpose. Is the bank in those circumstances put on inquiry and under a duty to a third party? This is the wider issue raised by the appeal.

[Reference was also made to In re Vautin [1900] 2 Q.B. 325.]

Heyman following. It is pertinent to consider the consequences that would arise in company law if the argument for the respondents were to prevail. Under section 95 of the Companies Act, 1948, every charge has to be registered to be valid against creditors or liquidators. If the respondents be right there would be a gap in the protection given to innocent creditors. It would also give rise to the danger of fraud. An asset would be entered in the company's accounts which would appear to be unencumbered and therefore misleading to those persons willing to lend the company money on the strength of the company's assets.

W. A. Bagnall Q.C. and *Michael Sherrard Q.C.* for the respondents.

There are two distinct questions for determination: (1) Was the £209,000 ever the beneficial property of the company (Rolls Razor)? In particular, was it the beneficial property of the company when the bank merged the accounts? (2) If the money came to the company as free money it was free to be used for the payment of creditors generally,

but if it is money impressed with a trust then the bank is bound by the trust unless it can show that it had no notice of the trust and that it was unaware that the sum in question did not form part of the free assets of the company.

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The ratio decidendi of the bankruptcy cases is that money paid by A to B, a debtor, for the specific purpose of paying it over to C, a creditor, never forms part of B's general assets for him to use as he pleases.

In all the bankruptcy cases that have been mentioned, save possibly Edwards v. Glyn, 2 E. & E. 29, three persons were involved: A the lender B the debtor who becomes the trustee and C the creditors, the payees of the money. If these cases are correct then there can only be one answer to the first question.

Suppose that before the bank had coalesced the accounts that the liquidator had paid the money back to Quistclose, this would have been precisely the same situation as arose in In re Rogers, Ex parte Holland & Hannen, 8 Morr. 243 and the decision must have been the same. It follows that the present appeal entails consideration of the question whether this long line of bankruptcy cases which commences with Toovey v. Milne 2 B. & A. 683 and ends with In re Hooley, Ex parte Trustee [1915] H.B.R. 181 was correctly decided.

It is fundamental to the present case to consider the interrelation between trust and contract. The whole of the appellants' case is based on a false premise. The appellants contend that a trust and a loan cannot co-exist. This is wholly fallacious on principle; a trust is the creature of equity and equity acts on the conscience. The obligation to repay is the characteristic of the legal ownership and not of the beneficial ownership.

There are three possibilities to be considered: (i) A contract but no trust. A pays £1,000 to an insurance company, the company agreeing to pay A or X £100 annuity for life. (ii) A trust but no contract. A trust created by will or a trust where A simply declares himself a trustee for B. (iii) Contract and trust. In every case of an inter vivace trust there exists both a contract and a trust. An example is where A pays £5,000 to B on the terms that B shall use it to pay the school fees of A's son. The detriment to A is the parting with the money in exchange for B's promise. There are two defects in the enforcement at common law of such an arrangement: (a) If B failed to pay, A could possibly only receive nominal damages. (b) A's son is not a party and could not sue.

True in these cases the contract is never mentioned for the simple reason that over the years it has been discovered that the remedies available in equity are so much more efficacious.

If A agrees to sell Blackacre to B for £10,000, that is a contract at common law, but it is also a transaction of which B could obtain specific performance in equity because in equity A is deemed to be a trustee for B of Black acre.

The following example illustrates the fallacy in the appellants' argument: H and W are about to marry and the question of a marriage settlement arises. H's father announces that he as settler will settle £50,000 on H and W, T being the trustee of the settlement. Subsequently £50,000 is paid to T on the trusts of the settlement. W's father has £50,000 which he is prepared to lend interest-free on the terms of the marriage settlement. Before the marriage is celebrated T has the £100,000 in his hands. Then the following events

occur: H dies before the wedding day and a week later T goes bankrupt. The £50,000 paid by H's father returns to him by way of a resulting trust. Is it to be said that the £50,000 paid by W's father is to remain in ***574** T's hands in order to satisfy his creditors in the liquidation simply because there was merely a promise by T to repay the loan in certain circumstances? In the appellants' submission there cannot be any difference in law between these two sums of £50,000. If that be right then that is an end of this case because it is plain that T has no beneficial interest in this money at all. Equally, here Rolls Razor had no beneficial interest in the £209,000; it was paid to the company for a specific purpose.

