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ARTICLES

CONTROLLING FIDUCIARY POWER

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A. INTRODUCTION

POWER held by fiduciaries is subject to many forms of control. All of these forms of control have to strike a balance between competing objectives. They must seek to curb the harm that the holder of power can inflict on those affected by it. Yet they must be careful not to abolish the discretion inherent in power itself.

This article examines the techniques used to control the power held by those who voluntarily undertake a task subject to fiduciary obligations. It focuses principally on express trustees and company directors, who by any reckoning form vitally important groups of fiduciary office-holders. Its concern, therefore, is with formal power in private law rather than informal power.[1]

The first step is to identify and investigate the various methods used to control power held by these fiduciaries: "It is a capital mistake to theorize before one has data. Insensibly one begins to twist facts to suit theories, instead of theories to suit facts."[2] Various significant implications then emerge from this analysis. One such is a clear appreciation of how the various doctrines relate to each other, both in terms of their techniques and their objectives. This, in turn, sheds light on how, if at all, these controls on power held by fiduciaries may themselves be described as aspects of fiduciary doctrine. Finally, this exercise helps to dispel some unnecessary confusion about the validity of acts that breach one or more of the controls, though questions of validity also turn vitally on the context in which the acts occurred.

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[1] P. Finn, "Controlling the Exercise of Power" (1996) 7 Public Law Review 86 at pp. 87–88. See also J.C. Shepherd, *The Law of Fiduciaries* (Toronto 1981).

[2] Sherlock Holmes in "A Scandal in Bohemia" (Sir Arthur Conan Doyle, *The Strand Magazine*, 1891).

B. The Techniques in Outline

The techniques used to control power held by fiduciaries fall into three categories. These techniques all assume that there has at least been a conscious attempt to exercise the power in question: if there were not, there would be no exercise of the power to control.[3] They also assume that any requirements as to the manner and form of exercising the power have been satisfied.[4]

The first category is comprised of doctrines which define – and, most importantly for present purposes, limit – the scope of the power concerned. They are construction, the requirement of good faith in the exercise of a power and the doctrine of fraud on a power (sometimes called the proper purposes doctrine). These techniques approach the task of determining the scope of a power in distinct ways. But they all have as their consequence a conclusion about the extent of the power. The act which constitutes a purported exercise of the power is void *ab initio*; though what that means precisely in any particular case requires further elucidation, when remedies are considered.

The second set of techniques addresses the process of decision making by a fiduciary. Controls of this type admit the existence and exercise of the relevant power; but the circumstances in which the power was exercised create a significant risk of sub-optimal decision making, and so these controls allow the exercise of the power to be undone. They comprise the self-dealing rule and, at least as currently formulated, the so-called principle in *Re Hastings-Bass*. In these cases, the act which constitutes an exercise of the power is not void *ab initio* but voidable.

The third type of control addresses the degree of competence with which the fiduciary exercised the power. This type of control is rather different from the others. So long as the fiduciary stays within the scope of the power, his exercise of the power is still valid even though he acted carelessly. The incompetence merely exposes the fiduciary to various sanctions against him personally. These sanctions, given their likely effect on the fiduciary's behaviour, constitute an indirect control on the power. The position is slightly complicated, however, because occasionally the scope of a power is taken to allow only action that is performed competently. In that case, incompetence will have the additional effect of rendering the purported exercise of the power void *ab initio*.

[3] See, *e.g.*, *Wilson* v. *Turner* (1883) 22 Ch.D. 521 and *Turner* v. *Turner* [1984] Ch. 100, esp. at p. 111, *per* Mervyn Davies J.

[4] There is much old learning about requirements of manner and form. It is of limited general relevance: see C.J.W. Farwell and F.K. Archer (eds.), *Farwell on Powers*, 3rd edn (London 1916), at pp.147–156, 380–383.

C. Techniques which concern Scope

Three techniques control power by limiting the scope of what action is authorised. These are the requirements that a fiduciary must exercise a power within its terms, in good faith and for proper purposes.

(i) Construction

Quite obviously, a fiduciary must act within his powers.[5] It is therefore crucial for the fiduciary (and any relevant court) to know the terms of the power in question. But vital as it is, there is little to say in a review such as this about the construction of powers. The courts have approached construction with various degrees of strictness over the years. But the object of the exercise is always the same: to see what meaning should be attributed to various words *in the particular context which frames the power in question*.[6] Construction is essentially about *words* in context, rather than *acts* (or *behaviour*) in context.[7] Indeed, the very fact that a power is held in a fiduciary capacity will influence its construction: a fiduciary must not benefit from using the power unless allowed to do so.[8]

It is therefore very difficult to say anything useful about construction without engaging in the minutiae of specific terms of particular powers in specific contexts. A word does not necessarily have one meaning only: context gives meaning to words, in the law at least.[9]

(ii) Good Faith

A requirement that fiduciaries should act in good faith is central.[10] To speak of a "duty to act in good faith", however, can easily conceal an important distinction. If that distinction is not made, confusion can easily follow.

Sometimes, the fiduciary's "duty to act in good faith" can mean that the fiduciary has a duty to do something particular in a certain way.[11]

[5] As regards trustees, see Underhill & Hayton, *Law of Trusts and Trustees*, 17th ed. (London 2007), §§[47.1]–[47.3] and the cases cited there. As regards directors, see Companies Act 2006, s. 171(a), codifying earlier case law in accordance with s. 170(3) and (4).

[6] Lord Nicholls, "My Kingdom for a Horse: The Meaning of Words" (2005) 121 L.Q.R. 577 at pp. 579–580. "In the law, context is everything": *R (Daly)* v. *Home Secretary* [2001] UKHL 26, [2001] 2 A.C. 532 at [28], *per* Lord Steyn.

[7] *Equitable Life Assurance Society* v. *Hyman* [2000] UKHL 39, [2002] 1 A.C. 408 at pp. 458–459, *per* Lord Steyn, who distinguishes between "interpretation" (ascertaining the meaning of express words) and "implication" (reading in limitations to express words based on the circumstances of the case).

[8] See, *e.g.*, *Kane* v. *Radley-Kane* [1999] Ch. 274.

[9] For a recent example, see, *e.g.*, *Bluebottle UK Ltd* v. *Deputy Commissioner of Taxation* [2007] HCA 54, (2007) 232 C.L.R. 598 at [31], *per curiam*. See also *Investors Compensation Scheme* v. *West Bromwich Building Society* [1998] 1 W.L.R. 896, particularly at pp. 912–913 (and principle (4)), *per* Lord Hoffmann and, generally, Lord Nicholls, *op. cit.* note 6 at pp. 578–579.

[10] *Bristol & West BS* v. *Mothew* [1998] Ch. 1 at p. 18.

[11] See, further, L. Ho "Good Faith and Fiduciary Duty", presented at the Obligations IV Conference, National University of Singapore, July 2008; Teele Langford, "*ENT Pty Ltd* v

For example, a director may have to disclose his own wrongdoing.[12] In other contexts, the same words may mean that the fiduciary has power to act, but no duty, yet if he does exercise that power, he must do so in good faith.[13] This article is concerned with the latter situation, where good faith qualifies the exercise of power, rather than demanding specific action.

In this context, the requirement of action in good faith is, in reality, a requirement not to act in bad faith.[14] Regularity is to be presumed: it is up to someone who alleges irregularity to establish that fact.[15] In addition, English rules of civil procedure specifically address the question of pleading and proving conscious bad faith (and cognate concepts such as fraud).[16] So the control on power is in truth negative in form, a prohibition of bad faith.

What amounts to bad faith can, of course, vary from case to case, but good faith and bad faith are both ascertained by reference to actual, subjective, states of mind. This has often been emphasised in judicial decisions, whether they concern trustees,[17] or directors.[18] Bad faith action has been taken to include acts taken for reasons of caprice or spite.[19] And good faith action can even include unauthorised action in some cases.[20]

Crucially, the requirement of good faith limits what a fiduciary may or may not do lawfully in exercise of his powers: good faith goes to the scope of a power.[21] Put the other way, bad faith action is outside the scope of a power.[22]

Sunraysia Television Ltd: A Positive Fiduciary Duty of Disclosure" (2008) 26 Company and Securities Law Journal 470.

[12] *Item Software (UK) Ltd.* v. *Fassihi* [2004] EWCA Civ 1244, [2005] 2 BCLC 91, rejected in Australia by *P & V Industries Pty Ltd* v. *Porto* [2006] VSC 131, (2006) 14 V.R. 1 and criticised by M. Harding, "Two Fiduciary Fallacies" (2007) 2 *Journal of Equity* 1.

[13] As regards trustees, see, *e.g.*, *Armitage* v. *Nurse* [1998] Ch. 241. As regards company directors, see, *e.g.*, *Regentcrest plc (in liquidation)* v. *Cohen* [2001] 2 BCLC 80 (ChD).

[14] Consider, *e.g.*, *Gisborne* v. *Gisborne* (1877) 2 App. Cas. 300 at p. 305, *per* Lord Cairns.

