# Trusts

# Section 53(1)(c) and Sub-trusts

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*Suppose a legal owner (A) declares himself a trustee of property in favour of an intermediate trustee (B) who (in turn) declares himself a trustee for a beneficiary (C). Does the sub-trust in favour of C trigger a requirement of signed writing under s.53(1)(c) of the Law of Property Act 1925? That section, as we know, applies to dispositions of subsisting equitable interests so the question is whether a declaration of a sub-trust falls to be characterised as effecting a "disposition" of B's equitable interest under the head trust. Surprisingly, there is no easy answer to this question.*


Section 53(1)(c) of the Law of Property Act 1925 provides as follows:

> "a disposition of an equitable interest or trust subsisting at the time of the disposition, must be in writing signed by the person disposing of the same, or by his agent thereunto lawfully authorised in writing or by will."

Section 205 of the 1925 Act defines "disposition" so as to include a "conveyance" and "conveyance" is defined to include a release and every assurance of an interest in property. The effect of s.53(1)(c) is that a disposition of an equitable interest in an existing trust has to be in writing (not merely evidenced in writing) and either signed by the person making the disposition or their authorised agent. It appears that the reason for the requirement is so that there is no room for doubt as to the identity of the beneficiaries to whom the trustees owe their duties. As Lord Upjohn put it in *Vandervell v IRC*:[1]

> "the object of the section, as was the object of the old Statute of Frauds, is to prevent hidden oral transactions in equitable interests in fraud of those truly entitled, and making it difficult, if not impossible, for the trustees to ascertain who are in truth his beneficiaries."

The point here is that trustees would be exposed if beneficiaries could dispose of their beneficial interest by notifying the trustee orally of that change and then later renege, leaving the trustee without ready means of proof that the trustee had paid out to the correct beneficiary.

[1] [1967] 2 A.C. 291 at 311.

## The traditional view

A sub-trust will not attract any formality if the subject-matter involves pure personalty. An oral declaration of the sub-trust is sufficient. If, on the other hand, the subject-matter is land, the sub-trust will require to be evidenced in writing, complying with s.53(1)(b) of the Law of Property Act 1925, in order to be enforceable.

So far as the application of s.53(1)(c) is concerned, the orthodox view, until relatively recently, was that, where the intermediate trustee (B) is a bare trustee with no active duties to perform (i.e., where the only duty as trustee is to hold the property to the beneficiary's order), he will be treated as having effected a disposition of his interest with the consequence that he "drops out of the picture" and the head trustee (A) holds the property on trust directly for the sub-trust beneficiary (C). On this reasoning, the sub-trust attracts the requirement of writing under s.53(1)(c) of the Law of Property Act 1925 because B's equitable interest has effectively passed to C who can now directly enforce his rights against A.

If, on the other hand, B is an active trustee under the sub-trust (e.g., exercising a discretion as to the distribution of income or the payment of rent/profits among the beneficiaries who have no right to call for the capital), the declaration of the sub-trust is treated as genuine with the possibility of a creation of a chain of trusts where the intermediate holder is not a mere repository and has continuing obligations in relation to the interest of which he is a trustee. This was alluded to by Briggs J in *Re Lehman Brothers International (Europe):*[2]

> ". . . a trust may exist not merely between legal owner and ultimate beneficial owner, but at each stage of a chain between them, so that, for example, A may hold on trust for X, X on trust for Y and Y on trust for B. The only true trust of the property itself (i.e., of the legal rights) is that of A for X. At each lower stage in the chain, the intermediate trustee holds on trust only his interest in the property held on trust for him."

A number of early authorities supported these principles.[3] Lord Evershed MR in *Grey v IRC*[4] refers to the "getting rid of" a trust or equitable interest where the intermediate trustee is a bare trustee with no active duties to perform. Similarly, at first instance in *Grey*,[5] Upjohn J opined that, where a donor declares himself a trustee of an equitable interest for a donee, the legal effect is that, where the sub-trust is passive, the head trustee becomes trustee for the donee and the donor disappears from the picture.