In general, the existence of a contractual obligation does not exclude the existence of a trust. The bankruptcy cases were rightly decided. The question whether rights lie in trust or in contract is unimportant save in three cases: (a) A third party can enforce a trust but not a covenant or contract; (b) where the trustee is insolvent, because if the right lies only in contract, all that arises is a dividend; (c) if the property has come into the hands of a third party. If it lies only in contract it will not bind a third party, but if there is a trust a third party will be bound by its terms.

The failure of the trust purpose creates a resulting trust in favour of the provider of the fund. Before the Executors Act, 1830, in relation to personal property if a man made a will and appointed executors but did not dispose of the whole of his personal estate the undisposed portion went to his executors at law, but if the testator had created his executors also *trustees* of the will they could not take in equity. Once a trust is created the trustee can never assert beneficial ownership of the trust property.

When a trust is created the equitable ownership is parted with only to the extent necessary to carry out the trust. In equity, Quistclose parted with this money only to the extent necessary to pay the dividend if it was paid. Once a situation arises where the dividend ceases to be payable the money is repayable to Quistclose.

Snell's Equity, 26th ed. (1966), p. 100, under the heading "contracts," is adopted as part of the argument. [Reference was made to Maitland's Equity, 2nd ed. (1936), p. 75.]

This transaction made Rolls Razor a trustee to make a dividend and upon this becoming an impossibility the money results to Quistclose: see *Commissioner for Stamp Duties, New South Wales v. Perpetual Trustee Co. [1943] A.C. 425*, 441. Reliance is also placed on the judgment of Hamilton L.J. in In re Watson, Ex parte Schipper, 107 L.T. 783, 784, which is applicable here. It is unlikely that Hamilton L.J., who, as Lord Sumner, delivered an opinion in *Sinclair v. Brougham [1914] A.C. 398*, would have said that the doctrine of unjust enrichment encroached upon the principle to be found in the bankruptcy cases. It would be against conscience to allow the bank to retain the sum in question here. It is plain from the documents that the money was only to be retained by Rolls Razor to pay the dividend and not to pay the shareholders a sum of money equal to the dividend in any event, for this would mean that the £209,000 was an outright gift from Quistclose and would be wholly inconsistent with the whole arrangement.

As regards the company cases, they differ from the present in that in those cases there was no *primary trust* to pay another person. The facts there were that there were payments by shareholders to a company as a consideration for the issue of shares and, because there was no primary trust that failed, the doctrine of a resulting trust could never apply and

therefore ***575*** the payer could only claim an equitable title if he could show that there was an express trust for him. Those cases, therefore, were concerned with whether there was an express trust created.

In Moseley v. Cressey's Co., L.R. 1 Eq. 405; Stewart v. Austin, L.R. 3 Eq. 299 and *In re Nanwa Gold Mines Ltd. [1955] 1 W.L.R. 1080* the word "purpose" is used in quite a different sense from its use here, for the purpose there is simply the adding of money to the general assets of the company in question in consideration for the issue of shares. The task of the plaintiffs there was to establish a trust in favour of the depositors. In the present case the respondents have established a fiduciary obligation to pay the money away as dividend. The whole purpose of the company cases was for the money to form part of the general assets of the company. The whole purpose here was that it was not to form part of Rolls Razor's general assets.

Plowman J. was wrong in holding that the company cases were relevant in deciding the present case.

Notice

The respondents do not dispute the appellants' submissions on the law on this issue. The question is: did the bank when it received the cheque for £209,000 know that it represented moneys which were free assets?

In the bank cases, two questions arise: (i) Is the money trust money? (ii) Has the bank's dealings with the money made it a party to a breach of trust?