[15] See, *e.g.*, *Re Oddy* (1911) 104 L.T. 128 at p. 131, *per* Joyce J. (trustees) and *In re Coalport China Co. Ltd.* [1895] 2 Ch. 404 at p. 409, *per* Lindley L.J. (directors).

[16] See Civil Procedure Rules, Practice Direction 16, para. 8(2), as supplemented by strict professional guidance to barristers in the Bar Council's Code of Conduct at §704(c). See also *Medforth* v. *Blake* [2000] Ch. 86 at p. 103, *per* Scott V.-C.

[17] See, *e.g.*, *In re Smith* [1896] 1 Ch 71 at p. 76, *per* Kekewich J. (in relation to powers of investment); *Bristol & West Building Society* v. *Mothew* [1998] Ch 1 at p. 18 and *Armitage* v. *Nurse* [1998] Ch. 241 at pp. 253–254, *per* Millett L.J. (general principle).

[18] *Re Smith & Fawcett Ltd* [1942] Ch 304 at p. 306; *Medforth* v. *Blake* [2000] Ch. 86 at p. 103, *per* Scott V.-C.; *Regentcrest plc (in liquidation)* v. *Cohen* [2001] 2 BCLC 80 (ChD) at [120], *per* Jonathan Parker J. See also *Extrasure Travel Insurances Ltd.* v. *Scattergood* [2002] EWHC 3093 (Ch), [2003] 1 BCLC 598 at [87]–[90], *per* Jonathan Crow Q.C.

[19] See the cases cited in note 17 above.

[20] *Armitage* v. *Nurse* [1998] Ch. 241 at pp. 251, 253–254, *per* Millett L.J.

[21] *Dundee General Hospitals Board of Management* v. *Walker* [1952] 1 All E.R. 896 at p. 905, *per* Lord Reid, a Scottish case cited with approval as regards English law in *Scott* v. *National Trust* [1998] 2 All E.R. 705 at pp. 717–718, *per* Robert Walker J.

[22] *Hopkins* v. *TL Dallas Group Ltd.* [2004] EWHC 1379 (Ch), [2005] 1 BCLC 543 at [87]–[91], *per* Lightman J.

(iii) Fraud on a Power and Proper Purposes

The next method of limiting and controlling the powers vested in fiduciaries likewise goes to the scope of the power concerned. It tends to be known as the doctrine of a "fraud on a power" in the context of trust law,[23] and as the "proper purposes" doctrine in company law.[24] Neither is a particularly accurate description: the doctrine might, perhaps, be more usefully called "the improper purposes doctrine".

Lord Parker provided a classic description of a fraud on a power in *Vatcher* v. *Paull*:

> The term [fraud] in connection with frauds on a power does not necessarily denote any conduct on the part of the appointor amounting to fraud in the common law meaning of the term or any conduct which could properly be termed dishonest or immoral. It merely means that the power has been exercised for a purpose, or with an intention, beyond the scope of or not justified by the instrument creating the power.[25]

The vice, therefore, lies in utilising a power for a purpose, or with an intention, beyond its scope. That distinguishes this technique for controlling power from the others just examined – techniques of construction and good faith. The prohibition on trustees acting "capriciously" is an aspect of this doctrine: it means that the trustees must not "act for reasons which … could be said to be irrational, perverse or irrelevant to any sensible expectation of the settlor".[26]

Courts and text-writers have identified three major grounds upon which an exercise of a power by trustees may be held to be fraudulent: where the appointment is made pursuant to an antecedent agreement between the donee and the object whereby a non-object is to benefit; where the appointment is made for a corrupt purpose; and where the appointment is made for purposes foreign to the power.[27] In fact, the first two categories are nothing more than sub-divisions of the third.[28] And, in any event, they are all just convenient ways of noting trends in the cases: the doctrine of a fraud on a power applies generally

[23] See, *e.g.*, G.W. Thomas, *Powers* (London 1998), Chapter 9.

[24] See, generally, *Gore Browne on Companies*, reissue (London 2008), at §§15[9]–15[9A]; P. Davies, *Gower & Davies Principles of Modern Company Law*, 8th ed. (London 2008) at pp. 500–501; R.C. Nolan, "The Proper Purpose Doctrine and Company Directors", in B. Rider (ed.) *The Realm of Company Law* (London 1998), ch. 1, and R.P. Austin, *Company Directors: Principles of Law & Corporate Governance* (Sydney 2005), at §§7.18–7.30. The term "fraud on a power" has been used in older company law cases, however: see, *e.g.*, *Spackman* v. *Evans* (1868) L.R. 3 H.L. 171 at p. 187, *per* Lord Cranworth.

[25] [1915] A.C. 372 at p. 378.

[26] *Re Manisty's Settlement* [1974] Ch. 17 at p. 26, *per* Templeman J.

[27] See *Kain* v. *Hutton* [2007] NZCA 199, [2007] 3 N.Z.L.R. 349 at [36], *per* Glazebrook J., citing Thomas, above note 23, at §9–20. In fact, this three-fold classification is much older: see *Farwell on Powers* (above note 4), at p. 460.

[28] *Farwell on Powers* (above note 4). Note also *Henty* v. *Wrey* (1882) 21 Ch.D. 332 at p. 354, *per* Lindley L.J.

to trustees' powers, even to their administrative powers.[29] No such sub-divisions of the proper purposes doctrine are generally made in company law.[30]

Clearly, a power can be used in good faith but for an improper purpose. The tests of good faith and proper purposes are conceptually distinct.[31] The point has been made crystal clear in the context of a company director.

> The position is different where a power conferred on a director is used for a collateral purpose. In such circumstances it matters not whether the director honestly believed that in exercising the power as he did he was acting in the interests of the company; the power having been exercised for an improper purpose, its exercise will be liable to be set aside.[32]

So, for example, directors may genuinely believe that a proposed take-over would be highly detrimental to the business and affairs of their company; but that still does not mean of itself that they can use their powers to allot and issue shares in order simply to create a majority of shareholders who will vote in general meeting against the takeover.[33] Similarly, trustees cannot make an appointment to a beneficiary in order to benefit someone who is not a beneficiary, however desirable they believe in good faith that may be for the family which includes both the beneficiary and the non-beneficiary.[34]

This is not to say that the mental state of the fiduciary is irrelevant to the doctrine of a fraud on a power.[35] In order to prove a fraud on a power, it is necessary to establish the purpose – the ends – for which the fiduciary chose to act.[36] That purpose – that aspect of the fiduciary's mental state – may fall outside the scope of what may legitimately be achieved by use of the power – something often called "the purpose of

[29] See, *e.g.*, *Robinson* v. *Briggs* (1853) 1 Sm. & G. 188, 65 E.R. 81.

[30] For examples of the doctrine in company law, see the texts cited in note 24 above.

[31] *The Bell Group Ltd (in liquidation)* v. *Westpac Banking Corporation (No. 9)* [2008] WASC 239 at [4456], *per* Owen J.

[32] *Regentcrest plc (in liquidation)* v. *Cohen* [2001] 2 BCLC 80 (ChD) at [123], *per* Jonathan Parker J. See also *Extrasure Travel Insurances Ltd.* v. *Scattergood* [2002] EWHC 3093 (Ch), [2003] 1 BCLC 598 at [92]–[93], *per* Jonathan Crow Q.C.

[33] *Hogg* v. *Cramphorn Ltd.* [1967] Ch. 254; *Bamford* v. *Bamford* [1970] Ch. 212, though note the possibility of greater judicial latitude evidenced (albeit *obiter*) in *Criterion Properties plc* v. *Stratford UK Properties LLC* [2004] UKHL 28, [2004] 1 W.L.R. 1846.

[34] *Wong* v. *Burt* [2004] NZCA 174, [2005] 1 N.Z.L.R. 91; *Kain* v. *Hutton* [2008] NZSC 61, [2008] 3 N.Z.L.R. 589 at [18], *per* Elias C.J., Blanchard, McGrath and Anderson J.J.

[35] See *Kain* v. *Hutton* [2007] NZCA 199, [2007] 3 N.Z.L.R. 349 at [113], *per* Glazebrook J., and on appeal, [2008] NZSC 61, [2008] 3 N.Z.L.R. 589 at [20], *per* Elias C.J., Blanchard, McGrath and Anderson J.J., citing *Re Burton's Settlement* [1955] Ch. 82.

