Understanding Remedies for Breach of Trust

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I. Introduction

A. *Taxonomy*

I want in this paper to make some comments about remedies for breach of trust, in an effort to increase understanding of the area. I will try to set my comments within the parameters of recent taxonomic research in the area of remedies in private law. There are two classifications that I will use that I believe are very useful. First, there is a functional characterisation. What is the remedy doing? Is it performative? In other words, is it a means of getting the trustee to perform the obligations that determine his or her status as a trustee, or that are correlative to the rights asserted by the beneficiary? Or is the remedy compensatory? Is it seeking to repair a loss suffered by the beneficiary? Or perhaps the remedy is provided in order to strip away the gain made by the defaulting trustee, what has become known widely in recent scholarship as disgorgement? Finally, perhaps there is scope for a punitive remedy? So that is one classification – performance, compensation, disgorgement or punishment? Another classification that is more established in our understanding of remedies in trusts law is the one that distinguishes personal from proprietary remedies. This distinction is in some respects subordinate to the first. Usually those remedies that call for performance, compensation or punishment are personal, directed against the defendant trustee personally. Those that call for disgorgement, on the other hand, are as likely to be proprietary as they are to be personal. In other words, they can be directed at determining and declaring the property rights in identified assets in the hands of the defendant trustee. I must add at the outset that I am in this paper concerned only with judicial remedies.

B. *Breach of Trust*

The notion of "breach of trust" itself is somewhat ambiguous. Beneficiaries, or more properly their counsel, normally allege "breach of trust" as if it were a sort of justificatory mantra in demanding a remedy. Judges are often parties to continuing confusion about the concept. Breach of trust is a fundamental part of the law of equity, and the concept needs to be approached with a little more sophistication than is often shown. To approach the subject through the law of remedies goes some way towards helping define the concept with greater precision.

A further initial point has to do with the fact that the notion of "breach" is inextricably tied up with duty. Analytically, a breach is a failure to sustain a duty. It does not necessarily import any element of moral turpitude or fault on the part

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of the duty-breaker. In that respect, a breach can loosely but correctly be described as a "no-wrong", in order to avoid the prevalent trend to describe all breaches of duty as wrongs, incorporating thereby some fault element. However, it must first be appreciated that a trustee owes duties to beneficiaries that do not require breach before they become legally "remediable". Thus, if a trustee's duty is in essence a primary obligation to perform some task, then an order for performance is a remedy available in equity to ensure the duty is fulfilled. A performance order (or "remedy") is obviously available in respect of both positive and negative obligations recognised exclusively in equity, since it is that jurisdiction that grants performance remedies for many other jurisdictionally non-equitable obligations, by means of injunction or decrees for specific performance. The issue of what performance entails in any circumstance is a separate matter, linked to the content of the relevant equitable duty in question.

If a trustee fails to perform a primary duty owed by him or her in equity, there is consequently a breach. That breach will give rise to a secondary right in the beneficiary to whom that primary duty is owed. That secondary right is the right to obtain a remedy. The breach creates a secondary duty in the trustee, the content of which is to remedy the consequences of the breach. The breach is analytically a "legal wrong", and it is remediable in a variety of ways that reflect the functional classification outlined earlier, but that also reflect the nature of the particular primary obligation breached. Thus, if there occurs a non-performance of a positive primary duty, or a failure to maintain a negative duty, and a "wrong" thereby occurs, that wrong may be remediable by means of an order requiring repair of the loss suffered by the beneficiary (compensation), or an order mandating the stripping of gains made by the trustee (disgorgement). At common law, compensation, under the rubric "damages", has tended to be understood as the presumptive content of a wrongdoer's secondary obligation to remedy a "wrong". However, the presumptive content of a wrongdoer's secondary obligation to remedy a wrong in equity has tended to be the taking away of the gain made, or in terms of the notation used in this discussion, disgorgement (or restitution in the sense of "giving up", rather than of "giving back"), usually through a process of accounting for profits followed by an order for payment of the profit as ascertained, or by a proprietary remedy attached to identified assets in the hands of the defendant, such as a constructive trust. These responses are remedies responding to wrongdoing. They are presumptive only. Common law wrongs can, at least in some circumstances, also be met by disgorgement; and equitable wrongs can also, as we shall see, be met by reparative (often loosely called equitable) compensation where appropriate.

C. *Compensation*

"Compensation" is a somewhat problematic concept here. The work of Dr Steven Elliott in his important 2002 Oxford DPhil thesis, *Compensation Claims Against Trustees*, has shown that while "compensation" is normally used to refer to a monetary remedy available only for loss caused by a wrongdoing, or breach of duty, where the objective is to repair a loss suffered by the claimant (this is the well-established assumption that reparation is indeed the normal connotation of "compensation"), it transpires that the apparently compensatory jurisdiction of equity is far more complicated than this.

There is a further form of compensation by payment of money, as revealed by the manner in which equity deals with the enforcement of the primary obligations of trustees (and more generally those fiduciaries who have custody of property on behalf of others, whom we can herein term "custodial fiduciaries" or trustees interchangeably), which class of fiduciaries was of course for a very long time almost the sole focus of equity's attention. In this circumstance, as Elliott writes, "compensation consists in a money equivalent to property of which a person has been deprived or denied".[1] Elliott calls this "substitutive compensation because it is calculated to provide a substitute for the property".[2] But, as Elliott goes on to show, from very early times equity was also concerned with monetary compensatory awards founded on the objective of reparation for loss caused by wrongdoing (or breach). Thus, in equity, compensation – in a non-technical sense of monetary orders – was from early on an established remedial response, but one which had two different functional objectives.

II. Enforcement of a Trustee's Primary Custodial Duty by Common Account

All custodial fiduciaries, of whom the express trustee is but the paradigm case, are bound to apply property they receive in their fiduciary capacity for the benefit of another, and are thus under a fiduciary duty to account for the trust fund, which duty arises immediately upon receipt of the relevant trust property. This is a primary obligation. It is enforceable in its character as a primary obligation by those who are interested in the trust fund and to whom the obligation is accordingly owed, *whether or not there has been any breach of that obligation by the fiduciary*. The enforcement of the primary obligation does not depend upon there being a prior breach established, because no secondary obligation is analytically necessary for its enforcement. The duty of a custodial fiduciary to render an account does not depend on the fiduciary's having mishandled the property or having otherwise breached his or her trust. Often of course it is a breach in the real world that brings the matter before a court, but the enforcement is directed at the administration or carrying out of the trust, not at remedying any breach. Hence, the mechanism by which it is enforced is the common account, or, as it is also known, "the order for administration in common form".[3] In *Glazier Holdings Pty Ltd v Australian Men's Health Pty Ltd (No 2)*, Austin J succinctly commented:[4]

> An order for an account of administration is made for the taking of accounts of money received and disbursed by the person who is responsible for the administration of a business enterprise or fund or other property [what I term

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1 Ch III, "Remedial Concepts", 1. Compensation.

2 Ibid.

3 This particular procedure can be understood as part of what is historically and more generally called "judicial execution proceedings". However, the latter are now rare, and the common account procedure is better understood as a form of direct enforcement of a custodial fiduciary's primary obligation of accountability. Other forms of direct enforcement of primary obligations are by direction of the Court, by means of an injunction or by declaration: see further R Chambers, "Liability" in P Birks and A Pretto (eds), *Breach of Trust* (Hart, Oxford, 2002) Ch 1, pp 10–11.

4 [2001] NSWSC 6, paras 37–38.

> herein a custodial fiduciary], and for payment of any amount found to be due by that person upon the taking of the accounts. ... In such a case the making of the order need not imply any wrongdoing by the defendant .... The usual form of order ... requires the defendant to account only for what he or she has actually received, and his or her disbursement and distribution of it. The defendant prepares accounts and it is open to the other parties to surcharge or falsify items in those accounts. A surcharge is the showing of an omission for which credit ought to have been given, while a falsification is the showing of a charge which has been wrongly inserted, the falsifying party alleging that money shown in the account as paid was either not paid or improperly paid ....

An account will balance when the sum of the receipts equals the sum of the discharges and property still in the custody of the trustee. If the account does not balance, the difference represents the sum that the custodial fiduciary is liable to make good *out of his or her own pocket*. It bears repetition, however, that the court orders that follow from the taking of the common account are not granted in order to enforce secondary obligations to make good (or otherwise to remedy) any loss caused by a breach of trust. In some cases, the orders are best understood analytically as being made to enforce the primary duties of the fiduciary, by directing the "restitution" or "restoration" of the trust property (either in specie or more likely by payment of a pecuniary substitute), either to the beneficiaries directly (where there is a duty on the trustee actually to distribute the fund to beneficiaries because the latter have an immediate right to be paid) or to the current trustee (where there is a duty on the trustee to transfer the trust fund to a replacement custodial fiduciary). In so far as any orders in this circumstance require the payment of money, they are not concerned with reparation, but with a substituted (monetary) performance. To the extent that the payment ordered looks like compensation, it is clearly "substitutive compensation", not "reparative compensation". In other circumstances, court orders after the taking of a common account may enforce primary duties of the custodial fiduciary, in a non-restitutionary or non-restorationary manner, by, for example, requiring the clear segregation and protection of the trust fund where the same custodial relationship is to continue as such into the future.