Foxton v. Manchester & Liverpool District Banking Co. (1881) 44 L.T. 406 establishes that once it is shown that the bank is aware that money is affected by a trust it is immaterial that the bank does not know the detailed terms thereof. It is sufficient to make the bank liable if it knew that it is a fund held in a fiduciary capacity and that a payment made by the trustees is inconsistent with their holding the fund in a fiduciary capacity. The same test was applied in *Union Bank of Australia v. Murray-Aynsley [1898] A.C. 693*.

It cannot be necessary for the bank to know who the beneficial owners are for the trustees themselves might not know, for example, where that question depends upon a contingency.

The bank having failed to tender any oral evidence on its behalf the question is: What inferences would a reasonable banker draw from the facts which are contained in the documents produced in evidence in this case? In the respondents' submission Mr. Parker, the manager of the appellants' city branch, knew that this money was provided by a third party for the specific purpose of paying the dividend due on July 24, 1964, and for no other purpose. The whole of the facts here are quite inconsistent with any contention that the manager thought that this money was freely available to pay off the overdraft.

The act of the bank in making this money available in a separate account is only conceivable on the documents with it being used for the dividend, for the bank would never have allowed any free assets of the company to be used for that purpose in view of the size of Rolls Razor's overdraft.

Reliance is placed on the decision of the Court of Appeal on this question.

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As to the argument based on the non-use of an answer to an interrogatory, the procedure is, as it was never used the interrogatory is deemed never to have been asked.

In conclusion, the argument for the respondents may be summarised as follows: (a) It is a fundamental principle of equity that if A pays money to B upon terms (accepted by B) that the money is to be applied for a specific purpose B is subject to an equitable obligation to apply the monies only for that purpose and cannot himself assert a beneficial title thereto and the money is subject to a trust of which B is the trustee. (b) If the specified purpose is for the benefit of identified persons or for charity (subject to exceptions not here material) the court in the exercise of its equitable jurisdiction in the execution of trusts will enforce the equitable obligation of B. (c) If the specified purpose is or becomes incapable of being achieved (wholly or in part) the money or so much thereof as has not been or cannot be applied for the specified purpose is held on trust - sometimes for convenience called a resulting trust - for A. Equity treats A as having disposed of his beneficial interest in the money only to the extent that the specified purpose is capable of being achieved. (d) The equitable obligation and trust aforementioned are binding on and enforceable against a third party who receives the money with the knowledge that it is subject to a trust. Such a third party cannot rely on the equitable defence of "bona fide purchaser for value without notice." (e) The foregoing principles apply even if the payment of the money by A to B is by way of loan; the contractual obligation of B to repay the loan does not preclude the application of equitable principles. In particular, where money is lent by A to B for the specific purpose of its being applied in the payment of a debt or debts of B, the money is held by B upon trust to apply it in payment of the debt or debts (if and so far as that purpose is capable of achievement) and subject thereto on trust for A. The money never becomes in equity the property of B beneficially. In support of this proposition the respondents rely on the following cases: Toovey v. Milne, 2 B. & A. 683; Edwards v. Glyn, 2 E. & E. 29; In re Rogers, Ex parte Holland & Hannen, 8 Morr. 243; In re Vautin [1900] 2 Q.B. 325; *In re Drucker (No. 1) [1902] 2 K.B. 55*, 237; In re Hooley, Ex parte Trustee [1915] H.B.R. 181. (f) The declaration of the dividend by the company in general meeting created a debt due from the company to the ordinary shareholders. The sum in question was paid by the respondents to the company upon the terms (accepted by the company) that it was to be applied only in the payment of the dividend and accordingly was held by the company upon trust to be so applied and never became in equity the property of the company beneficially. By virtue of section 212 (1) (g) of the Companies Act, 1948, upon the commencement of the voluntary winding up of the company the dividend could not be paid, the specified purpose ceased to be capable of achievement and this sum was thereupon held in trust for the respondents. (g) In the absence or any evidence from Mr. Parker or any other person on behalf of the appellants and upon the primary facts and the relevant documents it must be inferred, on a balance of probabilities, that the appellants knew, when they received this sum, that it was subject to a trust and was not the property of the company beneficially.