[36] *Farwell on Powers* (above note 4), pp. 484–485. Purpose is to be distinguished from motive: motive is essentially about antecedent reasons for action; purposes are essentially about prospective aims. See, *e.g.*, *Topham* v. *Duke of Portland* (1863) 1 De G.J. & S. 517 at pp. 570–571, 46 E.R. 205 at pp. 226–227, *per* Turner L.J., and *Topham* v. *Duke of Portland* (1869) L.R. 5 Ch. App. 40 at p. 57, *per* Lord Hatherley L.C. In this regard, *Extrasure Travel Insurances Ltd.* v. *Scattergood* [2002] EWHC 3093 (Ch), [2003] 1 BCLC 598 at [92]–[93], *per* Jonathan Crow Q.C., is unhelpful as the words "purpose" and "motive" are used interchangeably.

the power"; and if it does, the fiduciary has committed a *prima facie* fraud on the power. As Lord Parker of Waddington put it in *Vatcher* v. *Paull*:

> It is not enough that the appointor or some person not an object of the power may conceivably derive some benefit. If this were not so no father could appoint in favour of an infant child, because if the infant died under twenty-one the father himself would take as next of kin. In order to avoid such appointment it must be proved affirmatively, or the inference to be drawn from the circumstances must be, that the purpose of the appointment is not to benefit the infant but to benefit the appointor through the infant.[37]

High authority also confirms that the doctrine of abusing a power for an improper purpose is not the same as simply exceeding the power: the proper purposes doctrine and questions of construction differ in how they seek to control discretionary power. Lord Wilberforce noted the distinction in *Howard Smith* v. *Ampol Petroleum*:

> The directors, in deciding to issue shares, forming part of Millers' unissued capital, to Howard Smith, acted under clause 8 of the company's articles of association. This provides, subject to certain qualifications which have not been invoked, that the shares shall be under the control of the directors, who may allot or otherwise dispose of the same to such persons on such terms and conditions and either at a premium or otherwise and at such time as the directors may think fit. Thus, and this is not disputed, the issue was clearly *intra vires* the directors. But, *intra vires* though the issue may have been, the directors' power under this article is a fiduciary power: *and it remains the case that an exercise of such a power though formally valid, may be attacked on the ground that it was not exercised for the purpose for which it was granted*"[38]

But what, precisely, is this distinction?

Construction is concerned with words: attributing meaning to words, however strictly or loosely, and whatever the context, is the key to construction. By contrast, the proper purposes doctrine looks to the particular ends intended to be achieved through certain particular acts and determines whether such ends are contemplated (and therefore authorised) by the power in question.

[37] [1915] A.C. 372 at pp. 379–380. This statement, in particular its final and crucial phrase, appears to have been overlooked by Tipping J. the New Zealand Supreme Court, where the learned Judge criticised Lord Parker's earlier statement (at p. 378) that "it is enough that the appointor's purpose and intention is to secure a benefit … [for] some other person not an object of the power": *Kain* v. *Hutton* [2008] NZSC 61, [2008] 3 N.Z.L.R. 589 at [48]–[49]. See also *Lord Hinchinbroke* v. *Seymour* (1789) 1 Bro.C.C. 395, 28 E.R. 1200; *Portland* v. *Topham* (1864) 11 H.L. Cas. 32; *Henty* v. *Wray* (1882) 21 Ch.D. 332, *Re Dick* [1953] Ch. 343 and *Wong* v. *Burt* [2004] NZCA 174, [2005] 1 N.Z.L.R. 91.

[38] [1974] A.C. 821 at p. 834, emphasis added. See also *Fearon* v. *Desbrisay* (1851) 14 Beav. 635 at p. 642, 51 E.R. 428 at p. 431, *per* Romilly M.R., *Henty* v. *Wrey* (1882) 21 Ch.D. 332 at p. 355, *per* Lindley L.J. and *Macmillan Inc* v. *Bishopsgate Trust (No3)* [1995] 1 W.L.R. 978 at p. 984, *per* Millett J.

Naturally, there can be a degree of overlap between questions of construction and the proper purposes doctrine: the facts of cases are often ambiguous or can sensibly bear more than one interpretation. For example, it may be possible to view the purported exercise of a power of appointment as something not authorised by the words of the power, because *in substance* the trustees conferred benefit on someone outside the class of beneficiaries, or as something within the express language of the power, because the appointment was formally to an object of the power, but made for an improper purpose because the recipient was to hand on the benefit to a non-object.[39] Similarly, when directors of an insurance company purportedly used their discretion under the company's articles of association to reduce final bonuses payable under insurance policies issued subject to those articles, the directors' action was held to be invalid either by reason of an implied limitation on the relevant article, which is a matter of construction, or because they had abused the power conferred by the relevant article.[40] More generally, the scope of directors' actual authority is impliedly limited in that it is to be used for the "purposes of the company as set out in [its] memorandum of association".[41] That too could be regarded as a canon of construction or as an application of the proper purposes doctrine.

Indeed, it would be logically possible, though entirely artificial, to subsume the proper purposes doctrine entirely within questions of construction. A limitation to proper purposes could be seen as simply inherent in the words of a power. But that is simply a sleight of hand. The same processes would have to be undertaken to determine the limits of a power: both a focus on the words of the power and a focus on the particular ends to be achieved by using it. Furthermore, and as noted earlier, the court's duty to give effect to the terms of a power which is *prima facie* lawful restricts its ability to place implicit limitations on the power by reference only to the language of the power: exercises in linguistic analysis must have their limits if they are not to become absurd and lose their legitimacy.

The proper purpose doctrine does raise some difficulties, however. It is all very well to say that a power should not be exercised for a purpose beyond the scope of, or not justified by, the instrument creating the power. But how is that ascertained, and by reference to what criteria?

[39] See, *e.g.*, *Wong* v. *Burt* [2004] NZCA 174, [2005] W.T.L.R. 29.

[40] *Equitable Life Assurance Society* v. *Hyman* [2000] UKHL 39, [2002] 1 A.C. 408 at pp. 457–460, *per* Lord Steyn, and at pp. 460–462, *per* Lord Cooke of Thorndon. The other members of the House agreed with both speeches.

[41] *Rolled Steel Products (Holdings) Ltd.* v. *British Steel Corporation* [1986] Ch. 246 at p. 295, *per* Slade L.J. See also *Re Introductions Ltd.* [1970] 1 Ch. 199 at p. 211, *per* Harman J., though the abolition of a company's need to have objects, effected by Companies Act 2006, s. 31, will obviously alter this position.

In the case of a trust, these questions are answered by reference to the expectations of the settlor(s) of the trust.[42] The courts are concerned with the objectively understood expectations of the settlor, rather than his subjective intent, at least in any case other than where the settlor is the sole trustee.[43] The settlor is the very person who established what benefit, or what possibility of benefit, the beneficiaries are to have from the trust, so it makes perfect sense that the settlor's objectively expressed expectations form the criterion of any judgment on the propriety or impropriety of the trustees' exercise of powers which can affect that benefit (or possibility of benefit).[44] This may mean that the trustees, when exercising their powers, can properly take into account interests other than those of any beneficiaries,[45] though a trust surely cannot provide for the interests of beneficiaries to be entirely subordinated to those of non-beneficiaries, as that would be self-contradictory.[46]

The exercise of ascertaining a settlor's expectations may be more or less evidentially difficult: when making its findings, the court may or may not have the assistance of a letter of wishes,[47] or other admissible evidence. But the very exercise of seeking to discern the settlor's wishes is entirely comprehensible and something a judge can sensibly do, though a court may encounter some evidential difficulties in some cases, for example where a trust has more than one settlor, or where a trust has been amended,[48] or varied under the Variation of Trusts Act

[42] *Re Beatty's W.T.* [1990] 1 W.L.R. 1503 at p. 1506, *per* Hoffmann J. See also *McPhail* v. *Doulton* [1971] A.C. 424 at p. 449, *per* Lord Wilberforce; *Re Manisty's Settlement* [1974] Ch. 17 at p. 26, *per* Templeman J.; *Re Hay's S.T.* [1982] 1 W.L.R. 202 at p. 209, *per* Megarry V.-C., and *Hayim* v. *Citibank* [1987] A.C. 730 at p. 746, *per* Lord Templeman. For the distinction between the "real" settlor and the "nominal" settlor, see, *inter alia*, *Hartigan Nominees Pty Ltd* v. *Rydge* (1992) 29 N.S.W.L.R. 405 and *Breakspear* v. *Ackland* [2008] EWHC 220 (Ch), [2009] Ch. 32.

[43] See W.J. Mowbray *et al* (eds.), *Lewin on Trusts*, 18th ed. (London 2008), §[6-03]. Note *Vandervell* v. *I.R.C.* [1967] 2 A.C. 291 at p. 312, *per* Lord Upjohn and *In re Z Trust* [1997] C.I.L.R. 248 at p. 257, *per* Smellie J.

[44] Merely following the settlor's directions, however, could result in a finding that the purported trust is a sham: see *Rahman* v. *Chase Bank (C.I.) Trust Co Ltd* [1991] J.L.R. 103 and, more generally, M. Conaglen, "Sham Trusts" [2008] C.L.J. 176.

[45] See, *e.g.*, *Citibank NA* v. *MBIA Assurance SA* [2006] EWHC 3215 (Ch), esp. at [47]–[49], *per* Mann J., affirmed by the Court of Appeal, [2007] EWCA Civ 11 at [82], *per* Arden L.J. and at [95]–[97], *per* Dyson L.J., the Master of the Rolls agreeing with both judgments at [100].

[46] See further J. Hilliard, "The Flexibility of Fiduciary Doctrine in Trust Law: How Far does it Stretch in Practice?" (lecture to the Chancery Bar Association, 14th July 2008). The limitation also seems implicit in the *Citibank* case, note 45 above.

