Memorandum

To: Mr. Julius Heydon

From: Timothy Davis

Date: 27/11/2009

Re: Payment Advice

Dear Julius,

Pursuant to your instructions, I have considered the three payments you made in 2008 and analyzed the relevant legal issues as you have requested.

All supporting material leading to these conclusions is attached and if you have any further questions or inquiries please don’t hesitate to contact me.

Yours Faithfully,

Timothy Davis

1. **Issues**

2. **Issue 1**

2.1 *Unsecured Debt or Trust*

2.2 It is evident that the monies you have provided to Ernan have been offered on the basis that you intend for them to benefit your mother as a creditor. An important factor in providing this money to Ernan was that the monies were to be segregated into a separate bank account in his name.

2.3 This segregation has important legal ramifications in determining whether it is possible for you to enforce Ernan to pay the monies you have provided him to your mother. Most noticeably, in *G & M Aldridge Pty Ltd v Walsh*[1] Phillips JA commented that where money is owed to a creditor on the basis that the debt is to be satisfied out an general assets of the debtor, the relationship is one of debt only and cannot amount to a trust because there is no property set aside by the debtor which the creditor could require to be applied in satisfaction of the obligation owed.

2.4 Accordingly, the monies you have loaned to Ernan have been provided – and set aside – with the specific intention of satisfying the debt owed to your mother, as a creditor, from Ernan's segregated account.

2.5 In *Re Australian Elizabethan Theatre Trust*[2], Gummow J indicated that monies which are received on the basis that they are to be kept distinctly separate from a person's own accounts, and where the money is available only to satisfy a specific purpose which that person owes to a third person – then that person holds the money as trustee for that third person only to the extent to which a present right exists regarding the payment of those monies by the lender.

2.6 The absence of the word 'trust' in your instructions to Ernan may provide a plausible argument that a trust was not in fact your intention. In *Mead v Smith*[3] it was established that a trust will not be imposed by a Court when it is not sufficiently certain that the intention and language of the settlor was for a trust to be created.

2.7 In *Jeesup v Queensland Housing Commission,* the absent use of the word 'trust' and the provision of a payment into a nominated account without any stipulations regarding how the money was to be used were ruled as a strong indication that a trust was not intended. In contrast, in *Australasian Conference Assn Ltd v Mainline Constructions Pty Ltd*[4] it was commented that where money is lent by a donor to a donee with the mutual intention of it not forming part of the donees assets, but rather to be used exclusively for a specific purpose - then in the absence of any indication to suggest otherwise the arrangement will form a fiduciary obligation and a trust.

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[1] *G & M Aldridge Pty Ltd v Walsh* [1999] 3 VR; 601; (1999) 169 ALR 710; 154 FLR 24; 33 ACSR 456 at 550 per Phillips JA.
[2] *Re Australian Elizabethan Theatre Trust* (1991) 102 ALR 681 at 689 per Gummow J.
[3] *Mead v Smith* [1924] 1 Ch 88.
[4] *Australasian Conference Assn Ltd v Mainline Constructiosn Pty Ltd* (1978) 141 CLR 335 at 353; 22 ALR 1 at 18 per Gibbs ACJ.

2.8 Additionally, if the benefit conferred is intended to be used solely in favour a third party, then it is likely that a trust will arise and any property left in remainder after the terms of the trust are fulfilled with reside on resulting trust for the settlor.[5]

2.9 *Quistclose Trust*

2.10 A transaction which is encompassed within the details outlined in 2.7 has been explained in detail via a two-trust mechanism in *Barclays Bank Ltd v Quistclose Investments Ltd*[6]. In this case, the Court stated that a primary trust is formed to carry out a lender's stipulated instructions as to how the loaned monies are to be used coupled with a secondary trust which would take effect if the primary trust failed. Modern law has since favored a singular trust scenario created through an express[7] or resulting trust[8] in favour of, and protecting the intention of, the settlor.

2.11 The degree to which an express or resulting trust arises must be determined through intention, and if the intention is to benefit a third party through some contractual arrangement between the settlor and the trustee – Gummow J commented in *Re Australian Elizabethan Theatre Trust*[9] that the mutual intention of the settlor and the trustee should be examined in combination with 'the essence'[10] of their bargain.