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E. I. Goulding Q.C. in reply. The first principles which were developed by the appellants were textbook principles and these are not disputed.

Reliance was placed on *Snells Equity,* 26th ed. p. 100, but the statement at the very foot of that page and the top of p. 101 that:

> "On the other hand, although the common law courts persistently refused to recognise as actionable any breach of trust, there appears to be no reason why a trustee's breach of a trust which he has agreed with the settler to undertake should not be treated as a breach of contract remediable by an action for damages brought by the settler,"

is not supported there by any citation of authority. But whether there be authority or not it is of the first importance to recognise that it differs entirely from the beneficiaries' suit in equity. The party would be different. The settler would sue at common law for breach of contract and receive nominal damages of 40 shillings. The courts of equity would not execute the settlement at the suit of the settler. It is essential to recognise the difference between the two remedies.

As to the illustration of the marriage settlement and the two settlers, the appellants have there confused two concepts which have different results in law. W's father in that example could either have created a revocable trust and would then be entitled on revocation to the fund representing the cash handed over. He would not be a creditor of T. Alternatively, W's father could have lent £50,000 to T on terms that it was a loan. T could then declare himself a trustee of it on the terms of the marriage settlement but reserving to himself a right of revocation in case W's father should demand the return of the £50,000.

The inconsistency of the attitude taken up by the respondents appears from a more general part of their argument. If the money paid over by Quistclose was to go directly to the shareholders without any interest in the sum at any stage vesting in Rolls Razor then the proposed dividend cannot truly be called a "dividend" for a dividend is paid out of *the assets* of the *company,* that is, here, Rolls Razor. A company can only pay a dividend out of borrowed money if it forms part of its assets.

The object of what was done here was to discharge the debts of Rolls Razor in order to maintain its credit.

Notice

As to Foxton v. Manchester & Liverpool District Banking Co., 44 L.T. 406, the appellants concede that if the facts be that the bank knew that this money was trust money the fact that the bank did not know who was the beneficiary of the money would not avail the appellants.

The true test applicable here is: did the bank know that the money was not part of the assets of Rolls Razor? The bank did not know that the £209,000 was not the money of Rolls Razor. The only intended use of the money of which the bank was aware was that it was to he used for the payment of a dividend and that was a use of the money essentially appropriate to the use by Rolls Razor of its own assets.

As regards the interrogatories, there is no reported authority on this question. But in the appellants' submission a court is entitled to take ***578*** cognisance of the fact that a certain interrogatory was asked and answered even if the answer is not utilised by the party administering the interrogatory.

Their Lordships took time for consideration.

October 31, 1968.

LORD REID.

My Lords, I agree with the speech of my noble and learned friend, Lord Wilberforce. I would only add that I am by no means satisfied that this House would be precluded from holding, in such circumstances as exist in this case, that notice of the trust received by the bank after they had received the money could be effective.

I would dismiss this appeal.

LORD MORRIS OF BORTH-Y-GEST.

My Lords, I am in agreement with the speech of my noble and learned friend, Lord Wilberforce, which I have had the advantage of reading.

I would dismiss the appeal.

LORD GUEST.

My Lords, I have had the advantage of reading the opinion of my noble and learned friend, Lord Wilberforce. I agree with it and would dismiss the appeal.

LORD PEARCE.

My Lords, I have had the advantage of reading the opinion of my noble and learned friend, Lord Wilberforce. I entirely agree with it. Accordingly, I would dismiss the appeal.

LORD WILBERFORCE.