Common account is, therefore, a claim to performance. It is the vindication of an existing *in personam* primary right. It is the (judicial) method by which a custodial fiduciary is required to execute his or her personal obligation of accountability in respect of the trust property. If the fiduciary no longer has the original property, and cannot therefore specifically perform his or her primary obligation, the claim will be that he or she must perform by payment of a (substitutionary) monetary equivalent to re-establish the fund. This vindication claim cannot be a claim for damages to repair the loss suffered by reason of an equitable wrongdoing. As Elliott states: "The claim does not rest upon the allegation of loss in the sense of detriment or injury, and for this reason considerations of causation, remoteness, mitigation and contributory fault are inapposite. The award may be described as compensation but it is compensation of the substitutive variety."[5] The monetary equivalent (or "compensation") is measured by the objective value of the property lost as determined after the account is taken. The subjective position of the

5 Ch I "Introduction", 4. The Claims.

individual claimant beneficiary is not relevant in assessing the loss, nor is any "consequential loss" to be considered. Nor does the claim require any unjust enrichment by the custodial fiduciary. The claimant obtains no more and no less than the performance of the primary right to which he or she is entitled, being restoration of the trust fund, even if that requires a monetary substitution by the trustee himself of herself.[6]

III. Failure to Discharge a Trustee's Custodial Duty: Account on the Basis of Wilful Default

Of course, common account is not the only form of "account of administration" available against a custodial fiduciary. There is also available the "account on the basis of wilful default". As Austin J stated in *Glazier Holdings*:[7]

> The order is 'entirely grounded on misconduct', the defendant being required to account not only for what he or she has not received, but also for what he or she might have received had it not been for the default: ... the concept of 'wilful default' is confined to cases where there has been 'a loss of assets received, or assets which might have been received': ... the concept is evidently not confined to cases of conscious wrongdoing: ... the Court may make an order that general accounts be taken on the footing of wilful default if at least one instance of wilful default has been proved. ... An order for accounts based on wilful default has the effect of casting a much more substantial burden of proof on the accounting party than applies in the case of common accounts. On a falsification, the onus is on the accounting party to justify the account. ... An accounting on the footing of wilful default leads to an order requiring the defendant to replenish funds wrongfully depleted by him or her and in that sense to make restitution for the benefit of the claimant.

Austin J also pointed out an important aspect of the account on the basis of wilful default, by distinguishing it from an order for an account of profits.[8] The objective of the latter is to identify those gains made by the fiduciary through a finding of specific wrongdoing. That gain is then to be disgorged ("given up"), as a remedy for the wrongdoing, often, but by no means always, by means of a proprietary constructive trust. The former type of account relates to administration of the trust, where "emphasis is placed on whether the defendant has failed to discharge his or her duty, rather than whether the claimant has established active conduct in breach of duty".[9] One commentator has suggested

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6 This substitutive analysis explains the oft-cited statement of Street J in *Re Dawson* [1966] 2 NSWR 211, 214–216. The relief sought there was substitutive compensation. The primary liability of the defendant fiduciary was to restore the property in specie. If that were not possible, then the monetary compensation payable in lieu (which might, but only very loosely and inaccurately be termed "equitable compensation") must reflect the economic position had restoration in specie been possible. The case was not one where reparative compensation was sought. Street J was not stating the characteristics of the remedy of equitable compensation as reparation for loss. Since the compensation sought was substitutive, based on performance of the trustee's primary obligations, it demonstrated obviously claimant-friendly characteristics.

7 [2001] NSWSC 6, paras 39–42.

8 Ibid, paras 43–45.

9 Ibid, para 46.

that: "The technical meaning of 'wilful default' is a failure to receive assets that would have been received if the trust had been performed properly."[10] This leads to an important observation, made by Austin J in the extract quoted above. Charging a defendant trustee in his or her account means that he or she is chargeable with property actually received, and is liable to be surcharged with property he or she might have received. The basis upon which the defendant will be surcharged with forgone receipts (ie, beyond actual receipts) is wilful default. But it is likely that "wilful default" and "breach of trust" are co-extensive concepts, and that the focus of the account for wilful default extends beyond merely the failure to receive assets. If breach of trust amounts to nothing other than an infringement by the trustee of any duty owed as trustee to the beneficiary, then the basis upon which the trustee can be surcharged for foregone receipts, and probably for lost assets (lost, for example, by negligent conduct) as well, termed wilful default, is actually no greater than that the defendant trustee has breached a duty he or she owes by virtue of the office of trustee.[11] Thus, an "account on the basis of wilful default" encompasses the same ground as a standard "account in common form" (ie, what property the trustee received and what has become of it), but goes further (ie, the trustee may be surcharged with property he or she would have received but for his or her wilful default, meaning breach of trust). But more still needs to be said.

There is, it is now clear, a problem in linking too closely the two forms of accounts of administration. The danger is that an important functional – and thus taxonomic – point is missed. As seen above, the common form of account is not founded upon misconduct by the custodial fiduciary. The duty it enforces is a primary duty; its objective is merely to ascertain the property that the trustee is understood to hold in that capacity with a view to ensuring the carrying out of the trust obligations by the trustee. Any order of payment of money by the fiduciary personally in this context is at most substitutive (or performative) compensation. The wilful default form of account is, however, conceptually quite distinct. It is founded upon a breach of primary duty by the custodial fiduciary, hence a wrong, that has resulted in loss. The duty it enforces is a secondary or remedial duty. And its objective is to remedy the breach by making good the loss through surcharging the trustee's account. The focus is undeniably reparative compensation, because the surcharge, although usually but misleadingly described as a charge on the basis of what the fiduciary ought to have received but did not receive, is in reality a charge in the amount of the loss sustained, determined to be as if the fiduciary had received more than he actually did. This point was clearly made by Giles JA in *Meehan v Glazier Holdings*

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10 See R Chambers, "Liability" in P Birks and A Pretto (eds), *Breach of Trust* (Hart, Oxford, 2002) Ch 1, p 19.

11 Two definitions of what is encompassed by referring to a "breach of trust" are found in P Birks and A Pretto (eds), *Breach of Trust* (Hart, Oxford, 2002). Birks and Pretto comment that there are "breaches which consist in ultra vires acts and ... breaches which consist in doing badly acts which, done properly, would be intra vires": see "Preface", p ix. Mr Justice, then Professor, Hayton stated: "A breach of trust is any act or neglect on the part of a trustee which is not authorised or excused by the terms of the trust instrument or by law, or which fails to satisfy the duties imposed on a trustee conducting authorized activities": see "Overview", p 384.

Pty Ltd : "Under such an order the accounting party must account not only for what has actually been received, but also for what should have been received: that is, for what would have been received if the relevant duties of the accounting party had been properly discharged."[12]

Equity has thus long recognised monetary awards in connection with trusts and other custodial fiduciary relationships. These awards can be properly compensatory in their function, even though that function is hidden behind the obfuscatory and ancient language of accounts. Compensation is "achieved ... by making [custodial fiduciaries] accountable for assets which they [have] lost or [have] failed to receive".[13] The monetary "compensation" can, however, be measured differently, either as substitution for performance, or as reparation for loss.

IV. The Features of Reparative Compensation

Another important issue now presents itself. Is the award of reparative compensation for loss controlled by the same claimant-friendly characteristics[14] as control the award of the substitution for performance type of compensation? That was the very issue at stake in the important and difficult decision of the House of Lords in *Target Holdings Ltd v Redferns*.[15] The beneficiary's claim in that case was cast as one for substitutive compensation for performance of a primary obligation, but Lord Browne-Wilkinson, in a speech concurred in by the four other Law Lords, recast the claim as one for reparative compensation for loss suffered because of breach of a primary obligation. The decision reached is accordingly an extraordinarily difficult one to understand, and it has resulted in considerable confusion. I have fully analysed the case elsewhere.[16] My conclusion was that Lord Browne-Wilkinson's reasoning seems to amount to a suggestion that all monetary orders against trustees must be reparative in nature, and that accordingly the absolute nature of the trustee's performance obligation can in effect be softened, if not almost entirely avoided, by importing notions of causation of loss. I also went on in my earlier analysis to examine post-*Target Holdings* decisions in Australia and England that clearly reveal unease with Lord Browne-Wilkinson's position. Most recently, of course, in *Youyang Pty Ltd v Minter Ellison Morris Fletcher*,[17] the High Court of Australia has effectively avoided the reparative focus in *Target Holdings* by adopting an explanation of that decision articulated extra-judicially by Lord Millett.[18] This

12 (2002) 54 NSWLR 146, para 14. See also *Armitage v Nourse* [1998] Ch 241, 252 per Millett LJ: "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."

13 Birks and Pretto, Preface in *Breach of Trust*, p xi.

14 As outlined by Street J in *Re Dawson* [1966] 2 NSWR 211, 214–216.

15 [1996] 1 AC 421.

16 C Rickett, "Equitable Compensation: Towards a Blueprint?" (2003) 25 Sydney LR 31, esp 40–50.

17 (2003) 196 ALR 482.