2.12 In your circumstances, it is clear from the language you have used that you intend to dispose of your property for the benefit of your mother, and a strong argument exists that the use of the words 'must use this loan' manifestly establishes this directive. Furthermore, it is contended that both yours and Ernan's mutual intention was to immediately benefit your mother with the monies lent - suggesting that no beneficial interest was ever made in favour of Ernan directly. Such a mutual intention gives rise to a contractual agreement which provides, by implication, that Ernan would only use the monies to satisfy the debt with your mother.[11]

2.13 Typically when dealing with third parties, use of precatory language which does not definitively establish whether the transfer of property is to benefit the donee or some other third party can cause problems as to whether legal or equitable obligations were in fact directed to the third party. In *Re Australian Elizabethan Theatre Trust*[12], the Court commented that if the facts suggest that no contractual obligation existed between the borrower and the lender to pay third party creditors, then there is no concurrent intention to create a trust in their favour – instead, the borrower would hold the monies as a trustee of an express trust for the lender subject to the trust declaration to use the funds to pay creditors.

2.14 In your case we assume, unless you instruct otherwise, that you contractually agreed with Ernan to hold the loan until it was paid to Livina as a third party and that no other plausible use of the monies could occur. On this basis, and using the logic presented in 2.13, it is contended that an express *Quistclose* trust has arisen from the transfer of your property to

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[5] *Williams v Hopkins* [1950] Ch 204.
[6] *Barclays Bank Ltd v Quistclose Investments Ltd* [1970] AC 567.
[7] *Re Australian Elizabethan Theatre Trust* (1991) 102 ALR 681 at 689 per Gummow J.
[8] *Twinsectra Ltd v Yardley* [2002] All ER 377.
[9] Ibid 7 at 693.
[10] Ibid 6 at 580.
[11] In *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd* (1998) 165 107, Mason CJ and Wilson comment that in resolving the uncertainty as to third-party contracts in trusts, the Courts will examine the nature of the transaction and the relationship between the parties and their inferred intention which, it is contended in this case, is clearly to benefit Livina.
[12] *Re Australian Elizabethan Theatre Trust* (1991) 102 ALR 681 at 694 per Gummow J.

Ernan in favour of Livina. The loan moneys advanced by you to Ernan were segregated from his personal accounts and you clearly stipulated your specific purpose and intention on the day the loan agreement formed. As a result, the certainties of subject matter and object have been satisfied through such conduct.

2.15 If Ernan purports to use the money for any other purpose than that which you have directed in your instructions, then he is exceeding his authorized power and is in breach of his obligations as trustee. Any such exercise in this regard will be void and render Ernan liable under trust law and in breach of contract at common law.[13] The benefits to you as the lender of the monies under an express trust form the moment that the loan contract is created, and your security interest is in existence when the contract between you and Ernan is formed.

3. **Issue 2**

3.1 *Third Party Enforcement*

3.2 On the basis of facts you have provided, an express *Quistclose* trust has been created in favour of Livina as a beneficiary under this trust. Any beneficiary can institute proceedings to enforce the performance a trust whether their interest is vested or contingent.[14]

3.3 As a beneficiary, this infers that Livina is able to enforce performance of the trust against the trustee to fulfill the obligations stipulated as per your stated instructions. Accordingly, since it is assumed that Livina is *sui juris* and entitled to the trust property, she is able enforce the trustee to transfer the trust property to her. If the trust property was misappropriated by Ernan in a manner not authorized by yourself as the settlor, then Livina has access to the relevant remedies of an action for due administration of the trust estate, and if required, tracing the trust property and claiming priority to the trustees ordinary creditors.[15]

3.4 If the contention arises that Livina was not considered a beneficiary under the trust, the decision in *General Communications Ltd v Development Finance Corp of New Zealand*[16] suggests where the lender has a distinct interest in ensuring that the money being lent is to favour the creditor(s) of the borrower, the borrower is obliged at the whim of the lender to make these payments. If the creditor(s) are notified of these arrangements, then this can amount to an equitable assignment of the lenders rights against the borrower thereby giving the creditors an equitable interest in place of the lender.

3.5 In this regard and on the basis that Livina was aware of the trust formation, it is arguable that you have a 'distinct interest' in ensuring that your mother receives the monies intended for her in order to ensure that your family relationship remains amicable.