[47] See *Re Rabiotti's 1989 Settlement* [2000] W.T.L.R. 953 at pp. 967–968, *per* Deputy Bailiff Birt (Jersey Royal Court, Samedi Division); *Breakspear* v. *Ackland* [2008] EWHC 220 (Ch), [2009] Ch. 32 at [5]–[14], and esp. at [8], *per* Briggs J., though "[i]t may be that there are some matters in the memorandum [of wishes] which … it would not be proper for the trustees to take into account in the exercise of any, or of a particular, discretionary power": *Hartigan Nominees Pty Ltd* v. *Rydge* (1992) 29 N.S.W.L.R. 405 at p. 427, *per* Mahoney J.A.

[48] A power to amend trusts is common in pension trusts: see R. Self, *Tottel's Pension Fund Trustee Handbook*, 9th ed. (Haywards Heath 2005), at §6.3, and, by way of example, *Imperial Group Pension Trust Ltd* v. *Imperial Tobacco plc* [1991] 1 W.L.R. 589.

1958, or created out of another settlement.[49] If the court does encounter such problems, then it can supply default implications, if needs be fashioned by reference to "reasonable expectations". This might seem a similar exercise to the control of power in public law by reference to *Wednesbury* unreasonableness.[50] Nevertheless, the court should be very cautious about any such analogy between private and public law. In the private law context, the court is primarily engaged in a forensic exercise to establish a purpose, or purposes, and should only make implications in so far as it is defeated in that exercise: the court is not, as in public law, applying mandatory rules of law (or at least very strong default presumptions) generated by policy concerns of constitutional legitimacy and propriety.[51]

The question of what amounts to an improper purpose is more difficult to answer in other areas of law, such as company law. There are, as always in this area, two questions to address: first, how does a court determine the purposes for which a power may or may not be exercised; and secondly, how does the court establish the purposes for which the power was purportedly exercised, especially where a group of individuals, such as a board of directors, purport to exercise it.

In *Re Smith & Fawcett Ltd.*,[52] the answer to the first question was said to lie in construction of the company's articles of association. While that might be true in this particular case, which concerned only the limits on a very widely drawn power for directors to decline registration of a share transfer, it cannot explain cases such as *Howard Smith* v. *Ampol Petroleum*,[53] *Lee Panavision Ltd.* v. *Lee Lighting Ltd.*[54] and *Equitable Life Assurance Society* v. *Hyman*.[55] Context, not just construction of documentation, was vital in these cases. In *Howard Smith*, the case turned on the company's constitutional arrangements as a whole and expectations as to how those arrangements would operate in practice: the directors could not use their fiduciary power

[49] See, generally, A.J. Oakley, *Parker and Mellows: The Modern Law of Trusts*, 9th ed. (London 2008), at §§[18-024]–[18-044] and Lord Millett *et al*, *Forms and Precedents*, 5th ed. (London 2001), vol. 40(1), at §§[139] (settled advances); and [4359] and [4405] (powers for trustees to appoint trust funds to distinct settlements).

[50] *Scott* v. *National Trust* [1998] 2 All E.R. 705 at p. 718g. The charity involved in this case, the National Trust for Places of Historic Interest or Natural Beauty, is actually a corporation rather than a trust *stricto sensu*: see the National Trust Act 1907, s. 3. That should not affect this point, however.

[51] See Underhill & Hayton (above note 5), §§61.12–61.17. Rather ironically, the continuing place of *Wednesbury* unreasonableness in administrative law is moot: see, generally, H.W.R. Wade and C.F. Forsyth, *Administrative Law*, 9th ed. (Oxford 2004), pp. 371–372.

[52] [1942] Ch. 304 at p. 306, *per* Lord Greene M.R. See also *ANZ Executors & Trustee Co Ltd* v. *Qintex Australia Ltd* [1991] 2 Qd.R. 360 and *Advance Bank of Australia Ltd* v. *FAI Insurances Australia Ltd* (1987) 9 N.S.W.L.R. 464.

[53] [1974] A.C. 821.

[54] [1992] B.C.L.C. 22.

[55] [2000] UKHL 39, [2002] 1 A.C. 408.

to allot and issue shares in order to alter the balance of power amongst shareholders because that would undermine the established division of power and influence between the board and the general meeting. In *Lee Panavision*, the directors' extremely widely drafted power to make contracts on behalf of the company could not be used to enter into a long term arrangement for management of the company by a third party, because that would render worthless the power of the general meeting to remove the existing directors, appoint new ones and so change the way in which the company was managed. In *Equitable Life*, directors could not exercise a power in a way that would subvert the expectations of policies of insurance written subject to those articles; but it was not the language of the articles themselves which led to that conclusion.

Equally, it may be difficult to judge propriety and impropriety by reference to the actual assumptions or expectations of particular people. Those who first incorporate a company often have very little, if anything, to do with it – shelf companies are but one example of this. Companies often use "off the peg" constitutions, at least to begin with.[56] A company's constitution can be, and often is, changed over time, commonly by different groups of shareholders:[57] shareholders of a company come and go over time.[58] So where powers are constituted and conferred on directors by a company's constitution, and are to be exercised for the purposes for which those powers were conferred on the directors, it will often make very little sense for a court to seek to ascertain those purposes by reference to the expectations of a particular set of people. That is not to say that the expectations of particular people are never relevant: in some cases, such as a closely-held family company, it may be quite possible to ascertain the purposes for which a power was conferred on directors of the company by reference to the expectations of particular people. But in many cases, and much more often than in the context of trusts, the courts will be driven to stipulate the purpose of powers by means of their own default implications, generated by reference to common corporate practice and widely-held expectations of those involved in companies.[59] Where there is no direct evidence of that purpose, there is nothing else the courts can do if they are to apply a proper (or, rather, an improper) purposes doctrine.[60] But even here, much caution is warranted before making analogies between

[56] See the Companies (Tables A–F) Regulations 1985 (SI 1985/805) as amended, and the Model Articles of Association promulgated for the purposes of the Companies Act 2006 in the Companies (Model Articles) Regulations 2008 (SI 2008/3229).
[57] Companies Act 2006, ss. 21–27, replacing earlier legislation.
[58] Companies Act 2006, s. 544 and Part 21, re-enacting earlier legislation.
[59] See, *e.g.*, *Howard Smith* v. *Ampol Petroleum* [1974] A.C. 821.
[60] See, generally, Nolan, "The Proper Purpose Doctrine and Company Directors", (above note 24).

private and public law: the courts are making implications into a particular arrangement, rather than applying general law.[61]

Even once the purposes of a power are understood, a court will still face difficulty in answering the second question, namely how does it establish the purposes for which the power was purportedly exercised where a group of individuals, acting by a majority, such as a board of directors, have purported to exercise the power. "The application of the general equitable principle to the acts of directors managing the affairs of a company cannot be as nice as it is in the case of a trustee exercising a special power of appointment."[62] What the courts must try to do is to ascertain "the substantial object the accomplishment of which formed the real ground of the board's action",[63] and then judge that to be proper or improper according to the purposes of the power in question.

D. Techniques which concern Decision-Making

All the techniques for controlling fiduciary power which have been considered so far have sought in their different and partial ways to define and limit the scope of a power. Other techniques focus not so much on the scope of a power, but the process of decision making by a fiduciary which lies behind an exercise of the power. As noted earlier, controls of this type admit the existence and exercise of the relevant power; but the circumstances in which the power was exercised create a significant risk of sub-optimal decision making, so these controls allow both the exercise of the power and its consequences to be undone, subject always to the operation of any applicable defences.

(i) Self-Dealing

The first of the techniques for the control of power that concern decision-making is commonly known as the self-dealing rule. The self-dealing rule applies when a trustee deals with, or acts in relation to, assets comprised in the trust fund both *qua* trustee and in some other capacity.[64] It is immaterial for the purposes of the rule whether that trustee acts by himself in this other capacity or jointly with someone else.[65] Prior to the codification of directors' duties in Part 10, Chapter 2 of the Companies Act 2006, the self-dealing rule also applied when a

[61] See note 51 above and the text thereto. Note also S. Fridman, "An Analysis of the Proper Purpose Rule" (1998) 10 Bond Law Review 164, and P. Watts, "Judicial Review of Directors' Decisions – Another Bad Idea" [2007] Company and Securities Law Bulletin 75.

[62] *Mills* v. *Mills* [1938] HCA 4, (1938) 60 C.L.R. 150 at pp. 185–186, *per* Dixon J.

[63] *Ibid.*, approved in *Howard Smith Ltd.* v. *Ampol Petroleum Ltd.* [1974] A.C. 821 at pp. 835–836, *per* Lord Wilberforce.

[64] See, *e.g.*, *Wright* v. *Morgan* [1926] A.C. 788 (fiduciary's own interest adverse to that of his principal); *Re Thompson's Settlement* [1986] Ch. 99 at pp. 114–115, *per* Vinelott J. (fiduciary's interest as representative of others adverse to that of his principal).