18 "Equity's Place in the Law of Commerce" (1998) 114 LQR 214 (see *Youyang v Minter Ellison Morris Fletcher* (2003) 196 ALR 482, para 45).

view (it appears it may have first been articulated by the late Professor Birks[19]) sees *Target Holdings* as a standard substitutive compensation case, concerned accordingly with accounting: the solicitor-trustees were held accountable, and the reason why no compensation was awarded was because they had as it happened accounted for the funds paid away by obtaining the very mortgage that the beneficiary had authorized the trustees to acquire on their behalf. This interpretation of *Target Holdings* sustains therefore the traditional position on compensation as outlined earlier in this paper, but in reality the interpretation does not sit comfortably with the actual terms in which the decision in *Target Holdings* was reached. That decision will clearly need reconsideration by the House of Lords when appropriate in the future.

If we are able to posit, as does the High Court of Australia in *Youyang*, the maintenance of the traditional substitutive/reparative distinction, unsullied by the sort of adventurous analysis some suggest occurred in Lord Browne-Wilkinson's speech in *Target Holdings*, then we can conclude with some certainty that, in respect of their custodial duties, trustees can be required to perform by substitution, and can be required to make good losses (sustained because of a failure to perform) by reparation. The limits controlling the reparative remedy are claimant-friendly, and differ from those controlling the substitutive remedy only by introducing a causation requirement.[20]

V. The Non-Custodial Duties of Trustees

Thus far, our concern has been with duties owed by trustees in connection with the custody of the trust property. Custodial fiduciaries, however, also owe other types of duties to their beneficiaries. If such duties are breached, the temptation appears to be to lump such breaches into some general single category of breach of trust, simply on the basis that the duties are owed by persons who happen to be trustees. This temptation is one to be very much wary of, because the types of breaches within any such single general category will not all be the same, and accordingly their remedial consequences must also be different.

First, in addition to custodial duties, trustees owe non-custodial fiduciary duties of loyalty and fidelity that emanate from a relationship of trust and confidence, and manifest themselves in rules prohibiting profit-making at the expense of the beneficiary, and prohibiting activity which causes a conflict with the trustee's requirement to be loyal and faithful.[21] The results of breaches of the no-profit and no-conflict duties are remedied by traditional equitable responses; these responses are based taxonomically on secondary duties to remedy breaches of primary duties, which responses are analytically required – by the nature of

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19 "Equity in the Modern Law: An Exercise in Taxonomy" (1996) 26 UWALR 1, 45–48.

20 See, for examples, *O'Halloran v RT Thomas & Family Pty Ltd* (1998) 45 NSWLR 262; *Bairstow v Queens Moat Houses plc* [2001] 2 BCLC 531; and *Youyang v Minter Ellison Morris Fletcher* (2003) 196 ALR 482.

21 See, eg, *Breen v Williams* (1996) 186 CLR 71 (HCA); *Bristol and West Building Society v Mothew* [1998] 1 Ch I (CA); *Arklow Investments Ltd v Maclean* [2000] 2 NZLR 1 (PC); *Pilmer v Duke Group Ltd (in liq)* (2001) 75 ALJR 1067 (HCA); *Aequitas Ltd v Sparad No 100 Ltd* [2001] NSWSC 14, paras 278–288 per Austin J.

those very primary duties in question – to achieve disgorgement by stripping any gains made and / or to avoid any transactions entered into. These responses are consistent with the prohibitive objectives of the rules reflecting the content of the trustee's duties, and in that respect continue to be the presumptive responses for their breach. It is in that sense that they can be said to be "traditional" responses. What, however, of the non-presumptive response of reparative compensation? It is reasonably easy to appreciate why breaches of custodial fiduciary duties, whereby loss is caused to the trust fund, should be met where necessary by reparative compensation. The entire thrust of the custodial fiduciary's role is the management of the fund within certain limits and for the benefit of the beneficiaries. Loss by breach of duty to maintain the fund cannot be permitted and must be remedied. However, in respect of non-custodial fiduciary duties, where the focus of the duties appears to be proscriptive, it is less obvious that reparative compensation should follow automatically from their breach. To reach that conclusion needs, it is suggested, a re-visioning of the duty of loyalty and fidelity as prescriptive rather than proscriptive, or as constitutive of positive requirements, which, if breached in such a way as to result in loss, behove such a reparative compensatory response. In England, New Zealand and Canada such re-visioning has in effect occurred.[22] In Australia, on the other hand, there has been much less readiness to adopt such a re-visioning, and fiduciary duties have tended to retain their strongly proscriptive or negative character.[23] The debate as to the legitimacy of the re-visioning of these obligations is fundamental, but beyond the scope of this paper. I have discussed (on the assumption that a re-visioning is legitimate) the parameters of the reparative compensation remedy available for breaches of the non-custodial fiduciary duties of trustees in detail elsewhere.[24] In essence, the "absolute" nature of the duties, which carries with it the notion that any breach is "equitable fraud", sustains a claimant-friendly approach to the remedy, not unlike that found in cases of the breach of custodial duties. That conclusion does not, however, avoid the necessity to distinguish these different types of duty when detailing their breach and the proper remedial responses.

The need to distinguish different duties becomes irrefutable when the recent articulation of equitable duties of care and skill is taken into account. Such duties

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22 See *Bristol and West Building Society v Mothew* [1998] 1 Ch 1; *Swindle v Harrison* [1997] 4 All ER 705 (CA); *Longstaff v Birtles* [2002] 1 WLR 470 (CA). *Day v Mead* [1987] 2 NZLR 443 (CA); *Bank of New Zealand v New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 664 (CA). *Canson Enterprises Ltd v Boughton & Co* [1991] 3 SCR 534 (SCC); *Hodgkinson v Simms* [1994] 3 SCR 377(SCC).

23 See *Pilmer v Duke Group Ltd (in liquidation)* (2001) 75 ALJR 1067, 1084–1085 per McHugh, Gummow, Hayne and Callinan JJ, 1093–1096 and 1098–1100 per Kirby J (HCA); *Maguire v Makaronis* (1996-97) 188 CLR 449, 471–474 per Brennan CJ, Gaudron, McHugh, and Gummow JJ (HCA).

24 See C Rickett, "Compensating for Loss in Equity - Choosing the Right Horse for Each Course" in P Birks and F Rose (eds), *Restitution and Equity Vol 1: Resulting Trusts and Equitable Compensation* (LLP, London. 2000) Ch 10. In this context, the decisions of Fisher J in *Bank of New Zealand v New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 213, and of the Court of Appeal [1999] 1 NZLR 664 are of much interest (see further S Elliott, "Remoteness Criteria in Equity" (2002) 65 MLR 588).

are owed, inter alia, by trustees, but their breach, although categorised loosely as a breach of trust, has very different remedial consequences from those outlined thus far. In Australia, the High Court has, in obiter comments in *Youyang*,[25] cast doubt on the legitimacy of recognizing such duties at all. However, in England and New Zealand, the equitable duty of care and skill is now well established.[26] Where such a duty is breached, so as to result in loss, a remedial secondary duty arises. The case law thus far shows that the rules for reparative compensation for loss in breach of equitable duty of care cases will mirror to a considerable extent the rules developed for damages awards at common law. Thus, the remedy is likely to be much less claimant-friendly than its manifestation in the other situations of breach of trust already discussed.

Breach of trust, therefore, can sometimes mean the requirement to perform, or a failure to perform, primary duties that are custodial; or it can mean failure to maintain or perform primary fiduciary duties of loyalty and fidelity; or it can mean the failure to reach a standard of care and skill required by a duty to exercise that standard of care. These are conceptually distinct situations, which call for conceptually distinct remedies, some ordering actual or substitutive performance, some ordering reparative compensation, and some requiring disgorgement. So, when a beneficiary alleges a breach of trust, it behoves counsel and judges alike to consider carefully exactly what is in issue. A failure to do that simply compounds confusion, and risks either under-emphasising the beneficiary's rights or over-emphasising the trustee's obligations.

VI. Punitive Damages for Breach of Trust?

I turn now to the issue whether a punitive remedy can be awarded against a trustee in breach. The award of punitive damages has become something of an infatuation amongst private common lawyers. Indeed, the "remedy" has acquired all the marks of a legal juggernaut. It rolls on with little concern about its fundamental right to be on the road at all, caught up in the headiness of its own success as a means of getting a job done. And what job is that? Well, of course, of giving an extra, oftentimes very painful, slap on the wrist (or wrench of the wallet) to those who not merely breach a claimant's right, but who do so in a particularly horrible way.

It might intuitively be thought that equity, in respect of breaches of all manner of equitable duties, and in particular breaches of custodial duties and fiduciary duties of loyalty and fidelity, and in particular in view of the presumption equity gives to profit-stripping or disgorgement remedies, oftentimes of a proprietary character – oh, so harsh! – would be a much better candidate to embrace punitive

25 (2003) 196 ALR 482, paras 38–39. See also JD Heydon, "Are the Duties of Company Directors to Exercise Care and Skill Fiduciary?" in S Degeling and J Edelman (eds), *Equity in Commercial Law* (Thomson, Sydney, 2005) Ch 9.

