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Trusts

On the Horns of a Dilemma

R Fletcher★

Introduction

Illegality, as a concept, covers a multitude of sins and the differences that arise and the decisions of the courts are based on the principle of public policy. Under this heading it is the author's intention to examine the resulting trust, through the transfer of property in furtherance of a fraud, and illegality. Therefore, for the purpose of this discussion the Insolvency Act 1986 and the Insolvency (No.2) Act 1994 will not be examined.

The Resulting Trust

A resulting trust occurs through operation of law, *ie*, there is no need for any specific formalities for such a trust to arise, and the beneficial interest results back to the person who has provided the money. For example, A provides the finance and B purchases the property in his name. In this instance B would hold the property as trustee for A the beneficiary, under a resulting trust. Alternatively, a person about to start a risky business is concerned his debts may exceed his assets and decides to transfer his assets to his wife or son to render them safe from potential creditors. Complications have arisen in recent years when parties have used such a device to preserve property from creditors or for some other illegal purpose. It is usual in such circumstances to follow the equitable principles and let the loss lie where it falls.¹ However, as will be shown, the House of Lords has qualified this position and in given circumstances a person is now able to claim an interest in property, under a resulting trust, where there is no need to rely upon the illegal purpose.

Legal Title

A person is entitled to dispose of his property, *ie*, legal title, through the use of a trust and under the right circumstance such property would be protected should bankruptcy occur. Thus, the transferor would no longer have legal title to the property, it now belongs to the transferee. It is essential, for the transfer to be successful, that the transferor relinquishes any form of interest in the property, legal and equitable, if it is to be out of the reach of the transferor's creditors. If the transferor then wishes to claim the property back s/he has to prove the existence of a trust in his or her favour, as a beneficiary. Arguably, there was not a trust created in the first place, as this would defeat the objective of the transferor. For s/he must not hold any interest in the property to defeat the claims of the creditors. What the transferor is saying is: if I become

bankrupt then there was no trust. I transferred complete ownership of the property, legal and equitable. However, should bankruptcy not occur, then there is a trust and I now claim the beneficial interest. The substance of such agreements is self-evident – to commit a fraud against potential creditors.

Advancement

Such arrangements have arisen within marriages, families and partnerships. However, relationships break down, with the consequence of the transferee either claiming there was no trust, or the presumption of advancement is assumed due to the nature of the relationship between the parties. The principle of advancement assumes that a moral obligation exists between the parties due to the nature of their relationship. For example, when property is transferred from husband to wife, but not from wife to husband, and from father to child, the transfer is presumed to be an outright gift.

The courts, when dealing with such cases, have been asked to assist with claims in furtherance of an illegal transaction, whilst resolving the principles of equity and public policy. To demonstrate, a sample of cases will be examined, along with the judicial reasoning, to show how the law has developed and its current position.

The Dilemma

The case of *Tinker v Tinker* [1970] 1 All ER 540 upholds the principle that you cannot transfer property in such circumstances, and then attempt to reclaim it at a later date. This case involved a husband, who was self-employed, who was concerned that his business might fail and to protect his family home, on the advice of his solicitor, transferred the property into the name of his spouse. The business did not fail but his marriage did. The husband attempted to reclaim the home from his wife claiming she held it on trust for him absolutely. Lord Denning considered the facts and was of the opinion that the husband could not have it both ways: "So he is on the horns of a dilemma." The court held that the husband was unsuccessful in his claim. His evidence, according to the court, reinforced the presumption of advancement and the property was a gift to the wife.

The case of *Tinsley v Miligan* [1994] 1 AC 340, involved a relationship which did not give an automatic presumption of advancement. This case concerned Miss Milligan and Miss Tinsley, who were

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¹ The principle may be traced back to the dictum of Lord Eldon in *Muckleston v Brown* (1801) 6 Ves Jun 53, 69. This reflects the common law principle laid down by Lord Mansfield in *Holman v Johnson* (1775) 1 Cowp 341, 343, that "[no] Court will lend its aid to a man who founds his cause of action upon an immoral or illegal act".