My Lords, the events with which the present appeal is concerned took place in the final weeks preceding the collapse of Rolls Razor Ltd., an enterprise of which the moving spirit was Mr. John Bloom. The company's audited accounts for the year 1963 showed a considerable trading profit: an interim dividend of 80 per cent. had been paid, and the figures admitted of the payment of a substantial final dividend. On May 14, 1964, the directors, at a board meeting, agreed to recommend a final payment of 120 per cent. But the company had no liquid resources to enable it to pay this dividend, which required a net sum, after deduction of tax, of £209,719 8s. 6d. On June 4, 1964, its overdraft with the appellant bank was £485,000, against a limit of £250,000, and on that day the bank by letter to Mr. Leslie Goldbart, one of the directors, required this situation to be rectified, and stated that it would be unable to help in the payment of the final dividend unless this was made within the overdraft limit of £250,000.

The Annual General Meeting of Rolls Razor Ltd. was held on July 2, 1964, and payment of the 120 per cent. dividend was approved. No date was fixed by the approving resolution, but the directors contemplated that payment would be made on July 24. Approval of the dividend made the company a debtor in respect of the net amount to its shareholders. Provision of the sum required to pay it, as also of finance to enable the company to continue trading, was the subject of negotiations by Mr. Bloom during the early part of July. He succeeded in obtaining the money needed to pay the dividend from the respondent company, which he owned or controlled. At a board meeting of the latter held on July 15, 1964, it was ***579*** resolved that a loan of £209,719 8s. 6d. be made to Rolls Razor Ltd. "for the purpose of that company paying the final dividend due on July 24 next." On the

same day, a cheque for that sum was drawn by the respondent company in favour of Rolls Razor Ltd. Rolls Razor Ltd. sent this cheque to the appellant bank's city branch office together with a covering letter on the notepaper of Rolls Razor Ltd., also dated July 15, 1964, signed by Mr. Goldbart and addressed to Mr. G. H. Parker, a joint manager of that branch, in the following terms:-

> "Dear Mr. Parker,
>
> Confirming our telephone conversation of today's date, will you please open a no. 4 ordinary dividend share account.
>
> I enclose herewith a cheque valued at £209,719 8s. 6d. ... being the total amount of dividend due on July 24, 1964. Will you please credit this to the above mentioned account.
>
> We would like to confirm the agreement reached with you this morning that this amount will only be used to meet the dividend due on July 24, 1964."

From an answer to an interrogatory administered to the bank in the course of the action, it appeared that, in the telephone conversation referred to in this letter, Mr. Goldbart had informed Mr. Parker that arrangements had been made with an unspecified person to lend or otherwise provide money for the purpose of paying the dividend due to be paid by Rolls Razor Ltd. on July 24, 1964.

The appellant bank had, on June 8, 1964, opened an ordinary dividend No. 4 account. The respondents' cheque for £209,719 8s. 6d. was specially cleared and credited to this account on July 17, 1964. Mr. Bloom was unable to raise further sufficient finance and on July 17, 1964, the directors of Rolls Razor Ltd., resolved to put the company into voluntary liquidation; the appellant bank was so informed. On or about July 20, it amalgamated all the accounts of the company except the ordinary dividend No. 4 account. On August 5, 1964, the respondents' solicitors demanded repayment from Rolls Razor Ltd. of the sum of £209,719 8s. 6d.. but repayment was not made and no demand at this time was made upon the appellant bank. The effective resolution for the liquidation of Rolls Razor Ltd. was passed on August 27, 1964, and on the following day the appellant bank set off the credit balance on ordinary dividend No. 4 account against part of the debit balance on Rolls Razor Ltd.'s other accounts. There followed in due course demand by the respondents for repayment of this sum by the bank and the present proceedings.

Two questions arise, both of which must be answered favorably to the respondents if they are to recover the money from the bank. The first is whether as between the respondents and Rolls Razor Ltd. the terms upon which the loan was made were such as to impress upon the sum of £209,719 8s. 6d. a trust in their favour in the event of the dividend not being paid. The second is whether, in that event, the bank had such notice of the trust or of the circumstances giving rise to it as to make the trust binding upon them.