26 See *Bristol and West Building Society v Mothew* [1998] 1 Ch 1, 16–17 per Millett LJ (CA); *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145, 204–206 per Lord Browne-Wilkinson (HL); *White v Jones* [1995] 2 AC 207, 271–272 per Lord Browne-Wilkinson (HL); *Medforth v Blake* [2000] Ch 86 (CA); *Bank of New Zealand v New Zealand Guardian Trust Co Ltd* [1999] 1 NZLR 664 (NZCA), and *Permanent Building Society (in liq) v Wheeler* (1994) 14 ACSR 109, 157–158 per Ipp J (SCWA Full Ct).

damages than the common law ever was. After all, is it not a relatively small step from forcing a giving up (or, from the other side, a taking away) to punishing? However, equity has largely, at least outside New Zealand[27] and Canada, avoided the problem of punitive damages. They have nonetheless remained an enormous problem for common lawyers.

As is now well-known, a decision in New South Wales recently caused equity lawyers to confront the issue head on. It turns out to be an issue that requires a negotiation of the thickets of equity jurisprudence, and that also raises the whole contested matter of the coherence of private law in general. In *Harris v Digital Pulse Pty Ltd*,[28] the New South Wales Court of Appeal split on the matter. Although not a classic breach of trust case, there is much to be learned from it. Digital provided multi-media services to clients. The defendants were its employees. They became dissatisfied with Digital and decided to leave and set up their own competing business. While continuing in the employ of Digital they diverted business opportunities to themselves and their new company. Digital sued the defendants for, inter alia, breach of fiduciary duty. At first instance,[29] Palmer J awarded equitable reparatory compensation and, in the alternative, an account of profits for disgorgement. After a lengthy discussion concluding that exemplary damages can be awarded in equity, and having earlier listed the various factors that made punishment appropriate in the case before him, his Honour also awarded exemplary damages against the defendants.

An issue of law was thus taken to the Court of Appeal – was there jurisdiction in equity to order a punitive monetary award? Three rather different judgments were given, but the overall outcome of the case appears to be that there might be a future, in New South Wales at least, for punitive damages in at least some, rather restricted, cases of breaches of equitable duties, which might therefore catch some trustees in breach.

Spigelman CJ's judgment was a principled judgment focused at a conceptual level. In his Honour's view, it was neither necessary nor desirable to decide that a "punitive monetary award", as he preferred to term it, could *never* be awarded in equity, and he trumpeted remedial flexibility as a characteristic of equity jurisprudence. The key, however, was to examine the particular duty in issue, which here was a fiduciary duty arising as part of a fiduciary relationship "created by contract between the parties, in which one party has a fiduciary obligation to act in the interests of the other in relevant respects".[30] Being akin to a duty arising in contract rather than tort, it was appropriate to draw an analogy with the approach of contract law to punitive damages for breach. Since they were, in Australian law at least, unavailable, they should not be awarded in the instant case. Furthermore, equity's willingness to give relief for penalties in contract

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27 Where the majority decision of the Court of Appeal in *Aquaculture Corporation v New Zealand Green Mussel Co Ltd* [1990] 3 NZLR 299 planted the seed of a concept of penalty as legitimate in the local variant of equity, which has now grown into a large and rather aimless tree, mirroring to a large extent the common law juggernaut!

28 (2003) 44 ACSR 390.

29 (2002) 40 ACSR 487.

30 (2003) 44 ACSR 390, 391, para 5.

cases in general would be incompatible with imposing a penalty for breach of an obligation imputed by operation of law on the basis of an undertaking or agreement. This reasoning meant, as the Chief Justice acknowledged, that a refusal to provide a punitive monetary award would extend only to breaches of fiduciary obligations whose essential basis was a contractual relationship. As he said, "[t]here may be other cases in equity in which a tort analogy is more appropriate",[31] where, it seems, the arguments in favour of such an award might be strong, or perhaps the arguments against the award might be considerably weakened. A caveat must be entered at this point, however. Spigelman CJ also accepted Heydon JA's analysis of the authorities, and expressed general agreement with the latter's reasons, discussed below, (with one small reservation) for his very strong conclusion that there was no jurisdiction to award exemplary damages in equity. Unfortunately, we are accordingly left wondering to some degree exactly what Spigelman CJ's final position actually is!

This brings us to Mason P's analysis. His Honour's judgment leaves us in no doubt about his position.[32] In Mason P's opinion, "exemplary damages", as he preferred to term them, were available in the instant case. His Honour's lengthy and lucid account was built around the notion that the issue was one about the power of the Court, rather than a debate about jurisdiction.

> Both 'Equity' and 'Common Law' had adequate powers to adopt and adapt concepts from each other's system well before the passing of the Judicature Act, and nothing in that legislation limits such powers. They are of the very essence of judicial method which was and is part of the armoury of every judge in every 'common law' jurisdiction.[33]

Mason P was in favour of the principled integration of the two jurisdictions, and although he was not to be seen as asserting that the fusion of the administration of equity and common law per se justified awarding exemplary damages, notions of consistency and coherence required their availability, and their award in *Digital Pulse*. His Honour argued that equity's willingness to select more stringent remedies for some breaches of fiduciary duty meant that equity was trumpeting a "punitive/deterrent intent",[34] which "expresses more general public concerns"[35] than merely an interest in the private rights of the parties. The pressure for doctrinal coherence led Mason P to confront also the contract/tort analogy. Unlike Spigelman CJ, his Honour's view was that there was a much greater doctrinal and conceptual fit between tort and breach of fiduciary duty, than between the latter and contract. Given "the amplitude of equitable

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31 Ibid, 397, para 44.

32 See also Mason P's extra-judicial commentary in "Fusion: Fallacy, Fiction or Finished?" in S Degeling and J Edelman (eds), *Equity in Commercial Law* (Thomson, Sydney, 2005) Ch 3; and, in the same volume, the paper by A Burrows, "Remedial Coherence and Punitive Damages in Equity", Ch 13. See further A Duggan, "Exemplary Damages in Equity: A Law and Economics Perspective" (2066) 26 OJLS 303 and D Jensen, "Punishment, Deterrence and Fiduciary Obligations" (2007) 1 J of Equity 182.

33 (2003) 44 ACSR 390, 412, para 141.

34 Ibid, at 417, para 166.

35 Ibid, at 418, para 172.

remedial principles"[36] and the analogy of tort, it was entirely appropriate that equity should grant exemplary damages. Such was conceptually coherent with "the policies acceptable throughout tort law".[37]

For those who had had cause to examine the reflections on Palmer J's decision at first instance in the fourth edition of *Meagher, Gummow and Lehane's Equity – Doctrines and Remedies,* authored by, inter alia, Justice JD Heydon, the views of Heydon JA in his judgment in *Digital Pulse,* a judgment longer than those of Spigelman CJ and Mason P put together, came as no surprise. The textbook had expressed "amazement" at Palmer J's decision,[38] suggested that the judge (characterized as "the poor man's Robin Cooke"!) had "disregarded all [the] learning and principle" that no element of penalty was involved in awarding equitable compensation, and concluded that "one hopes that this is a decision which will never be followed".[39] Heydon JA, after an examination of all the learning and principle said to have been ignored by Palmer J, and a forthright rejection of the arguments used to bolster the pro-exemplary damages in equity line adopted by New Zealand and Canadian courts, and by increasing numbers of commentators, concluded that there was "no power in the law of New South Wales to award exemplary damages for equitable wrongs".[40] His Honour stated that "equity does not bear the same relationship to the instinct for revenge as the institution of marriage does the sexual appetite".[41] He held that neither the high rates of interest imposed on defaulting fiduciaries, nor the award of an account of profits, nor the provision made for allowances to defaulting fiduciaries, reflected any punitive approach by equity. Indeed, some doctrines of equity reflected quite the opposite, notably equity's rules relating to penalties and forfeitures and equity's refusal to grant injunctions against crimes. Furthermore, the award of exemplary damages in equity was, in Heydon JA's view (a view expressly rejected by Spigelman CJ and by implication by Mason P), given their punitive nature, in effect judicially to create new criminal sanctions in the 21st Century attaching to conduct that was not necessarily criminal. Equity should not be the handmaid of punishment.[42]

It is impossible, of course, to do justice to the three judgments in the course of a short description. There is much learning, and much argument, in all of them. However, a fundamental issue, so seldom addressed in judgments dealing with claims for exemplary or punitive damages, was sadly only at best hinted at in the *Digital Pulse* judgments also. This is a shame. At common law, in tort at least, the acceptance of punitive damages by the highest courts in the Commonwealth jurisdictions makes a return to the fundamental issue extraordinarily difficult for any but the most robust final appellate court. But in equity the issue is open, at least outside New Zealand and Canada. It can be examined without the

36 Ibid, at 423, para 204.

37 Ibid, at 425, para 213.

38 *Meagher, Gummow and Lehane's Equity – Doctrines and Remedies* (LexisNexis Butterworths, Australia, 2002) p 80.

39 At p 839.

40 (2003) 44 ACSR 390, 500, para 470.