[65] See, *e.g.*, *Re Thompson's Settlement* [1986] Ch. 99.

director dealt with his company.[66] The name "self-dealing rule" is therefore a slight misnomer, for application of the rule does not necessarily depend on there being one person who is party to a transaction in two different capacities: a company and its directors are distinct people, after all.[67] What matters is that a particular person, the fiduciary, is concerned with both sides of the transaction in question. The self-dealing rule addresses transactions that have occurred, or at least are taken to have occurred. It is not concerned with the logically prior question of whether a transaction ever occurred which binds the principal at all.[68] Nor is it concerned with whether the fiduciary concerned had authority to enter into the transaction.[69]

Transactions involving self-dealing involve a fiduciary in the exercise of powers conferred for the benefit of his principal; and those situations are the relevant cases for present purposes. By contrast, situations which attract the operation of the fair dealing rule are not relevant for present purposes: they do not involve the fiduciary exercising his powers to act for the benefit of his principal, as the fiduciary is acting on his own behalf with his principal.[70] These circumstances are therefore of no concern to an exploration of fiduciary power.

It is clear even from this brief overview of the self-dealing rule that the rule is concerned with the risks inherent in a situation, not the scope of a power. The risk is that a fiduciary will deviate from his duty in a situation where that duty is, or may be, in conflict with some interest of the fiduciary or some other duty of his. The rules which respond to that risk are designed to mitigate it and promote the due performance of the fiduciary's undertaking, though they cannot ensure that.[71] Consequently, where a fiduciary has power to engage in a transaction (a sale, a mortgage, or whatever), and he enters into the transaction in exercise of that power, but suffers from some actual or possible conflict of duty and interest (or duty and duty) when he does so, the transaction will not be void – the fiduciary had the requisite power – but the transaction can be set aside, subject to any applicable defences. If a transaction involves

[66] See, *e.g.*, *Burland* v. *Earle* [1902] A.C. 83; *Re Cape Breton Co. Ltd.* (1885) 29 Ch.D. 795; *Hely-Hutchinson* v. *Brayhead Ltd.* [1968] 1 Q.B. 549. The somewhat problematic successor to the self-dealing rule in company law is Companies Act 2006, s. 177.

[67] Companies Act 2006, s. 16, re-enacting earlier legislation.

[68] In this regard, see A.J. Oakley, *Constructive Trusts*, 3rd. ed. (London 1996), at pp. 146 *et seq.*, noting the texts cited there, and Part G(ii) below.

[69] See *Ingram* v. *IRC* [1997] 4 All E.R. 395 at p. 425, *per* Millett L.J.

[70] As regards the fair dealing rule, see *Tito* v. *Waddell (No. 2)* [1977] Ch. 106 at p. 241, *per* Megarry V.-C. There is a convincing argument that the fair dealing rule and the self-dealing rule are not separate rules but applications of the same principle to differing patterns of facts: M. Conaglen, "A Re-Appraisal of the Fiduciary Self-Dealing and Fair Dealing Rules" [2006] C.L.J. 366. That debate does not affect the point, however: only the self-dealing rule, or the pattern of facts where a fiduciary acts on behalf of his principal, is relevant for present purposes.

[71] For a comprehensive treatment of the issues raised in this paragraph, see Conaglen, "The Nature and Function of Fiduciary Loyalty" (2005) 121 L.Q.R. 452 and *Fiduciary Loyalty* (Oxford 2010, forthcoming).

both an excess or abuse of power and self-dealing, a claimant will be able to argue his claim on either basis, and, if necessary, elect between them.[72]

Self-dealing has attracted much attention in the cases.[73] In evidential terms, it is not difficult to make out a *prima facie* case that a fiduciary has breached the rule: a beneficiary or principal has merely to show the transaction happened in the stated circumstances of conflict. But the practical importance of the rule must not be overstated. It is possible to draft around the rule governing self-dealing in most if not all cases.[74] That weakens the practical impact of the rule. It may be, therefore, that claimants have to rely on other controls on fiduciary power, such as those described in the previous section, even in cases which, at first sight, might appear to involve self-dealing.

(ii) The Principle in Re Hastings-Bass [1975] Ch. 25

In *Sieff* v. *Fox*, Lloyd L.J. (giving judgment in the Chancery Division) recognised the *Hastings-Bass* principle as a distinct basis for setting aside the purported exercise of a power vested in trustees.[75] With respect, that must be right. The principle does not address the question of whether the trustees have exceeded their powers. It addresses the context within which they sought to exercise a power. It concerns action which was authorised, both in form and in substance, but nevertheless taken on the basis of incorrect or inadequate considerations. The principle has also been applied to directors in the context of company law.[76] though there is a nice question as to how (if at all) the principle has been subsumed into the new statutory codification of directors' duties enacted by Part 10, Chapter 2, of the Companies Act 2006.[77]

[72] As regards the general principle of pleading inconsistent cases, see, *e.g.*, *Oliver Ashworth (Holdings) Ltd.* v. *Ballard (Kent) Ltd.* [2000] Ch. 12 at p. 31, *per* Robert Walker L.J.; *A* v. *A* [2007] EWHC 99 (Fam) at [16], *per* Munby J. In the context of transactions that can be argued to be either void in equity or voidable, see *Baker* v. *Potter* [2004] EWHC 1422 (Ch) at [109], *per* David Richards J., distinguishing *Re Ciro Citterio Menswear plc* [2002] EWHC 662 (Ch), [2002] 1 B.C.L.C. 672. See also Part G(iii) below.

[73] This much is obvious even from a cursory glance at the footnotes in P. Finn, *Fiduciary Obligations* (Sydney 1977), M. Conaglen, "The Nature and Function of Fiduciary Loyalty" (above note 71), "A Re-Appraisal of the Fiduciary Self-Dealing and Fair Dealing Rules" (above note 70), and *Fiduciary Loyalty* (above note 71).

[74] For examples of such drafting, see (in the context of trusts) *Forms & Precedents* (above note 49), volume 40(1), at §[3583], and (in the context of company law) Table A (1985, *op. cit.* note 56) regs. 85–86, 94–98; and note Companies Act 2006, s. 175(5).

[75] [2005] EWHC 1312 (Ch), [2005] 1 W.L.R. 3811 at [38].

[76] *Hunter* v. *Senate Support Services Ltd.* [2004] EWHC 1085 (Ch), [2005] 1 B.C.L.C. 175. Application of the principle in company law is hard to justify in the light of *Harlowe's Nominees Pty. Ltd.* v. *Woodside (Lakes Entrance) Oil Company NL* [1968] HCA 37, (1968) 121 C.L.R.483 at p. 493, *per* Barwick C.J., McTiernan and Kitto J.J., and *Howard Smith Ltd.* v. *Ampol Petroleum Ltd.* [1974] A.C. 821 at p. 832, *per* Lord Wilberforce.

[77] See Dame Mary Arden *et al*, *Buckley on the Companies Acts*, 15th ed. (London 2008), §§[810]–[815], [866]. A court might be tempted to characterise the principle (at least in company law) as resting on an implied term of a company's constitution governing the exercise of power by directors, so as to fall within Companies Act 2006, s. 171(a), or as an aspect of the proper purposes doctrine, within s. 171(b). Alternatively, it might remain uncodified: s. 170(3) means that the codification of directors' duties is not necessarily exhaustive.

After a very thorough review of the prior authorities, Lloyd L.J. restated the *Hastings-Bass* principle as follows.

> Where trustees act under a discretion given to them by the terms of the trust, in circumstances in which they are free to decide whether or not to exercise that discretion, but the effect of the exercise is different from that which they intended, the court will interfere with their action if it is clear that they would not have acted as they did had they not failed to take into account considerations which they ought to have taken into account, or taken into account considerations which they ought not to have taken into account.[78]

There has been severe and telling criticism of the principle. It was originally used to determine whether a distribution of trust funds, which was deprived of its full intended effect by operation of law, should nevertheless stand so far as possible; yet it has come to operate as something of a "get out of gaol free" card for trustees who took, and then regretted, a decision that had its intended effect on the trust fund, but also had unintended and unpleasant collateral consequences – often to do with taxation.[79] In such a case, the result of the decision should stand (unless there are other reasons for setting it aside), though it might well expose the trustees to purely personal liability for breach of their duties of care and skill.[80] The *Hastings-Bass* principle can also operate capriciously, as it is often not clear what fiduciaries should or should or should not take into account when making a decision.[81] Nonetheless, the principle exists, at least for the moment, and it warrants explanation.

There has been much comment on the basis of the principle.[82] It is often compared to the law governing mistaken transactions. However, the fiduciary's mistake, or misapprehension, is not as to what he has done – for example, as to whether a trustee has exercised a power, such as a power of appointment or a power of advancement. It is, if anything, a mistake or misapprehension as to the factors which led the

[78] *Sieff* v. *Fox* [2005] EWHC 1312 (Ch), [2005] 1 W.L.R. 3811 at [119]. The *Hastings-Bass* principle does not apply to a mistaken failure to decide to act: *Breadner* v. *Granville-Grossman* [2001] Ch. 523.

[79] Lord Neuberger, "Aspects of the Law of Mistake", lecture to the Chancery Bar Association, London, 19th January, 2009.

[80] See Part E, below.

[81] R.I. Barrett, "The Principle in *Re Hastings-Bass*", lecture to Superannuation 2006, Melbourne, 23rd February, 2006.