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lovers. They purchased a home together which was registered in the sole name of Miss Tinsley with the intention that they should have equal shares in the property. The purpose for omitting Miss Milligan's name from the legal title was to allow her to make false claims for Housing Benefit. The couple parted company and Miss Milligan claimed that Miss Tinsley held the property on trust, in equal shares. Whilst Miss Tinsley attempted to exclude this claim by using the common law doctrine *ex turpi causa non oritur actio* (no right of action arises from a base cause) and through the equitable maxim "he who comes to equity must come with clean hands".

It was the submission of the appellant, Miss Tinsley, that:

"... the court will not give effect to an equitable interest arising from a transaction which is unlawful by reason of a claimant's unlawful purpose; and that accordingly the respondent was unable to establish any equitable interest in [the property], or defeat the appellant's claim to possession. This principle was said to be well recognised in a number of authorities; but reliance was placed in particular on *Gascoigne v Gascoigne* [1918] 1 K.B. 223 and *Tinker v Tinker* [1970] 1 All ER 540, both decisions of the Court of Appeal."²

However, by a bare majority, (Lord Keith and Lord Goff dissenting) Miss Milligan was successful in her claim based upon a resulting trust. The court found that Miss Milligan was able to establish her equitable interest without relying on the illegal transaction. This appears to be contrary to public policy: to assist a claim in furtherance of an illegal act. The property was purchased in the sole name of Miss Tinsley to allow Miss Milligan to make fraudulent claims for housing benefit, which were shared between the parties. Enochson³ is critical of their Lordships' decision and believes the illegal contract was relied upon to prove Miss Milligan's equitable interest under the resulting trust. Lord Browne-Wilkinson's reasoning was:

"... in cases where the presumption of advancement does not apply, a plaintiff can establish his equitable interest in the property without relying in any way on the underlying illegal transaction. In this case, the respondent ... simply pleaded the common intention that the property should belong to both of them and that she contributed to the purchase price: she claimed that in consequence the property belonged to them equally ... Therefore the respondent was not forced to rely on the illegality to prove her equitable interest."⁴

The law has developed, in such circumstances, along these guidelines. For example, in the case of *Tribe v Tribe* [1996] Ch 107 which concerned a plaintiff who was responsible for the repairs on two business leases, which had been served with notices for dilapidations requiring substantial work to be carried out. The plaintiff, faced with such demands, transferred his shares in the family company to his son, the defendant, to safeguard his assets. The illegality was self-evident: to deceive the plaintiff's creditors by creating the impression he had no means of meeting their demands. However, there was no need to

implement the scheme, any claims by the landlord were met, there was no need to rely upon the illegality. Thus, the father sought recovery of the shares from the son who resisted and raised the defence of illegality. The father's claim was successful on the basis that the illegal purpose had not been carried out, it remained unfulfilled no creditor had been deceived. Rose⁵ believes the decision in *Tribe* has clarified the law:

"by reformulating the rules on withdrawal [before the illegal act takes place] ... withdrawal can suppress the defence of illegality, allow an otherwise valid action in restitution to proceed, and provide an independent, policy-motivated ground for restitution."

However, although the father did not rely upon the illegal act he did set it up in readiness to proceed. Arguably, the decision of the Court of Appeal may be sending out the wrong message and should reconsider the issue when dealing with future claims.

Conclusion

The law has developed on an *ad hoc* basis which is not consistent with common law rules, *ie*, a claimant should not be assisted in the furtherance of an illegal act. Their Lordships have used various mental gymnastics to obtain, what they perceive, justice. It appears ludicrous to enforce an arrangement where the objective is to commit a fraud. Their Lordships have supported their decision(s) based upon the premise: the illegal act either did not occur or was not relied upon to enforce the trust. The law is supposed to reflect the morals of our society and distinguish right from wrong. It would appear from cases such as *Tinsley v Milligan* and *Tribe v Tribe* the distinction is not so clear.

² [1994] 1 AC 340, p 253 (c-d).

³ 1995, p 149.

⁴ At pp 371-372.

⁵ 1996, pp 389-390.