41 Ibid.

42 Ibid, at 470, para 352.

encrustation of case law, in a clear and focused manner.

The question whether exemplary damages are, or should be, available in equity boils down to a re-visitation of the more general debate about their availability within the private law generally. The fundamental issue is to address their coherence *within the very structure of private law claims,* whether those claims are sourced at common law or in equity. In an important article,[43] Dr Allan Beever, now of Durham Law School, has argued, in my view convincingly, that private law and exemplary damages cannot be brought together into a single legal structure, without then having to pretend that the structure makes sense. Essentially, what he means is that exemplary damages are an alien life form in the realm of private law. A very similar argument has also been articulated by Professor Ernest Weinrib.[44]

The remedies of reparative compensation and / or disgorgement or restitution are legitimate responses to a breach of a duty that is owed to the particular claimant by the particular defendant. The key point is that the breach of the initial duty-right relationship creates the claimant's claim, which is correctly a claim *in personam* arising from a secondary duty owed to that particular claimant by that particular defendant. The duty breached defines the response. This analysis is the correct structural analysis of a private law claim in the area of the law of wrongs (analytically understood). In claims for performance of a primary duty by the defendant, the focus on the primary duty in the duty-right relationship very obviously fits the model of the private law duty-right relationship. Enforcement of property rights is a little more complex, as we shall see herein, but since most property rights are enforced indirectly through breaches of *in personam* duties, even here this private law model is vindicated.

Let us return to the facts of *Digital Pulse* to illustrate the point. Assume, as opposed to what happened in the Court of Appeal, that Palmer J's decision at first instance were to be upheld. We can say that, as a matter of practical fact, the award of punitive damages to Digital Pulse followed on from a breach of the fiduciary duty by the defendants. However, the remedy cannot, conceptually, fit the breach alleged, and that must be so whether the primary duty breached is regarded as a common law duty, or an equitable duty, or a "like a contract" duty, or even as a "like a tort" duty. The response of punitive damages, said to flow from the secondary remedial duty raised upon the breach of the primary duty, simply cannot be founded in a duty to pay punitive damages *owed by the defendants to Digital Pulse as the claimant.* A secondary duty raised in the defendants to compensate for loss caused, or to give up profit made, fits the primary fiduciary duty they owed to begin with to Digital Pulse. But a secondary duty in the defendants to pay a fine, even if the fine is directed to be paid to Digital Pulse

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43 "The Structure of Aggravated and Exemplary Damages" (2003) 23 OJLS 87. Dr Beever has continued his attack on the award of punitive damages in a particularly erudite paper delivered at a conference in August 2006 in Brisbane, titled "Justice and Punishment in Tort: A Comparative Theoretical Analysis" and to be published in C Rickett (ed), *Justifying Remedies in Private Law* (Hart Publishing, Oxford, 2008).

44 "Punishment and Disgorgement as Contract Remedies" (2003) 78 Chi-Kent L Rev 55.

rather than into the common purse, can only be a duty owed to society at large. Perhaps there is a primary duty in the defendants, owed to society at large, not to breach in a particularly horrible way another duty owed only to Digital Pulse, a breach of which raises the secondary remedial duty to pay punitive damages to Digital Pulse? This is perhaps what Mason P in *Digital Pulse* was reaching towards when he suggested that, insofar as deterrence existed as a feature of equitable remedies, its focus was to express general public concerns.[45] Whatever, the award of punitive damages to Digital Pulse cannot be justified as part of the legal relationship between Digital Pulse and the defendants. The defendants' liability to pay punitive damages can only arise from a wrong to society, not from a wrong to Digital Pulse. That appears in fact not to be too far removed from Heydon JA's critical criminal sanction analysis. It is unfortunate, however, that the use of the terminology "criminal" appears to have worried both Spigelman CJ and Mason P.

The immediate conclusion must be, as Dr Beever's and Professor Weinrib's arguments show, that punitive damages are inconsistent with the structure of liability in private law and must be rejected as a proper part of that law. Thus, appeals to coherence in modern private law as requiring equity's embrace of exemplary or punitive damages are misplaced. In fact, a coherent *private* law requires equity to reject exemplary damages. If equity avoids succumbing to the enticing call for complete integration with the common law, it might in fact lead to the correction of an error in the common law itself. Equity must keep its senses, and common law must come back to its senses. *Digital Pulse* represents a crack in the wall. One hopes the juggernaut will not come crashing through it! Punishment cannot be justified as a remedy for any form of breach of trust.[46]

VII. A Trustee's Proprietary Duties

Trustees' duties extend of course beyond merely personal duties. They have custody of property, in which the beneficiaries have proprietary rights, and accordingly an appreciation of the full panoply of remedies for breach of trust must take into account remedies for breach of property rights or rights *in rem* asserted by the beneficiaries.

A. *The Nature of Rights* in Rem

Some initial conceptual comments are needed in order to make sense of the specific position. The common law, including here equity, and indeed most sophisticated legal systems, recognise a distinction between rights *in personam* and rights *in rem*. Broadly speaking, a right *in personam* is a right against a particular individual, while a right *in rem* is a right held against an indefinite class of persons in respect of an asset (*res*). The distinction may also be described in terms of exigibility: from whom may the right be demanded?[47] Rights *in personam* are

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45 (2003) 44 ACSR 390, 418, para 172.

46 It is unfortunate therefore to see that such a distinguished trusts lawyer as Justice Hayton suggests otherwise: see "Unique Rules for the Unique Institution, the Trust" in S Degeling and J Edelman (eds), *Equity in Commercial Law* (Thomson, Sydney, 2005) Ch 11, espec 300–304.

47 See P Birks, *An Introduction to the Law of Restitution* (Clarendon, Oxford, 1985)

exigible against a specific individual, while rights *in rem* are exigible against an indefinite class of persons. However, while this distinction between rights *in personam* and rights *in rem* accords with our intuitive understanding of property rights as being essentially thing-centred, the question whether rights *in personam* and rights *in rem* are qualitatively or analytically different is more controversial. This controversy is largely a consequence of the scholarship of Professor Wesley Hohfeld.[48] Hohfeld sought to eliminate, or at least to minimise, the distinction by deconstructing rights *in rem* into mere bundles of rights *in personam*. For Hohfeld, a right *in rem* was to be understood merely as a vast bundle of rights *in personam*, held by the right-holder against each and every other member of society.[49] However, Hohfeld did recognise that rights *in rem* and rights *in personam* differ from each other. This difference lay for Hohfeld in the fact that rights *in rem* always exist as bundles of fundamentally similar rights *in personam*. While Hohfeld's analysis has been highly influential, it is now widely regarded as fatally flawed.[50] One sign of this was Hohfeld's inability to explain why, in the case of rights *in rem*, the rights *always* come in bundles of rights *in personam*. Hohfeld made this distinction through the concepts of "multital" rights (rights *in rem*) and "paucital" rights (rights *in personam*).[51] This is clearly the defining feature of property rights, yet he was unable to offer a positive explanation of this quality.

The better and prevailing view, therefore, is that rights *in rem* are qualitatively distinct from rights *in personam*. This distinction lies primarily in the identity of the subject of the obligation that the right reflects.[52] While a right *in personam* embodies an entitlement against a particular person, the subject of a right *in rem* is not a particular person but a thing or *res*. The *res* thus stands between the right-holder and the duty-ower as the focus of both the right and the duty. The right to enjoyment of the *res* is one held as against every person subject to the particular legal system, but it is a right held as against an indefinite class of persons rather than specific individuals. The correlative duty is one owed by everyone, and everyone owes the same duty, but it is not owed directly to the individual right-holder.[53] Rather, it is a duty in respect of the *res* itself. Accordingly, the right-duty correlation in respect of a right *in rem* is both impersonal and asymmetrical.[54] It is impersonal in that there is no direct chain of obligation between the right-

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49–50; J Penner, *The Idea of Property in Law* (Clarendon, Oxford, 1997) p 31.

48 *Fundamental Legal Conceptions as Applied in Judicial Reasoning* (Yale UP, New Haven, 1919).

49 Generally, see J Harris, *Property and Justice* (Clarendon, Oxford, 1996) pp 120–125; T Eleftheriadis, "The Analysis of Property Rights" (1996) 16 OJLS 31.

50 See P Birks, "Before We Begin: Five Keys to Land Law" in S Bright and J Dewar (eds), *Land Law: Themes and Perspectives* (OUP, Oxford, 1998) p 473; J Penner, "The 'Bundle of Rights' Picture of Property" (1996) 43 UCLA L Rev 711; J Harris, *Property and Justice* (Clarendon, Oxford, 1996) pp 120–125.

51 See *Fundamental Legal Conceptions as Applied in Judicial Reasoning* (Yale UP, New Haven, 1919) p 72.

52 See J Penner, *The Idea of Property in Law* (Clarendon, Oxford, 1997) pp 23–31.

53 See J Penner, *The Idea of Property in Law* (Clarendon, Oxford, 1997) p 24 and L Smith, *The Law of Tracing* (Clarendon, Oxford, 1997) pp 50–51.