## The modern view

The orthodox view has since been called into question. In *Nelson v Greening & Sykes (Builders) Ltd*,[6], the Court of Appeal concluded that the earlier authorities on "dropping out" were merely stating that the head trustee (A) might decide as a practical matter that it was more convenient to deal directly with the beneficiary of the sub-trust (C) rather than the

[2] [2010] EWHC 2914 (Ch), at [226].
[3] See, most notably, *Burgess v White* (1759) 1 Eden 177, *Grainge v Wilberforce* (1889) 5 T.L.R. 436; *Onslow v Wallis* (1849) 1 Mac. & G. 506 and *Re Lashmar* [1891] 1 Ch. 258.
[4] [1958] Ch. 690.
[5] [1958] Ch. 375, at 382.
[6] [2007] EWCA Civ 1358.

intermediate trustee (B).[7] But this did not mean that, as a matter of law, the intermediate trustee ceases to be a trustee.

On this view, a declaration of a sub-trust is not a disposition of the intermediate trustee's equitable interest and so does not need to satisfy s.53(1)(c). This is certainly the wider interpretation of the *Nelson* ruling which is also consistent with the view adopted by Lord Radcliffe in *Oughtred v IRC,*[8] which assumes that a bare constructive trustee of a subsisting equitable interest remains "in the picture" until completion of the transaction which removes him from it. The narrower view, however, is that *Nelson* is confined to its own facts, namely, that the earlier authorities on dropping out do not apply to a case where the trust property is a purchaser's interest under a contract of sale. In *Nelson*, A contracted to sell land to B who was acting as nominee for C. C paid the purchase price to A, but B failed to complete the transfer in accordance with the contract between A and B. The court held that, in such a case, A continued to hold the land on trust for B and B (in turn) held his interest under the uncompleted contract for C. Lawrence Collins LJ (who gave the leading judgment) stated:[9]

> ". . . it seems to me that the authorities have no application to a case where the trust property is the purchaser's interest in land created by the existence of an executory contract for sale and purchase".

There is also another (more recent) case in point. In *Sheffield v Sheffield,*[10] HH Judge Pelling QC held that there was nothing inconsistent with the earlier case law and the *Nelson* ruling. The head trustee (A) may choose whether to deal with the intermediate trustee (B) or not, but this did not mean that the intermediate trustee's equitable interest was effectively transferred to the sub-beneficiary (C).[11] The learned judge was also mindful of the principle enunciated by Turner LJ in *Milroy v Lord*[12] that "if the settlement is intended to be effectuated by one of the modes to which I have referred, the court will not give effect to it by applying another of those modes". The approach taken in the earlier authorities appeared to contradict this principle because it involved the court giving effect to a declaration of trust by treating it as if it were an assignment. This was precisely what Turner LJ in *Milroy* suggested could not be done. Like *Nelso*n, however, the *Sheffield* decision may be explained on a narrower footing because the learned judge also distinguished the earlier case law on the ground that they were "different from the situation where trustees under a head trust pay trust monies to a sub-trustee who is a bare trustee for a beneficiary."[13] There is also the case of *Drakeford v Cotton,*[14]where Morgan J appears to have assumed (without discussion) that s.53(1)(c) has no application to sub-trusts. In the course of his judgment, he stated:[15]

> "If A wished to transfer her entire beneficial interest to A and B, then such a transfer would fall within [s.53(1)(c)]. If A wished to direct the trustees to hold the property on trust for A and B, then that too would fall within the sub-section. However, if A wished to declare a sub-trust of her subsisting beneficial interest in favour of A and B,

[7] [2007] EWCA Civ 1358, at [57].
[8] [1960] A.C. 206.
[9] [2007] EWCA Civ 1358, at [58].
[10] [2013] EWHC 3927 (Ch).
[11] [2013] EWHC 3927 (Ch), at [85].
[12] (1862) 4 D.F. & J. 264, at 274.
[13] [2013] EWHC 3927 (Ch), at [83].
[14] [2012] EWHC 1414 (Ch).
[15] [2012] EWHC 1414 (Ch), at [79].

then that would not fall within the sub-section. If A and B wished to declare new trusts of the property in favour of A and B, then that too would not fall within the sub-section."