[82] Lord Walker of Gestingthorpe, "The Limits of the Principle in *Re Hastings-Bass*" (2002) 13 King's College Law Journal 173; J. Hilliard, "*Re Hastings-Bass*: Too Good to be True?" (2002) 16(4) Trust Law International 202; D. Goodman and C. Groves, "Need Trustees' Mistakes Stand?" [2002] Private Client Business 102; B. Green, "The Law Relating to Trustees' Mistakes – Where Are We Now?" (2003) 17(3) Trust Law International 114; J. Hilliard, "Limiting *Re Hastings-Bass*" [2004] The Conveyancer 208; D.A. Hayton, "Pension Trusts and Traditional Trusts: Drastically Different Species of Trusts" [2005] The Conveyancer 229; Barrett, above note 81; H.W. Tang, "Rationalising *Re Hastings-Bass*: A Duty to Act on Proper Bases" (2007) 21(2) Trust Law International 62 and in H. Tijo (ed.) *The Regulation of Wealth Management* (Singapore 2008), 305.

fiduciary to act.[83] And in that, the principle raises difficult questions of evidence – what did the trustees (or directors) believe at the time, without the benefit, or influence, of hindsight – and difficult questions of law – just what should they have taken into account.[84] These problems are particularly acute in company law, where directors have traditionally been accorded great latitude in their decision making in response to the uncertainties they face.[85] Section 172 of the Companies Act 2006 may now reduce the scope of such problems: the section contains a non-exhaustive list of factors that directors should take into account when making decisions, though that list comes at the cost of encouraging procedural rigidity in the directors' deliberations.

Notwithstanding these difficulties, the principle in *Re Hastings-Bass*, as presently stated, resembles the self-dealing rule in various ways. Both the principle and the rule do not delimit the scope of a power; nor are they concerned with whether the power was exercised. Rather, they both address the process of decision making that antedates and lies behind action taken pursuant to a power.

Of course, it would be possible to make the principle go to the scope of a power by stipulating that the power only exists if the fiduciary has properly determined to exercise it: that is, by implicitly limiting the scope of the power. The authors of Underhill & Hayton conclude that proper decision making "is requisite for the exercise of a fiduciary power of appointment or advancement, and if not present the exercise will be void *in the absence of contrary intent in the trust instrument*".[86] A power could explicitly be limited so that the fiduciary only has such power if he has properly considered the circumstances relevant to his proposed action pursuant to the power; but that certainly does not mean this should be the default implication where no such words are used. Any such implied limitation on the power is very artificial: it does not sit easily with the words of a power, which are concerned with what may be done by the fiduciary, either generally or more specifically, rather than the decision-making behind any action.

There are, of course, also marked differences between the self-dealing rule and the principle in *Re Hastings-Bass*. The self-dealing rule is concerned with the risk of a flawed decision, whether or not the result of the decision proves objectionable. In consequence, a transaction falling within the scope of the rule is voidable *ex debito justiciæ*, without proof of unfairness, save in exceptional circumstances.[87] By contrast,

[83] See *Abacus Trust (Isle of Man) Ltd.* v. *Barr* [2003] EWHC 114 (Ch), [2003] Ch. 409 at [32], *per* Lightman J.
[84] See Barrett, above note 81.
[85] See the Australian authorities cited in note 76 above.
[86] Underhill & Hayton, *Law of Trusts and Trustees* (above note 5), §61.22, emphasis added.
[87] As regards the basic rule, see, *inter alia*, *Ex parte James* (1803) 8 Ves. 337 at p. 345, 32 E.R. 385 at p. 388, *per* Lord Eldon C.; *Wright* v. *Morgan* [1926] 1 A.C. 788 and *Tito* v. *Waddell (No. 2)* [1977]

the principle in *Re Hastings-Bass* is only triggered where the results of the decision, whether direct or indirect, differ from those which would have followed if the decision had not been flawed.[88]

Nevertheless, the two doctrines both address the process of making a decision to exercise a power. They are concerned with flaws or the risk of flaws in decision-making. Again, where a transaction involves both an excess or abuse of power and inadequate decision-making, so as to infringe the principle, a claimant should be able to argue his claim on either basis, and, if necessary, elect between them.[89]

E. Care and Skill

When trustees exercise their powers of management, they are undoubtedly under duties of reasonable care and skill. These arise in equity,[90] though in England and Wales the equitable duties have, to a large extent, been replaced by largely equivalent duties under the Trustee Act 2000. Similarly, company directors owe duties of reasonable care and skill. These duties were originally a matter of case law, evolving through a somewhat tortured process of development.[91] Whether they were strictly common law duties or equitable duties has been a matter of some debate,[92] though that question need not trouble the present discussion.[93] They are now statutory duties.[94]

Duties of care and skill indirectly control the exercise of power by fiduciaries. Want of due care and skill does not, of itself, vitiate a transaction, but rather exposes the fiduciary to a personal monetary liability for breach of his duty,[95] which is generally seen as a non-fiduciary duty.[96] Naturally, the fiduciary will not want to incur

Ch. 106 at p. 241, *per* Megarry V.-C. As regards exceptional circumstances, see *Holder* v. *Holder* [1968] Ch. 353; *Hillsdown plc* v. *Pensions Ombudsman* [1997] 1 All E.R. 862 at pp. 895–896, *per* Knox J. and *Public Trustee* v. *Cooper* [2001] WTLR 901 at p. 993, *per* Hart J.

88 *Sieff* v. *Fox* [2005] EWHC 1312 (Ch), [2005] 1 W.L.R. 3811 at [119], *per* Lloyd L.J., considered in *Smithson* v. *Hamilton* [2007] EWHC (Ch) 2900, [2008] 1 W.L.R. 1453 at [53], *per* Park J.

89 See note 72 above and its accompanying text.

90 *Re Whiteley* (1886) 33 Ch.D. 347, 355 *per* Lindley L.J., affirmed *sub nom. Learoyd* v. *Whiteley* (1887) 12 App. Cas. 727; emphasis added. See also *Cowan* v. *Scargill* [1985] Ch. 270, and *Nestle* v. *National Westminster Bank plc* [1994] 1 All E.R. 118, 140 (C.A.) *per* Leggatt L.J.

91 *Daniels* v. *Anderson* (1995) 37 N.S.W.L.R. 438 (NSWCA); *Re Barings plc (No. 5)* [1999] 1 BCLC 433; *Equitable Life* v. *Bowley* [2003] EWHC 2263 (Comm), [2004] 1 BCLC 180.

92 See *Daniels* v. *Anderson* (1995) 37 N.S.W.L.R. 438 (NSWCA), *Lagunas Nitrate Co. Ltd.* v. *Lagunas Syndicate* [1899] 2 Ch. 392 at pp. 435, 437, *per* Lindley L.J., and, more generally, W. Heath, "The Director's 'Fiduciary' Duty of Care and Skill: A Misnomer" (2007) 25 Company and Securities Law Journal 370.

93 In this regard, note *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145 at p. 205, *per* Lord Browne-Wilkinson.

94 Companies Act 2006, s. 174.

95 See, *e.g.*, *Learoyd* v. *Whiteley* (1887) 12 App. Cas. 727 and *Daniels* v. *Anderson* (1995) 37 N.S.W.L.R. 438 (NSWCA).

96 *Permanent Building Society* (*in liquidation*) v. *Wheeler* (1994) 14 A.C.S.R. 109 at pp. 157–158, *per* Ipp J.; *Colin Gwyer & Associates Ltd.* v. *London Wharf (Limehouse) Ltd.* [2002] EWHC 2748 (Ch), [2003] 2 BCLC 153 at [83], *per* Leslie Kosmin Q.C.; *Extrasure Travel Insurances Ltd.* v. *Scattergood* [2002] EWHC 3093 (Ch), [2003] 1 BCLC 598 at [87]–[90], *per* Jonathan Crow Q.C.

such liability, and in seeking to avoid it he will attempt to act with the requisite care and skill.

Of course, the fiduciary's negligence may be such as to raise evidential inferences that he had acted in bad faith, or for improper purposes, and so raise the question of whether his action was outside their authority. But that is a matter of evidential inference, rather than a direct response to any want of care and skill.

In principle, therefore, duties of care and skill do not necessarily go to the scope or exercise of a power: it is possible to exercise a power badly. The position is complicated, however, by the fact that the scope of authority can be defined as authority to something with due care and skill; and the consequence of that would be that negligent action would be outside the scope of authority.

There is some evidence that courts, on occasions, construed trustees' powers of sale in this way, though the terms of the trust, or statute law, sometimes relieved a purchaser of the consequences of breach.[97] Nowadays, authority to act should not be implicitly limited so as to confer authority to act competently but not otherwise. And if the authority were expressly so limited, the effect of that limitation on third parties should be restricted: at the very least, they should be entitled to assume that no such limitation exists unless they know to the contrary.