54 See J Penner, *The Idea of Property in Law* (Clarendon, Oxford, 1997) p 29.

holder and duty-ower and the identity and personal characteristics of the right-holder are irrelevant to the articulation and understanding of the right. It is asymmetrical in that the right is held as against a class of persons, but the duty is owed to the *res*.

B. *Sanctioning Interference With Rights* in Rem

An important analytical consequence of the nature of rights *in rem* concerns the manner in which an interference with an asset is sanctioned. Although a right *in rem* is a right that binds all the world, when a right *in rem* is infringed by interference with the relevant asset, that infringement is necessarily the activity of a particular person. Accordingly, for the right *in rem* to mean anything in respect of that particular person, a secondary or consequential *in personam* obligation must be generated, by virtue of which that person's activity is sanctioned. Thus, *Salmond* states:

> The reason why sanctioning rights are *in personam* is obvious enough. Rights *in rem* are negative and avail against the all the world, *i.e.*, an open or indefinite class of persons. Violations of such rights, therefore, must consist of positive acts, and positive acts can only be performed by specific persons; it makes no sense to talk of a positive act performed by an indefinite class of persons; in other words a violation by all the world is a logical impossibility. Consequently it is only against specific persons that sanctioning rights can be either necessary or operative: they must be, therefore, rights *in personam*.[55]

To similar effect, Professor James Penner states:

> We do not have to frame the duty to respect property as a duty to particular individuals, but as a duty in respect of things. This will, of course, benefit the individual right-holders, but they need not be individually enumerated in order to understand the content of the duty. When the duty is breached, and the individual owner sues the individual trespasser, only then do we have a claim which is properly *in personam*, against a specific individual. But we must bear in mind that this is a secondary, or remedial right which arises on the breach of the primary one.[56]

The *in personam* sanctioning right thus arises on the interference with the right *in rem*, in order to transform the rights held by a particular individual in respect of the *res*, which are owed by an indefinite class of persons, into a right in that particular individual held as against another particular individual. Although this process might be described in terms of a crystallisation of the right held as against an indefinite class of persons into a right held as against a particular person,[57] the right *in personam* nevertheless arises not as a substitute for the right *in rem*, but in addition to it. The existence of the right *in personam* "does not turn powers and rights *in rem* into a different kind of power or right *in personam*, because these powers and rights continue to exist only so long as the *res* itself does, and only

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55 See P Fitzgerald, *Salmond on Jurisprudence* (12th ed, Sweet & Maxwell, London, 1966) p 244).

56 See *The Idea of Property in Law* (Clarendon, Oxford, 1997) p 24.

57 See C Noyes, *The Institution of Property* (Longmans, Green & Co, New York, 1936) p 241.

against those who are in actual violation of the right *in rem* ...".[58]

Property rights are, therefore, in one sense, inert or superstructural rights. Although they create right-duty relationships that bind everyone as a class, in order to sanction interferences with those rights *in rem* it is necessary to create right-duty relationships between the particular right-holders and the particular infringers. It is only by creating these additional rights *in personam* that the law can sanction or remedy particular infringements. It is clear from an analysis of claims that serve to protect rights *in rem* that the *in personam* sanctioning rights that arise upon an interference with rights *in rem* do in fact arise in response to and serve to vindicate rights *in rem*.

This is most obviously so in respect of common law and equitable claims to vindicate property rights. The existence at common law of the right to recaption of an asset shows that it is not *analytically necessary* in every case for a right *in rem* to generate an *in personam* sanctioning right for the right *in rem* to be vindicated. Since the claimant's focus in a case of recaption is directly against the asset itself, there is no need for an *in personam* sanctioning obligation. It is, however, also the case at common law that in many circumstances, a sanctioning right *in personam* arises in order to deal with an interference with the claimant's asset and hence his or her right *in rem*. This is most clearly so in the case of the torts of trespass, detinue and conversion. It can accurately be said therefore that the common law provides no direct claim to enforce and protect rights *in rem*.

A claimant holding an equitable property right may, however, unlike in the common law, seek directly to enforce that right. In substance, the claimant asks the court to declare his or her equitable ownership of the identified asset.[59] Thus, for example, in *Macmillan Inc v Bishopsgate Investment Trust plc (No 3)*,[60] the claimant effectively asked the court to declare that the shares which Rupert Maxwell caused to be transferred to Berlitz belonged in equity to it and that Berlitz as transferee but not bona fide purchaser thus held the shares on trust for it. Such a claim, the equivalent of a *rei vindicatio* in classical Roman Law,[61] is based upon the claimant's equitable proprietary entitlement to the asset in the defendant's hands and will succeed without proof of fault. It is, in a functional sense, a remedy that provides for performance of the content of the right *in rem*. The declaration of equitable ownership is, however, inert.[62] In order to recover

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58 See J Penner, *The Idea of Property in Law* (Clarendon, Oxford, 1997) p 31.

59 See *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] AC 669, 707 per Lord Browne-Wilkinson; also P Birks, "Property and Unjust Enrichment: Categorical Truths" [1997] NZ L Rev 623, 650; P Birks, "Personal Property: Proprietary Rights and Remedies" (2000) 11 King's College LJ 1, 4-5; M McInnes, "Knowing Receipt and the Protection of Trust Property: *Banton v CIBC*" (2002) 81 Can Bar Rev 171, 176–177.

60 [1996] 1 WLR 387 (CA).

61 See B Nicholas, *An Introduction to Roman Law* (Clarendon, Oxford, 1962) pp 125–128; W Buckland, *A Textbook of Roman Law from Augustus to Justinian* (3rd ed rev by P Stein, CUP, Cambridge, 1963) p 675;F Schulz, *Classical Roman Law* (Clarendon, Oxford, 1951) pp 368–372.

62 See P Birks, "Property and Unjust Enrichment: Categorical Truths" [1997] NZ L Rev 623, 656; P Birks, "Property, Unjust Enrichment, and Tracing" (2001) 54 CLP 231, 250.

the asset itself and thus fully vindicate his property right, a claimant also needs a right as against the defendant to have the defendant transfer the asset to him or her. This right, which is a right *in personam* distinct from and additional to the right *in rem*, is accordingly the mechanism by which the particular defendant's interference with the claimant's right *in rem* is sanctioned.

The next important analytical question is: what is the event that gives rise to the *in personam* sanctioning right? We can immediately reject any suggestion that the event is the order of the court. The court's order is remedial only in the weakest possible sense.[63] It reflects a pre-existing right that arose at the moment of the interference and therefore well before the litigation ever began. This would be true, moreover, even if the court were not prepared to order the transfer of the particular asset, but instead ordered the defendant to pay a sum of money. It is important not to infer from the pecuniary nature of the award that the award is in response to some wrongdoing. It is perfectly rational for a system of law to convert all obligations into pecuniary form at the point of judgment. In Roman law, this was referred to as the principle of *condemnatio pecuniaria*.[64] As we have already noted, the common account operates also in exactly this manner – a performance duty is converted into a monetary order.

The remedy, whether in specie or in pecuniary form, reflects and fulfils a pre-existing right. The *in personam* duty to transfer the asset is and must be a response to the claimant's right *in rem*. This conclusion rests upon three considerations.

First, the existence of the duty to transfer the asset is intelligible only in terms of the pre-existing right *in rem*. Where, as with the *rei vindicatio*, the claimant's case rests on his right *in rem*, the only justification or explanation of the claimant's right to have the asset transferred to him or her is that right *in rem*. This is manifested in the definition of those entitled to bring a claim in conversion in terms of those with either actual possession or the right to possess. Possession is central to the common law concept of title to chattels.[65] The claimant is entitled to the asset precisely because it is his. This point can also be demonstrated in a different way. As a possessor, a defendant has a form of property right that is good against all except the rightful owner.[66] Indeed, in some circumstances possession becomes a property right good against all including the rightful owner. Thus, for example, in *Armory v Delamirie*,[67] Pratt CJ said: "[T]he finder of a jewel, though he does not by such finding acquire an absolute property or ownership, yet he has such a property as will enable him to keep it against all but the rightful owner ..." The only reason, therefore, for imposing a duty on the defendant to transfer the asset, thereby overreaching his possessory right, is

63 See P Birks, "Rights, Wrongs, Remedies" (2000) 20 OJLS 1, 15.

64 See H Jolowicz, *Historical Introduction to the Study of Roman Law* (Cambridge University Press, Cambridge, 1961) pp 210–212, 220–221.

65 See A Honore, "Ownership" in A Guest (ed), *Oxford Essays in Jurisprudence* (OUP, Oxford, 1961) Ch V, p 113; C Rose, "Possession as the Origin of Property" (1985–1986) 52 Univ Chicago L Rev 73.

66 See *J A Pye (Oxford) Ltd v Graham* [2003] 1 AC 419.

67 (1772) 1 Strange 505 (see W Rogers, *Winfield and Jolowicz on Tort* (15th ed, Sweet & Maxwell, London, 1998) p 600; A Dugdale, *Clerk & Lindsell on Torts* (18th ed, Sweet & Maxwell, 2000) p 749.

that the claimant is indeed the owner and thus has a superior entitlement. The claimant's right *in rem* is, therefore, both a necessary and sufficient explanation of the duty to transfer the asset.