It is not difficult to establish precisely upon what terms the money was advanced by the respondents to Rolls Razor Ltd. There is no doubt that ***580** the loan was made specifically in order to enable Rolls Razor Ltd. to pay the dividend. There is equally, in my opinion, no doubt that the loan was made only so as to enable Rolls Razor Ltd. to pay the

dividend and for no other purpose. This follows quite clearly from the terms of the letter of Rolls Razor Ltd. to the bank of July 15, 1964, which letter, before transmission to the bank, was sent to the respondents under open cover in order that the cheque might be (as it was) enclosed in it. The mutual intention of the respondents and of Rolls Razor Ltd., and the essence of the bargain, was that the sum advanced should not become part of the assets of Rolls Razor Ltd., but should be used exclusively for payment of a particular class of its creditors, namely, those entitled to the dividend. A necessary consequence from this, by process simply of interpretation, must be that if, for any reason, the dividend could not be paid, the money was to be returned to the respondents: the word "only" or "exclusively" can have no other meaning or effect.

That arrangements of this character for the payment of a person's creditors by a third person, give rise to a relationship of a fiduciary character or trust, in favour, as a primary trust, of the creditors, and secondarily, if the primary trust fails, of the third person, has been recognised in a series of cases over some 150 years.

In Toovey v. Milne (1819) 2 B. & A. 683part of the money advanced was, on the failure of the purpose for which it was lent (viz, to pay certain debts), repaid by the bankrupt to the person who had advanced it. On action being brought by the assignee of the bankrupt to recover it, the plaintiff was non suited and the non suit was upheld on a motion for a retrial. In his judgment Abbott C.J. said, at p. 684:

> "I thought at the trial, and still think, that the fair inference from the facts proved was that this money was advanced for a special purpose, and that being so clothed with a specific trust, no property in it passed to the assignee of the bankrupt. Then the purpose having failed, there is an implied stipulation that the money shall be repaid. That has been done in the present case; and I am of opinion that that repayment was lawful, and that the non suit was right."

The basis for the decision was thus clearly stated, viz., that the money advanced for the specific purpose did not become part of the bankrupt's estate. This case has been repeatedly followed and applied: see Edwards v. Glynn (1859) 2 E. & E. 29; In re Rogers, Ex parte Holland and Hannen (1891) 8 Morr. 243; *In re Drucker (No. 1) [1902] 2 K.B. 237*; In re Hooley, Ex parte Trustee [1915] H.B.R. 181. In re Rogers, 8 Morr. 243was a decision of a strong Court of Appeal. In that case, the money provided by the third party had been paid to the creditors before the bankruptcy. Afterwards the trustee in bankruptcy sought to recover it. It was held that the money was advanced to the bankrupt for the special purpose of enabling his creditors to be paid, was impressed with a trust for the purpose and never became the property of the bankrupt. Lindley L.J. decided the case on principle but said (at p. 248) that if authority was needed it would be found in Toovey v. Milne, 2 B. & A. 683and other cases. Bowen L.J. said (8 Morr. 243, 248) that the money came to the bankrupt's hands impressed with a trust and did not become the property of the bankrupt ***581*** divisible amongst his creditors, and the judgment of Kay L.J., at p. 249, was to a similar effect.

These cases have the support of longevity, authority, consistency and, I would add, good sense. But they are not binding on your Lordships and it is necessary to consider such arguments as have been put why they should be departed from or distinguished.

It is said, first, that the line of authorities mentioned above stands on its own and is inconsistent with other, more modern, decisions. Those are cases in which money has been paid to a company for the purpose of obtaining an allotment of shares (see Moseley v. Cressey's Co. (1865) L.R. 1 Eq. 405; Stewart v. Austin (1866) L.R. 3 Eq. 299; *In re Nanwa Gold Mines Ltd. [1955] 1 W.L.R. 1080*). I do not think it necessary to examine these cases in detail, nor to comment on them, for I am satisfied that they do not affect the principle on which this appeal should be decided. They are merely examples which show that, in the absence of some special arrangement creating a trust (as was shown to exist in In re Nanwa Gold Mines Ltd.), payments of this kind are made upon the basis that they are to be included in the company's assets. They do not negative the proposition that a trust may exist where the mutual intention is that they should not.