4. **Issue 3**

4.1 From the facts provided, it is suggested that you transferred $1 million dollars to Kendra who then deposited the monies into a separate bank account. Subsequently, you then agreed that the money was to be used solely and exclusively to purchase a dwelling house. If this is the case, it is possible that the relationship formed between you and Kendra is one of mere

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[13] *Baston v Gideon Investments Pty Ltd (in liq)* (2000) 35 ACSR 466 at 473.
[14] *Spellson v George* (1987) 11 NSWLR 300 at 316.
[15] *Re Blackpool Motor Card Co Ltd* [1901] 1 Ch 77 at 85.
[16] *General Communications Ltd v Development Finance Corp of New Zealand Ltd* [1990] 3 NZLR 406 at 422-23.

debtor and creditor if the transfer was absolute and a lack of sufficient evidence exists which suggest that your intention was to create a trust over money in that separate account.[17]

4.2 However, for the basis of this advice, it is assumed that you did not intend for absolute equitable title to transfer to Kendra unless she fulfilled your instructions set out in the contractual agreement formed between you both at the time of the loan transfer. Whether or not an express trust has been created needs to be again determined by reference to your intention, as stated in 2.6 and 2.7 above. The question in every case always rests on whether the parties intended for the monies to be at the free disposal of the recipient.[18]

4.3 Since the monies have been lent by you to Kendra, and it is clear from the contractual agreement that your subsequent mutual intentions were that the monies were not to form part of Kendra's general assets but rather be used 'solely and exclusively' for a specific purpose, then an implied stipulation exists – in the absence of evidence to the contrary – that if that purposes fails, the monies will be repaid. It is contended this arrangement gives rises to a fiduciary obligation and a trust[19] – made more apparent by the agreement 'not requiring Kendra to repay any monies she expended on the dwelling house'. Such a statement provides that any monies which are not spent on the dwelling house are to revert back to you as the lender.

4.4 As stated in 2.10 and 2.11, the degree to which an express or resulting trust arises must be determined through the intention of the settlor. This intention can be inferred from the language employed during contractual formation and the relevant circumstances of the relationship between the parties.[20] Subject to any contractual agreement, it is evident from the language used that you intended for the Kendra to immediately hold the monies borrowed on trust for you as the lender – subject to a mandate to use the funds for your stipulated purpose.[21]

4.5 As a result, it is contended that an express *Quistclose* has formed from the monies lent to Kendra as your intention was never to transfer equitable title to her unless she fulfilled your specific requirement to only purchase a dwelling house. The monies which you lent to Kendra had a strict condition of fulfillment attached, and it is assumed that Kendra accepted the money with the prior knowledge of this restriction.[22] Accordingly, if Kendra misuses the funds for any other purpose than as you have directed – she would be liable for breach of her fiduciary obligations as trustee, and in breach of the contract you created at common law.

4.6 While it is possible that a Court may contend that a lack of intention in this situation forms a resulting trust[23] - it is argued, on the facts provided, that an express *Quistclose* trust is imposed from the outset of the loan contract when the monies were first transferred to Kendra as the certainties of intention, subject matter and object are satisfied.

4.7 If the trust is in existence at this point, then as the lender, you have a security interest before any plausible breach of contract. This is particularly important as the imposition of a resulting trust would form only after the loan monies have been advanced and misused – not

[17] *Re Fada (Aust) Ltd*; Ex parte Brown [1927] SASR 590.
[18] *In re Goldcorp Exchange Ltd* [1995] 1 AC 74.
[19] *Australasian Conference Assn Ltd v Mainline Constructions Pty Ltd* (1978) 141 CLR 335 at 353; 22 ALR 1 at 18 per Gibbs ACJ.
[20] *Walker v Corboy* (1990) 19 NSWLR 382.
[21] *Re Australian Elizabethan Theatre Trust* (1991) 102 ALR 681 at 693 per Gummow J.
[22] *General Communications Ltd v Development Finance Corp of New Zealand Ltd* [1990] 3 NZLR 406 at 433.
[23] *Twinsectra Ltd v Yardley* [2002] All ER 377.

before.[24] In contrast, an express trust would infer that Kendra bears a personal liability for any breach of the trust declaration in addition to reconstituting the trust fund back to its original state if the trust funds were used for any other purpose than as directed by the contract.

4.8 This is uniquely different to a resulting trust which infers that property 'springs back' to the beneficiary after the funds have been misused. For a resulting trust to form, you must have passed full equitable title to the Kendra from the outset for the monies to 'spring back' - or as Lord Millet suggests in *Twinsectra Ltd v Yardley*[25] - you must have retained equitable title in the monies from the beginning. If full equitable title was passed from the beginning, then such a contention is inconsistent with the ideology of monies being able to 'spring back'. Thus, it is contended that an express trust has formed in this situation in accordance with your intention.