However, Professor Birks suggested that the event that gives rise to this right is "the receipt of an asset belonging to another".[68] While the description of the event as the acquisition of an asset belonging to another is not inappropriate, and may indeed be more graphic, it is nevertheless plain that such an event is not intelligible without the reference to the right *in rem*. The fundamental legally relevant element of this event is that the thing received is one that belongs to another. While the receipt of the asset is that matter that brings the claimant to court, the receipt itself is legally significant only because another person owns the asset received. The mere receipt of an asset is incapable of generating any rights to recovery and it is only where the receipt infringes the claimant's persisting right *in rem* that there is anything for the law to respond to. Notwithstanding this, however, Birks insisted that this event must be located in his miscellaneous fourth category. This is so, it seems, primarily as a result of Birks's commitment to the proposition that rights *in rem* cannot be a category of event.[69] While in principle one could continue to insist that the event must still be located in the miscellaneous fourth category, such is the prevalence of property rights in the legal system that this would not only greatly distend the miscellaneous category, but it would also seem to run counter to the very impetus for taxonomy: the identification from the mass of individual genera and species.

Secondly, the identification of the event as the claimant's right *in rem* is consistent with and gives effect to the idea that the duty to transfer the asset is consequential upon the *rei vindicatio*. The claimant's claim, it must be reiterated, is based upon his right *in rem* in the asset and serves to vindicate that right. In essence, what the claimant seeks is the return of his property. The additional right *in personam* to a transfer of the asset is merely the perfection or realization of his claim to recover his asset. The right *in personam* is only necessary because, as indicated above, the right *in rem* is inert and can be made to bear directly on the particular defendant only through the imposition of a further personal obligation. Moreover, the claimant's right *in rem* is also the basis upon which the courts conceive themselves to be acting. Thus, for example, in *Macmillan Inc v Bishopsgate Investment Trust plc (No 3)*, Millett J, as he then was, said: "any liability of the defendants to restore the shares or their proceeds to Macmillan or to pay compensation for their failure to do so must be based upon Macmillan's continuing ownership of the shares."[70]

Thirdly, the event that gives rise to the duty to transfer the asset must be the claimant's right *in rem* because there is simply no other event in play that would entitle the claimant to the delivery up of the asset. Almost by definition the event cannot be in the category of consent. The claimant's case arises as a result of a

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68 See P Birks, "Property and Unjust Enrichment: Categorical Truths" [1997] NZ L Rev 623, 657; P Birks, "Property, Unjust Enrichment, and Tracing" (2001) 54 CLP 231, 251; P Birks, "Unjust Enrichment and Wrongful Enrichment" (2001) 79 Texas L Rev 1767, 1775.

69 See P Birks, "Property, Unjust Enrichment, and Tracing" (2001) 54 CLP 231, 245.

70 [1996] 3 All ER 747, 758.

non-consensual transfer of the asset. Nor, however, is the event found in the wrong of interference with the asset. While, of course, it is the interference that brings the claimant into court,[71] the mere receipt of the asset by the defendant is not of itself wrongful.[72] It is thus not surprising that the claimant is not required to prove fault or wrongdoing as a pre-condition to establishing the defendant's duty to transfer the asset. This conclusion is, moreover, borne out by a comparison with the recaption of goods.[73] Here, the claimant does not need the court's help to recover the asset, but instead relies directly on his property right. Thus, for example, if the claimant sees his bicycle, which has been taken from him, leaning against a wall in the High Street, he is able fully to vindicate his right *in rem* in the bicycle by simply re-taking it. The act of re-taking, and the duty imposed on the defendant to transfer the bicycle in cases where it cannot be simply re-taken, are functionally equivalent. Both serve to fulfil the claimant's right *in rem* by restoring the asset to the claimant. This equivalence suggests strongly that, at an analytical level, the duty imposed to transfer the asset must arise as a consequence of the claimant's right in rem. It is, in essence, a duty to perform the content of the right *in rem* vis-à-vis the claimant.

Locating the event in the category of unjust enrichment, rather than in consent or wrongdoing, seems more plausible, though ultimately this possibility must also be rejected. Although the event could be made to fit within the notion of unjust enrichment, principally by treating the notion of "enrichment" as satisfied by the mere factual receipt of the asset, as Birks notes, it is neither desirable nor plausible to do so.[74] One consequence of identifying the event as unjust enrichment would be to subject the claimant's rights to the defence of change of position. The consequence is that merely because of the inert nature of rights *in rem*, which requires the imposition of a consequential duty to transfer the asset, the rights *in rem* would be subjected to the inherent weakness of all rights consequent upon unjust enrichment. Not only is this in fact not the law, but it would also represent an undesirable weakening of the security and enforceability of property rights.

An analysis of the duty to transfer the asset in terms of unjust enrichment must

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71 There is an important analytical distinction between the *possibility* of analysing the claimant's case as one for redress for a wrong and the necessity of doing so. In cases where the law will give effect directly to the primary right, there is no need for a wrongs analysis. Perhaps the clearest example of this is the case of contract. The right to specific performance is not a response to the wrong of breach of contract, but is the fulfilment of the right to performance. Thus, specific performance is available where there is no breach: *Hashim v Zenab* [1960] AC 316 (PC). See also *Semelhago v Paramadevan* [1996] 2 SCR 415 (performance secured by an award of money as a substitute. The same point can be seen from my earlier analysis of common account. See further S Smith, "Substitutionary Damages" to be published in C Rickett (ed), *Justifying Remedies in Private Law* (Hart Publishing, Oxford, 2008).

72 See P Birks, "Property and Unjust Enrichment: Categorical Truths" [1997] NZ L Rev 623, 657; P Birks, "Property, Unjust Enrichment, and Tracing" (2001) 54 CLP 231, 251.

73 See *In re Eastgate* [1905] 1 KB 465; *Tilley v Bowman* [1910] 1 KB 745.

74 See P Birks, "Property and Unjust Enrichment: Categorical Truths" [1997] NZ L Rev 623, 657–658.

also now be regarded as having been ruled out as a matter of precedent by the decision of the House of Lords in *Foskett v McKeown*.[75] The case concerned a claim to money stolen by a trustee to acquire, in part, an insurance policy. The House of Lords held that the beneficiaries of the trust were entitled to a beneficial interest in the proceeds of the policy in the same proportion as the trust money that had been used to acquire it. For present purposes, the importance of the case is that their Lordships treated the beneficiaries' rights in the proceeds of the policy as arising, not from unjust enrichment, but from the beneficiaries' rights in the original trust money. Lord Browne-Wilkinson's view was that: "The only trusts at issue are the express trusts of the purchasers' trust deed. Under those express trusts the purchasers were entitled to the equitable interests in the original moneys. Like any other equitable proprietary interest, those equitable proprietary interests ... now exist in any other property which, in law, now represents the original trust assets."[76] These comments leave little room for any conclusion other than that the event from which the duty to transfer arises following a successful *vindicatio* is the claimant's property rights.

C. *Protecting Proprietary Rights at Common Law and in Equity*

We can compare the manner in which protection of property rights is carried through by common law and in equity, thus:

1. At common law, the interference with a right *in rem* is in substance sanctioned by an *in personam* obligation to pay compensation.
2. However, because the common law does not know the *rei vindicatio* (thus the claimant cannot be heard in court to rely directly on his right *in rem*) (although historically detinue may have had this role[77]), the common law has come to interpose an *in personam* obligation of non-interference with the claimant's right *in rem*. The *in personam* obligation to pay compensation for loss is then formally referable to that obligation (but indirectly referable to the right *in rem*). (In the case of the historical form/role of detinue, it was a claim directly to vindicate the right *in rem*, which was realised by an *in personam* duty to deliver up the asset or to pay the money equivalent of the asset (but not the value of the loss to the claimant – which is what conversion does). Conversion (through trespass on the case) came to dominate the field, thus "hiding" detinue's role as a common law *rei vindicatio*.)
3. The existence of the *in personam* duty of non-interference is intelligible only in terms of the right *in rem*:
   i) the *in personam* duty of non-interference is necessarily dependent upon the right *in rem* – one only has a duty not to interfere because

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75 [2001] 1 AC 102. Professor Birks acknowledges this in "Property, Unjust Enrichment, and Tracing" (2001) 54 CLP 231, and in "Receipt" in P Birks and A Pretto (eds), *Breach of Trust* (Hart, Oxford, 2002) Ch 7; see also P Millett, "Proprietary Restitution" in S Degeling and J Edelman, *Equity in Commercial Law* (Thomson, Sydney, 2005) Ch 12.

76 [2001] 1 AC 102, 108.

77 For fuller discussion, see RB Grantham and CEF Rickett, "Property Rights as a Legally Significant Event" [2003] CLJ 717, 735–737.

of the claimant's ownership;

ii) the right *in rem* is an obligation mediated through the *res* and binds the whole world rather than individuals. The interference with the right, however, can only be by a particular individual. Thus, the sanctioning right can only be by way of an *in personam* obligation, and this is so for both vindication and loss claims (both detinue and conversion).