The second, and main, argument for the appellant was of a more sophisticated character. The transaction, it was said, between the respondents and Rolls Razor Ltd., was one of loan, giving rise to a legal action of debt. This necessarily excluded the implication of any trust, enforceable in equity, in the respondents' favour: a transaction may attract one action or the other, it could not admit of both.

My Lords, I must say that I find this argument unattractive. Let us see what it involves. It means that the law does not permit an arrangement to be made by which one person agrees to advance money to another, on terms that the money is to be used exclusively to pay debts of the latter, and if, and so far as not so used, rather than becoming a general asset of the latter available to his creditors at large, is to be returned to the lender. The lender is obliged, in such a case, because he is a lender, to accept, whatever the mutual wishes of lender and borrower may be, that the money he was willing to make available for one purpose only shall be freely available for others of the borrower's creditors for whom he has not the slightest desire to provide.

I should be surprised if an argument of this kind - so conceptualist in character - had ever been accepted. In truth it has plainly been rejected by the eminent judges who from 1819 onwards have permitted arrangements of this type to be enforced, and have approved them as being for the benefit of creditors and all concerned. There is surely no difficulty in recognising the co-existence in one transaction of legal and equitable rights and remedies: when the money is advanced, the lender acquires an equitable right to see that it is applied for the primary designated purpose (see In re Rogers, 8 Morr. 243where both Lindley L.J. and Kay L.J. recognised this): when the purpose has been carried out (i.e., the debt paid) the lender has his remedy against the borrower in debt: if the primary purpose cannot be carried out, the question arises if a secondary purpose (i.e., repayment to the lender) has been agreed, expressly or by implication: if it has, the remedies of equity may be invoked to give effect to it, if it has not (and ***582*** the money is intended to fall within the general fund of the debtor's assets) then there is the appropriate remedy for recovery of a loan. I can appreciate no reason why the flexible interplay of law and equity cannot let in these practical arrangements, and other variations if desired: it would be to the discredit of both systems if they could not. In the present case the intention to create a secondary trust for the benefit of the lender, to arise if the primary trust, to pay the dividend, could not be carried out, is clear and I can find no reason why the law should not give effect to it.

I pass to the second question, that of notice. I can deal with this briefly because I am in agreement with the manner in which it has been disposed of by all three members of the

Court of Appeal. I am prepared, for this purpose, to accept, by way of assumption, the position most favorable to the bank, i.e., that it is necessary to show that the bank had notice of the trust or of the circumstances giving rise to the trust, at the time when they received the money, viz., on July 15, 1964, and that notice on a later date, even though they had not in any real sense given value when they received the money or thereafter changed their position, will not do. It is common ground, and I think right, that a mere request to put the money into a separate account is not sufficient to constitute notice. But on July 15, 1964, the bank, when it received the cheque, also received the covering letter of that date which I have set out above: previously there had been the telephone conversation between Mr. Goldbart and Mr. Parker, to which I have also referred. From these there is no doubt that the bank was told that the money had been provided on loan by a third person and was to be used only for the purpose of paying the dividend. This was sufficient to give them notice that it was trust money and not assets of Rolls Razor Ltd.: the fact, if it be so, that they were unaware of the lender's identity (though the respondent's name as drawer was on the cheque) is of no significance. I may add to this, as having some bearing on the merits of the case, that it is quite apparent from earlier documents that the bank were aware that Rolls Razor Ltd. could not provide the money for the dividend and that this would have to come from an outside source and that they never contemplated that the money so provided could be used to reduce the existing overdraft. They were in fact insisting that other or additional arrangements should be made for that purpose. As was appropriately said by Russell L.J., ([1968] Ch. 540, 563F) it would be giving a complete windfall to the bank if they had established a right to retain the money.

In my opinion, the decision of the Court of Appeal was correct on all points and the appeal should be dismissed.

Representation

Solicitors: Durrant Cooper & Hambling; D. J. Freeman & Co.

Appeal dismissed. (J. A. G.)