**Is Nelson correct?**

The writer would venture to suggest that *Nelson* is probably correct on its wider interpretation. As has already been observed by other commentators, a distinction needs to be made between an *equitable* interest and a *beneficial* interest. The two are not the same. So, when an intermediate trustee (B) makes a declaration of trust of his equitable interest, he does not deprive himself of that interest but simply creates a *second* equitable interest held by the sub-beneficiary (C). So, this does not give rise to any disposition of a "subsisting" equitable interest attracting s.53(1)(c). B's equitable interest is not lost or transferred to C. His interest is still an *equitable* interest in the trust property, but this is no longer a *beneficial* interest as he holds that interest on trust for the sub-beneficiary, whose distinct equitable interest is a beneficial interest. On this analysis, B's equitable interest is not lost even if the sub-trust is passive. Webb and Akkouh[16] make the point that:

> "Given that a declaration of trust of your equitable interest does not deprive you of that interest but simply creates a second equitable interest held by the sub-beneficiary, one may expect that this does not involve any disposition of a subsisting equitable interest and hence does not require writing and signature to be effective (unless of course it is a sub-trust of land or a testamentary sub-trust, in which case s.53(1)(b) of the Law of Property Act or s.9 of the Wills Act would apply)."

Another writer[17] has suggested that *Nelson* is "strong authority for dismissing the [bare trust/active duties] distinction, disapproving as it does the automatic dropping out of the picture of the sub-trustee . . ." This view also finds some support in the remarks of Dixon J in *Comptroller of Stamps (Victoria) v Howard Smith:*[18]

> "A voluntary disposition of an equitable interest may . . . consist of an expression or indication of an intention on the part of the donor that he shall hold the equitable interest vested in him upon trust for the persons intended to benefit . . . in that case, he retains the title to the equitable interest, but constitutes himself trust thereof, and, by his declaration, imposes upon himself an obligation to hold it for the benefit of others, namely, the donees."

An analogy can be made here with the law on sub-leases. Let us suppose that a landlord grants a lease to a tenant who (in turn) grants a sub-lease to a sub-tenant. By creating a sub-lease, the intermediate tenant does not dispose or assign any part of his interest in the demised premises – instead, the tenant carves out a lesser estate from his own leasehold interest in favour of the sub-tenant.[19] The sub-lease, therefore, does not give rise to an assignment of the leasehold term, but operates to grant the sub-tenant a secondary estate which is separate and distinct from estate created by the head lease. Moreover, in terms of the required formalities, whilst the assignment of any tenancy will be void unless made by

[16] C. Webb and T. Akkouh, *Trusts Law*, (4th ed., 2015), Palgrave Law Masters, at pp. 151-153.
[17] J. E. Penner, *The Law of Trusts*, (9th ed., 2014), Oxford University Press, at p. 16.
[18] (1936) 54 C.L.R. 614, (High Court of Australia).
[19] See, *Milmo v Carreras* [1946] K.B. 306.

deed complying with s.52(1) of the Law of Property Act 1925, a sub-lease taking effect in possession for a term not exceeding three years at the best rent will be valid at law even if made orally.[20]

So far as the *Nelson* decision is concerned, there is also an important policy argument that distinguishing between active/passive sub-trusts is illogical and that the requirements of writing under s.53(1)(c) should either apply to all such trusts or to none. *Nelson* favours the latter view on the ground that the sub-trust creates a new equitable interest rather than the disposition of an existing interest regardless of whether or not the intermediate trustee (C) has any active duties under the sub-trust. There is, however, also a strong argument for retaining s.53(1)(c) in all cases where an intermediate trustee declares a sub-trust of his equitable interest.