The reasons are clear. If a transaction could be undone by the principal of a fiduciary simply because the fiduciary's negligence meant that the transaction was unauthorised, the principal could escape bad bargains made on his behalf, or for his benefit, by the fiduciary. Yet if the principal had made the same bargain for himself, that would not be possible: regret over a bad bargain is not recognised in the case law as a reason to allow the bargain to be unpicked. It would be deeply unjust to allow one but not the other, and so favour the use of a fiduciary in the formation of transactions over direct dealings by principals.[98] Further, it would undermine the security of contracts and the two-party doctrine of mistake.[99]

F. Substantive Implications

An attempt to pick out themes from a very broad range of law is always risky: the law is rarely so precisely stated, or understood, to allow

[97] E.B. Sugden, *A Practical Treatise of Powers*, 8th ed. (London 1861), at p. 863; Bailey, "Trusts and Titles" [1942] *Cambridge Law Journal* 36 at pp. 38–39.

[98] An analogous criticism has been made of the principle in *Re Hastings-Bass*, which has been used to allow trustees to unpick transactions that had disadvantageous tax consequences where a similarly mistaken individual would not be able to do so: Underhill & Hayton, *Law of Trusts and Trustees* (above note 5), §61.24.

[99] *Bell* v. *Lever Brothers Ltd.* [1932] A.C. 161.

such an exercise to be undertaken with anything more than guarded optimism. Nevertheless, various themes emerge from the foregoing survey of the law.

(i) Commonalities of Technique

All the techniques for controlling power directly – that is, techniques concerning scope and decision making, but not duties of care and skill – are essentially negative in form. All of them prohibit or proscribe certain conduct, rather than directing or prescribing any particular action. It is exceptionally difficult to stipulate specifically and positively what a trustee managing a trust fund, or a director managing a company, should in fact do, without thereby abolishing managerial freedom: there are so many different circumstances which may arise in the course of conducting the undertaking, and so many different, unobjectionable ways of performing the undertaking; and neither the parties concerned, nor the courts, can easily predict them.[100]

However, the rejection of prescriptive duties to act, and to act with diligence, does not alone explain the proscriptive content of the controls on fiduciaries' power in English law: at first sight, it would appear that the law could have easily used broad, open-textured, open-ended prescriptive rules (for example, a duty to act in someone else's best interests) in order to control fiduciary managers without unduly limiting their discretion. However, such rules would still be very uncertain in their application, and therefore correspondingly likely to inhibit managerial activity. Instead, English law has concluded that it is more efficient to imply duties which remove specified conduct from the realm of the permissible, rather than to impose duties which stipulate in very broad terms the way in which that undertaking should be performed.

A negative, or proscriptive, formulation of the controls on fiduciaries' powers has another practical consequence. It means that the techniques of control can readily be transposed from one situation to another – for example, from the control of trustees to the control of company directors to the control of agents. The positive undertakings of various fiduciaries vary enormously: what has to be done by the trustee of a family settlement is very different from what an executive director of a publicly traded company has to do. The transposition of their positive duties to act therefore makes no sense at all; but it makes perfect sense to prohibit bad faith, improper purposes and the like in a whole variety of circumstances.

[100] Note Austin, (above note 24), at §§7.20–7.21.

(ii) Commonalities and Differences of Nature

The techniques examined in this paper all go to define, limit and control the power vested in fiduciaries. Which of these techniques themselves merit the description "fiduciary" is a vexed question, however. The answer to that question, as so often, depends on the criterion of discrimination used to establish both similarities and differences. And various different criteria can quite plausibly be put forward for that purpose.

Most recently, attempts to define what is a fiduciary obligation have focused on the principles regulating actual or possible conflicts between a fiduciary's duty to his principal and his self-interest or duties he owes to someone else. These so-called "conflicts rules" form an undisputed aspect of fiduciary doctrine.[101] They are necessary, in the strict logical sense, to any concept of fiduciary obligation, and so they form a firm basis from which to start an investigation of what fiduciary obligations might be. Indeed, the conflicts rules have been said to constitute the only true fiduciary obligations: the conflicts rules are said to be uniquely fiduciary.[102] If that is right, the techniques for controlling power held by a fiduciary which involve defining the scope of the power, as well as the principle of *Re Hastings-Bass*, all are non-fiduciary; and duties of care and skill are most certainly not fiduciary.

It is perfectly legitimate and sensible to use a criterion of uniqueness as the touchstone of what may be correctly described as a fiduciary obligation. But it is not the only way of determining when an obligation should be called "fiduciary". Another way to do that is to treat as fiduciary those obligations which invariably attach to a particular person because he has undertaken, or because the law requires him, to act for the benefit of another. These two approaches, as might be expected, yield very different answers.

The requirement that powers be exercised in good faith is not unique to fiduciaries: it also applies to other holders of a power.[103] Yet a fiduciary is always subject to this requirement.[104] To say that a person

[101] P. Finn, "The Fiduciary Principle", in D. Waters (ed.), *Equity, Fiduciaries and Trusts* (Toronto 1989); P. Finn, "Fiduciary Law and the Modern Commercial World", chapter 1 in E. McKendrick (ed.), *Commercial Aspects of Trusts and Fiduciary Relationships* (Oxford 1992); M. Conaglen, "The Nature and Function of Fiduciary Loyalty" (2005) 121 L.Q.R. 452 at pp. 454–460 and *Fiduciary Loyalty* (above note 71).

[102] *Ibid.*

[103] *Aleyn* v. *Belchier* (1758) 1 Eden 132 at p. 138, 28 E.R. 634 at p. 637, *per* Lord Northington. A few examples of powers that must be exercised in good faith suffice to make the point: *Allen* v. *Gold Reefs of West Africa* [1900] 1 Ch. 656 (shareholders' power to alter a company's articles of association); *Yorkshire Bank* v. *Hall* [1999] 1 W.L.R. 1713 (mortgagee's power of sale); *Paragon Finance* v. *Nash* [2001] EWCA Civ 1466, [2002] 1 W.L.R. 685 (mortgagee's power to set interest rates under the mortgage); *Redwood Master Fund Ltd.* v. *TD Bank Europe Ltd.* [2002] EWHC 2703 (Ch), [2006] 1 BCLC 149 (lenders' power to alter the terms of a loan syndication).

[104] *Armitage* v. *Nurse* [1998] Ch. 241; *Bristol & West BS* v. *Mothew* [1998] Ch. 1; *Item Software (UK) Ltd.* v. *Fassihi* [2004] EWCA Civ 1244, [2005] 2 BCLC 91.

may not act in circumstances where some interest or other obligation conflicts, or may conflict, with his duties, and yet to allow him to act in bad faith, simply makes no sense. Moreover, the content of this requirement – what actually amounts in a given case to good faith or bad faith action – will be informed by the fiduciary's undertaking to act in the interests of another, that is, by the very same fact which explains and justifies the application of the conflicts rules to the case. So an obligation of good faith action is part of the group of techniques that always controls the exercise of power by a fiduciary. It is necessary, but not sufficient, to identify a fiduciary; and it is a necessary part of ensuring due performance of the fiduciary's undertaking.

Like good faith, fraud on a power and the proper purpose doctrine are excluded from the realm of the fiduciary if that is taken to be those obligations which only attach to fiduciaries and no one else: the doctrine of a fraud on a power definitely applies to personal (that is, non-fiduciary) holders of power.[105] Again like good faith, these doctrines nevertheless apply to all instances of power held by a fiduciary: no fiduciary could conceivably be allowed to exercise a power for an improper purpose given that he is expected to act in the interest of another. And again, the determination of what is a proper or an improper purpose –that is, the scope of a power as limited by the purposes for which it was conferred – will be informed by the fiduciary's undertaking to act in the interests of another: that is, by the very same fact which explains and justifies the application of the conflicts rules in the case.

The principle of *Re Hastings-Bass* is rather more difficult to locate as a matter of doctrinal analysis. If the principle really is about adherence to the proper processes of decision-making, it does not appear to be part of fiduciary law in the exclusive sense – in the sense of obligations that attach exclusively to fiduciaries.[106] It is also not clear whether the doctrine is generally applicable to all fiduciaries: to date, it has been applied to express trustees and company directors.[107] However, in so far as it is possible to tell at this stage, it seems that the reason why proper decision-making is required according to the principle in *Re Hastings-Bass* is to make it more likely that the fiduciary will act in the best interests of his beneficiary. In other words, application of the principle in *Re Hastings-Bass* is informed by the fiduciary's undertaking to act in

[105] See (again) *Aleyn* v. *Belchier* (1758) 1 Eden 132 at p. 138, 28 E.R. 634 at p. 637, *per* Lord Northington; *Price* v. *Bouch* (1986) 53 P. & C.R. 257 (power to administer a scheme of development); *National Grid Co. plc* v. *Laws* [1997] OPLR 207 (powers of an employer company under a pension trust); *Yorkshire Bank plc* v. *Hall* [1999] 1 W.L.R. 1713; (mortgagee's power of sale); *Paragon Finance* v. *Nash* [2001] EWCA Civ 1466, [2002] 1 W.L.R. 685 (mortgagee's power to set interest rates under the mortgage). See, generally, Underhill & Hayton (above note 5), §1.76.

[106] Consider *Hunter* v. *Senate Support Services Ltd.* [2004] EWHC 1085 (Ch), [2005] 1 B.C.L.C. 175 at [165]–[173], *per* John Randall Q.C., addressing the similarity of the principle to the *Wednesbury* principles of public law.