4. The right to compensation for loss is thus a response:
   - formally, to the breach of the *in personam* right to non-interference;
   - in substance, to the interference with the right *in rem*.
5. The *in personam* rights generated from the right *in rem* can be expressed in terms of the realization, performance or sanctioning of the right – ie: how (by what mechanism) is a right held against the world (but no-one in particular) made to apply to a particular individual? The answer depends in large measure on the nature of the mechanisms for realization that are available:

   i) Where the system of law will directly realise the right *in rem*, that right is made to bite on the individual by an *in personam* order to deliver up the asset (detinue at common law; and a direct order in equity);

   ii) Where the system does not directly realise the right *in rem*, that right is made to bite on the individual by way of an *in personam* duty of non-interference (conversion at common law; and knowing receipt in equity).

D. *Understanding Tracing and Equity's* Rei Vindicatio

Our understanding of the manner in which property rights are properly recognized and protected is further complicated of course by the fact that both common law and equity recognise rights *in rem* in respect of assets substituted for the original assets in issue, through the doctrine of tracing. Analytically, the key question in the context of tracing is, which right does tracing transmit from asset 1 (the original) to asset 2 (the substitute)? There are two possible answers. First, it might be the original right *in rem* itself. That right *in rem* thus detaches from asset 1 and goes to asset 2, thus enabling the claimant to say of asset 2 "that thing is mine!" just as he could have in respect of asset 1. Alternatively, it might be the right to have the asset delivered that is transmitted to asset 2. The claimant's *in personam* right to restoration of the asset (asset 1) is transferred to asset 2. The first answer appears to be more consistent with the general understanding of what occurs in tracing and is consistent with the equitable doctrine of overreaching.

Professor Birks argued[78] that all rights born of tracing are responses to the legal

[78] Birks's view has been supported since by others (A Burrows, "Proprietary Restitution: Unmasking Unjust Enrichment" (2001) 117 LQR 412; R Chambers, "Tracing and Unjust Enrichment" in J Neyers, M McInnnes and S Pittel (eds), *Understanding Unjust Enrichment* (Hart, Oxford, 2004) Ch 11. Cf G Virgo, "Vindicating Vindication: *Foskett v McKeown* Reviewed" in A Hudson (ed), *New Perspectives on Property Law, Obligations and Restitution* (Cavendish, London, 2004)

event of unjust enrichment. This would require that the right *in rem* in asset 2 must be a new right (right in rem^2). If, however, the right is the same right, the event generating the right *in rem* in asset 2 is the same event as gave rise to the right *in rem* in asset 1. The analysis in the first answer offered in the previous paragraph of this paper is of course silent on whether the right *in rem* in asset 2 is the same right as in asset 1 or whether analytically it is a new right. In fact, it is quite possible to concede that the right is a new right without having to adopt Birks's unjust enrichment position. The crucial point, if it is a new right, is: what is the event to which it is a response? Birks says it is a new right because of the "break" in the chain – the old right is replaced with a power *in rem* in the claimant to vest a title in the substituted asset in himself. The event, says Birks, is therefore unjust enrichment. Although the new asset 2 never belonged to the claimant, it was obtained at the claimant's expense by using his asset 1; and the unjust factor was absence of consent.[79]

The equitable doctrine of overreaching suggests, however, that it is the same right. Overreaching allows and explains how an authorised disposition of a trust asset by the trustee extinguishes the beneficiary's equitable interest in the asset (asset 1), and how the beneficiary acquires an equitable interest in whatever asset (asset 2) was acquired in substitution for the first asset. This must involve a transfer of the same right *in rem* in asset 1 to asset 2. If it does not, then this would mean analytically that each new asset acquired by the trust in substitution for an existing asset would be held on a new separate trust. This is problematic in that: (i) it completely destroys the unity of the trust (which is highly counter-institutive); and (ii) it would fundamentally undermine the perpetuity rule – perpetuity would run differently for each new asset/trust, meaning the "trust" could go on forever.

A complete picture of equity's protection of property rights in asset substitution contexts requires further reference to the relationship between equity's *rei vindicatio* and its possible realisation of rights *in rem* by means of a lien.

E. *Realising Rights* in Rem *by a Lien*

In addition to an infringement of the claimant's equitable property rights, a substitution of assets also of course constitutes wrongful conduct by the trustee (being a breach of his primary duty of strict compliance with the terms of the trust, in particular the duty not to make unauthorized investments). This gives rise to an *in personam* accounting obligation to restore the trust fund, for which a lien (after identification of the substitute asset by the exercise of tracing) is one possible response, in addition to a compensatory response for the loss caused by the wrongful conduct. This is the point made forcefully by Lord Millett in *Foskett v McKeown* in an important paragraph in his speech.[80] If the claimant chooses a lien instead of compensation, he is in effect affirming the unauthorized nature of

Ch 10. For further discussion, see L Smith, "Unravelling Proprietary Restitution" (2004) 40 Can Bus LJ 317; cf most recently L Smith, "Tracing" in A Burrows and Lord Rodger of Earlsferry (eds), *Mapping the Law* (Oxford University Press, Oxford, 2006) Ch 7).

79 See P Birks, "Property, Unjust Enrichment, and Tracing" (2001) 54 CLP 231, 246.

80 [2001] 1 AC 102, 130.

the investment and is seeking a restoration of the trust fund. The claimant's claim is nonetheless a personal claim, and the lien is available to secure the trustee's personal obligation correlative to the claimant's personal right. The claimant beneficiary is given the advantage of choosing a lien over pure compensation simply because he or she is equity's special concern and because of the need to maintain the integrity of the trust relationship.

One alternative analysis of the option of a lien, put forward by Professor Birks, is that it is a proprietary remedy alternative to the *rei vindicatio*. The claimant asserts his subsisting equitable property right, but that ownership is realized not via a declaration of ownership (and re-conveyance), but by the imposition of an obligation to repay the value of asset 1.[81] The mere fact that the claimant's claim is one based on his property right does not entail that the realisation of that right must be by way of a declaration of ownership – even in Roman law, the *rei vindicatio* was subject to the alternative of "substitute compensation" in the form of a *condemnatio pecuniaria*. That the choice between the alternatives is the claimant's own reflects the claimant's position as equity's special concern. This analysis is entirely consistent with the idea of tracing as a neutral process, silent as to both the claim and the remedy. However, Birks's alternative view cannot be correct, since the *rei vindicatio* is concerned with the substitution of the asset, and not with the value of the asset.[82] It must also to be understood that the claimant is not simply electing the remedy, but rather the claim itself (although this is not always clear in practice, conceptually it must be the case).

A different point is made by Professor James Penner, who argues that by bringing a personal claim for breach of trust, the beneficiary in effect falsifies the account and thereby disowns any interest in the proceeds of the falsified account, and thus should have no right to claim a lien over them or any other property in the hands of the trustee.[83] He surmises from what he sees as this conceptual difficulty an explanation of the grant of a lien as follows: the beneficiary adopts the unauthorized transaction as a secured loan to the trustee, secured against the substitute property, and the lien in effect satisfies the beneficiary's personal claim for repayment of that loan. Of course, Penner is correct in his point that the beneficiary has in effect falsified the account, but it is unnecessary to go on from there and attempt to construct a justification for equity's recognition of a lien as a possible remedy that takes us beyond the simple fact that equity has long recognized the position of the beneficiary as deserving of special protection to ensure the trustee's performance of his personal duty.[84]

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81 See P Birks "Personal Property: Proprietary Rights and Remedies" (2000) 11 King's College LJ 1, 5.

82 Ross Grantham and I made this error in our discussion of tracing in *Enrichment and Restitution in New Zealand* (Hart, Oxford, 2000) p 439.

83 See "Duty and Liability in Respect of Funds" in J Lowry and L Mistelis (eds) *Commercial Law: Perspectives and Practice* (Lexis Nexis Butterworths, London, 2006) pp 218–219.

84 See, for a very clear example of this beneficiary-friendly attitude of equity, *Scott v Scott* (1963) 109 CLR 649 (HCA).

VIII. Conclusion

Equity responds to breaches of trust in a range of functional ways. It shows a keen concern that trustees perform their obligations. At a personal level, the mechanism of common account is designed to ensure this. In the context of a beneficiary right *in rem*, the equitable version of the Roman Law's *rei vindicatio*, supplemented by the peculiar reach of tracing, allows for the equivalent of performance. Equity also provides for reparative compensation, notably in the form of an account for wilful default, and perhaps in a more modern guise known as equitable compensation. Equity has long provided for disgorgement of gain made in breach of trust and other duties, consistent with the other-regarding nature of the duties in focus. Equity as applied in New South Wales and several other errant jurisdictions has flirted with punitive monetary awards, a state of affairs without any solid foundation in private law theory. An awareness of the different functions of different remedies, alongside an awareness of the content of different duties (both primary and secondary), ensures a coherent and rational understanding of this important area of theory and practice. Last but not least, the tendency to provide proprietary relief where necessary to achieve the functional objective in such a way as recognizes the special nature of equity and its primary players is well noted in its disgorgement-focused responses and in its willingness not only to supply the equivalent of a *rei vindicatio* but also to aid the beneficiary who suffers a misconduct by the trustee's misapplication of trust funds to have a proprietary response to the personal wrong.