**The argument for applying s.53(1)(c) to all sub-trusts**

A major criticism of the *Nelson* approach is that it flies in the face of the inherent policy behind s.53(1)(c). After all, the purpose of the sub-section is to require written evidence of what happens to equitable interests which might be hidden beneath the legal title and be susceptible to fraudulent activity. It seems preferable, therefore, to insist upon compliance with s.53(1)(c) for *any* sub-trust regardless whether the intermediate trustee is active or passive.

The argument was made forcibly by another commentator[21] back in 1984 who argued that the sub-trust should be treated as carving out a subsidiary equitable entitlement in C's favour out of the intermediate trustee's original equitable interest – in other words, the sub-trust involves a disposition "out of" the intermediate trustee's interest, not a disposition of the interest itself. On this analysis, however, s.53(1)(c) would not bite because the sub-section is concerned with dispositions of "subsisting" equitable interests and not to dispositions "out of" such interests. It was also argued, however, that a part disposal of B's equitable interest should fall within s.53(1)(c) and this should be characterised as a disposal of the beneficial *part* of B's bundle of subsisting equitable rights:[22]

> "It has already been noted that the characteristic which makes a subsisting equitable interest worthy of protection is the beneficial interest attached to it. When looked at in this way, it will readily be seen that assignments and declarations of trust, both of which have the effect of extinguishing the beneficial interest, are equally deserving of formal protection. And both should be caught by s.53(1)(c) by adopting the notion of a declaration of trust working a 'part disposal' of a subsisting equitable interest . . ."

There is certainly much to be said for this view, not least because it avoids the current anomaly that "a declaration of trust shifting beneficial ownership falls outside s.53(1)(c), whilst a subsequent assignment of the declarant's outstanding valueless equitable right falls within it."[23] The point here is that like transactions should be treated in the same way.

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[20] See, s.54(2) of the Law of Property Act 1925.

[21] See, B. Green, "Grey, Oughtred and Vandervell – A Contextual Reappraisal", (1984) 47 M.L.R. 385.

[22] B. Green, "Grey, Oughtred and Vandervell – A Contextual Reappraisal", (1984) 47 M.L.R. 385, at p. 398.

[23] B. Green, "Grey, Oughtred and Vandervell – A Contextual Reappraisal", (1984) 47 M.L.R. 385, at p. 399.

## Conclusion

Whilst both the *Nelson* and *Sheffield* rulings can be interpreted narrowly confining them to the facts of each case – the former, where the trust property is a purchaser's interest under a contract of sale and the latter, where the head trustee pays trust money to a sub-trustee who is a bare trustee for a beneficiary – the better view is that they have effected a change in the law.

On the *Nelson* analysis, although the practical effect of creating a sub-trust might seem to amount to the "getting rid" of the intermediate trustee's equitable interest, allowing the intermediate trustee (B) to deal directly with the sub-beneficiary (C), this is not the same as saying that, as a matter of law, B's equitable interest is effectively transferred to C. The sub-trust involves the creation of a *new* equitable interest in favour of C rather than the disposition of an existing interest. On this reasoning, B does not drop out of the picture simply by declaring the sub-trust. The consequence of this analysis, however, is that no sub-trusts require writing, except where the subject-matter is land or the sub-trust is testamentary.

Although this conclusion has the merit of uniformity, it does contradict the inherent policy underlying s.53(1)(c). After all, the rationale of the sub-section is to prevent fraud by prohibiting oral hidden transfers of equitable interests under trusts and assist trustees by enabling them to identify the whereabouts of the equitable interest arising under a trust.[24] Policy considerations, therefore, clearly favour the opposite view that both assignments and declarations of trust should be treated in the same way and be caught by s.53(1)(c). The *Nelson* ruling may, therefore, require further consideration at some future date.

[24] *Vandervell v IRC* [1967] 2 A.C. 291, at 311, *per* Lord Upjohn.