5. **Issue 4**

5.1 You have stated that both you and PAYG agreed that your money was to be paid in to PAYG Client Prepayment Account for the specific purpose of conducting your funeral on your death. Subject to the terms of the contract, it is arguable that you have merely entered into a debtor and creditor relationship if the transfer of your monies was absolute and you had no intention of retaining any equitable title in your money.[26]

5.2 On the basis of the language used, it does not seem *prima facie* evident that your intention was for these funds to be held on trust when you first conferred them. The necessary appropriation of specific property to be held on trust must be accompanied by sufficient acts and words which show that you, as the creditor, intended the debtor to hold the property on trust.[27] Most noticeably, the word 'should' does not sufficiently indicate that a binding obligation existed on PAYG behalf to hold your funds on trust and it inherently provides for a level of discretion. Consequently, it is arguable that use of such language is precatory.

5.3 However, it is still possible that under your contract of purchase your monies are capable of forming a trust in the hands of the vendor. In *Re Kayford Ltd*[28] it was considered whether sums of monies paid by a purchaser under a contract for the sale of goods and services should be capable of being the subject of a trust in the hands of the vendor. The Court suggested[29] that the question required to be answered was whether the money in the bank account was held on trust for those who paid into it, or whether it formed part of the general assets of the company. It held that there was an intention by the company to ensure that monies sent by customers remained in their beneficial ownership and ruled a trust existed. Most noticeably the Court stated that

> *'the sender may create a trust by using appropriate words when he sends the money, or the company may do it by taking suitable steps on or before receiving the money. If either is done, the obligations in respect of the money are transformed from contract to property, from debt to trust'.*[30]

[24] *Twinsectra Ltd v Yardley* [2002] 2 AC 164, 187-193.
[25] *General Communications Ltd v Development Finance Corp of New Zealand Ltd* [1990] 3 NZLR 406 at 433.
[26] *Re Fada (Aust) Ltd*; Ex parte Brown [1927] SASR 590.
[27] Ibid
[28] *Re Kayford Ltd (in liq)* [1975] 1 WLR 279.
[29] *Re Kayford Ltd* [1975] 1 All ER 604 at 607.
[30] Ibid at 608.

5.4 The decision in *Re Kayford Ltd*[31] was clarified in *Re Goldcorp Exchange*[32] where the Privy Council stated[33] that it

> *'[w]as necessary to show that either a mutual intention existed that the monies should not fall into the general fund of a company's assets but should be applied only for a special purpose or that having originally been paid over without restriction the recipient has later constituted himself as a trustee of the money'.*

5.5 Both these cases can be contrasted with the decision in *Re Fada (Australia) Ltd*[34] were a company open a new bank account named 'Fada (Australia) Ltd Trust Account' to hold share application money. Piper J held that the payment of monies into this 'trust account' did not create any trust in favour of the applicants as the mere naming of the account was not sufficient enough to show an intention on the part of the company to declare itself a trustee.

5.6 The fact that your money was held within a 'Client Prepayment Account' with 'clients other monies' does suggest that PAYG may be holding your monies on trust. In *Hunter v Moss*[35] the Court held that if each part of trust property is indistinguishable from the rest – in this cash your prepayment – specific distribution is not required and will not cause a trust to fail. Despite this, it is contended that insufficient intention exists which can definitively clarify if this account was purposely separated to hold your monies on trust.

5.7 Accordingly, the lack of a mutual intention between both parties is *prima facie* evidence that your funeral monies were not meant to be held on trust on your behalf and consequently nothing specifically restricted the funds being used as part of PAYG general accounts. Payment into a separate bank account is, in the absence of contractual obligations, not a conclusive indication of an intention to create a trust,[36] and other indications of the debtor's intention to keep your monies separate from their other general assets must be provided before a sufficient intention presumption can arise.[37]

5.8 Consequently, it is contended – in the absence of evidence to the contrary – that your relationship with PAYG is merely one of debtor and creditor and you are bound by the contractual provisions you signed accordingly.

Word Count: 2,996

[31] *Re Kayford Ltd* [1975] 1 All ER 604 at 607
[32] *Re Goldcorp Exchange* [1995] 1 AC 74.
[33] Ibid at 100.
[34] *Re Fada (Australia) Ltd* [1927] SASR 590
[35] *Hunter v Moss* [1994] 3 All ER 214 affirmed in Australia in *White v Shortall* [2006] NSWSC 1379 via Thomas, Susan & Vicki Vann, *Trusts*, LexisNexis Butterworths, 2008, Pg 64
[36] Ibid.
[37] *OT Computers Ltd* (*in administration) v First National Tricity Finance Ltd* [2003] EWHC 1010 (Ch).

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