[107] See Part D(ii) above.

the interests of another.[108] Against that, even a fiduciary who has made a decision in breach of the principle in *Re Hastings-Bass* can still fulfil his duty to act in good faith in what *he thinks* are the best interests of his beneficiary. On balance, though, it does seem that the principle serves to protect the integrity of the fiduciary's execution of his undertaking, in a manner functionally akin to the conflicts rules: after all, even someone in breach of the conflicts rules could, in principle, still fulfill his duty to act in good faith in what he thinks are the best interests of his beneficiary.

This leaves two techniques of controlling fiduciaries' powers still to consider: construction and duties of care and skill. Quite manifestly, neither of these techniques involves fiduciary obligations in the strict sense of obligations peculiar to fiduciaries alone. But neither are they directly informed by the fiduciary's undertaking to act in the interests of another.

As regards construction, clearly any power can only be understood once correctly construed. Construction is essentially about understanding words in context; and for present purposes, the context of the words conferring a power is the undertaking of a fiduciary. It is inevitable, therefore, that construction of a fiduciary's power will be to some extent influenced by his obligations to act in good faith in the interests of his principal. One example, noted earlier, is the principle that a person must not use power held in a fiduciary capacity to benefit himself unless allowed to do so. However, the process of construction of a fiduciary's powers will be more strongly informed by his undertaking itself – what functions he has, what tasks he is to accomplish – rather than the fact that his undertaking is to be accomplished in good faith for the benefit of someone else.

Finally, what of care and skill? While there are some arguments that a fiduciary's duties of care and skill are themselves fiduciary obligations,[109] leading modern judicial opinion in England,[110] supported by legal historical scholarship,[111] is that they are not fiduciary.

[108] *Smithson* v. *Hamilton* [2007] EWHC 2900 (Ch), [2008] 1 W.L.R. 1453 at [97], *per* Sir Andrew Park.

[109] J.S. Getzler, "Equitable Compensation and the Regulation of Fiduciary Relationships", in P. Birks and F. Rose (eds.), *Restitution and Equity* (London 2000), 235, "Duty of Care" in P. Birks and A. Pretto (eds.), *Breach of Trust* (Oxford 2002), 41, "Am I My Beneficiary's Keeper? Fusion and Loss-Based Fiduciary Remedies" in S. Degeling and J. Edelman (eds.), *Equity in Commercial Law: Volume 1* (Sydney 2005), 239; J.D. Heydon, "Are the Duties of Company Directors to Exercise Care and Skill Fiduciary?", *ibid.*, 185. Note also *Youyang* v. *Minter Ellison Morris Fletcher* [2003] HCA 15, (2003) 212 C.L.R. 484 at [39], *per curiam*.

[110] *Permanent Building Society* (*in liquidation*) v. *Wheeler* (1994) 14 A.C.S.R. 109 at p. 157, *per* Ipp J. The leading statement in English law to this effect was made by Millett L.J. in *Bristol & West BS* v. *Mothew* [1998] Ch. 1 at p. 18: see *Johnson* v. *EBS Pensioner Trustees Ltd.* [2002] EWCA Civ 164, [2002] Lloyd's Rep PN 309 at [37], *per* Mummery L.J.

[111] W. Heath, "The Director's 'Fiduciary' Duty of Care and Skill: A Misnomer" (2007) 25 Company and Securities Law Journal 370.

Furthermore, like techniques of construction, duties of care and skill may be moulded in their content to some extent by an appreciation that a fiduciary has to perform his tasks in good faith in the interests of his principal; but again, setting the standard of care and skill which the fiduciary must display when he acts for his principal will be more strongly informed by those very tasks, rather than the fact that he has to act in good faith for his principal.[112] The juridical nature of duties of care and skill may be common across legal categories;[113] but content of the duty – the standard of care and skill – expected of a trustee is very different from that expected of a director, which is in turn different from that expected of a solicitor, for example. That is simply because these various fiduciaries have very different jobs. Finally, it should be remembered that duties of care and skill can be excluded from any application to a fiduciary undertaking.[114] At most, therefore, they can only have a contingent connection to other obligations properly described as fiduciary.[115]

(iii) Summary

Different judges and commentators use different criteria to identify "fiduciary" obligations for different purposes; and there is nothing remotely wrong – or, indeed, unusual – about that. Sometimes, the object is to identify those obligations which are "uniquely fiduciary": that is, those which are necessarily found in connection with any relationship described as fiduciary *and* are sufficient to identify every relationship described as fiduciary. If that is the object of the exercise, then the conflicts rules are rightly identified as the "uniquely fiduciary" set of obligations.[116] But this is not the only way of looking at the law, nor is it always the most useful. Categorisation of any set of facts is a purposive activity: distinctions amongst that set of facts can be drawn in different places for different purposes. The word "fiduciary" may be used to describe obligations which invariably attach to a particular person because he has undertaken, or because the law requires him, to act for the benefit of another. As well as the conflicts rules, these obligations would include the requirements to exercise a power in good faith and for a proper purpose. However, the position of the principle in *Re Hastings-Bass* is rather less clear.

[112] Note *Permanent Building Society* (*in liquidation*) v. *Wheeler* (1994) 14 A.C.S.R. 109 at p. 158, *per* Ipp J.
[113] Note *Henderson* v. *Merrett Syndicates Ltd.* [1995] 2 A.C. 145 at p. 205, *per* Lord Browne-Wilkinson.
[114] *Armitage* v. *Nurse* [1998] Ch. 241.
[115] *Cf.* P. Birks, "The Content of Fiduciary Obligation" (2000) 34 Israel Law Review 3.
[116] See above note 101.

G. Remedial Implications

This section considers precisely what the courts can do in response to quash the exercise, or purported exercise, of power by a fiduciary. It does not address the personal liabilities which attach to the holder of the power or those who dealt with him. The pattern of these responses is clear: as should be expected, they reflect the reasons why some exercise or purported exercise of a power may be impugned.

Accordingly, the distinction between "void" and "voidable" turns on the reasons why a transaction or purported transaction can be questioned. If the flaw in what happened was that the fiduciary had no authority to act as he did, then *prima facie* his decision to act will be void in equity, and his action pursuant to that decision will also be treated as void in equity. If that result is not possible, then the fiduciary's decision to act will still be void in equity, consistently with principle, but the result of his actions (for example, the creation of new legal property) will necessarily fall to be treated as only voidable in equity. Context matters vitally to remedies. As will be seen, one good example of this situation is the improper allotment and issue of shares in a company. By contrast, if the fiduciary did have authority to do what he did, but he acted on the basis of a flawed decision, then his action should in principle be voidable: in private law at least, flawed exercise of authority is still an exercise of authority until set aside.

(i) Techniques which concern Scope

If a power is purportedly exercised beyond its scope, the purported exercise is in principle a nullity, though the operation of equitable defences may preclude a particular claimant from successfully making such an allegation and so give some effect to the purported exercise of the power. Furthermore, other rules of law may well apply to the acts which constitute the purported exercise of the power, and those rules may mean that the acts have some legal effect or consequences. Some examples serve to make these points much clearer.

Where a trustee makes a contract that is beyond his powers, that contract may well bind him at law, because the trustee is a juridical person, and so may make contracts unless subject to some particular disability. If the trustee makes the contract in breach of trust, the breach will not affect the *prima facie* validity of the contract itself; but it will mean that the trustee may not indemnify himself out of the trust fund when he comes to perform his obligations under the contract.[117]

[117] See, *e.g.*, *Hosegood* v. *Pedler* (1896) 66 L.J. Q.B. 18 at pp. 20–21; *Vacuum Oil Co. Pty. Ltd.* v. *Wiltshire* (1945) 72 C.L.R. 319 at pp. 324–325 and 335. See also *Donaldson* v. *Smith* [2006] EWHC 1290 (Ch) at [54].

Equally, where trustees make a contract in breach of trust, a court will not grant specific performance of the contract.[118]

If a trustee disposes of an asset outside the scope of his equitable powers, that disposition will not overreach the beneficiaries' interests: it is ineffectual in equity. However, the beneficiaries may be affected by the consequences of the disposition – for example, they may lose their rights to reclaim the asset because it is now owned at law by a bona fide purchaser for value without notice of the wrongfulness of the disposition.[119] All this is utterly obvious in cases where trustees dispose of an asset in the course of administering the trust. But the same principles apply where the trustees distribute trust assets to a beneficiary. So, for example, if a trustee purports to exercise a power of appointment outside its scope – however that may come about – the trustee's acts do not amount to an exercise of the power, but may have consequences at law.

A classic example of this is *Cloutte* v. *Storey*.[120] A power of appointment was purportedly exercised over a trust fund, but the appointment was actually in fraud of the power. The beneficiaries in default of appointment claimed that they were still entitled to the fund as against the assignee of the purported appointee. They won: the purported appointment was void, and so created no equitable title to the fund. The Court of Appeal did recognise, however, that if legal title to the trust assets had been transferred to the purported appointee, that would have been effective, and an assignee of that legal title might be able to make out a defence of bona fide purchase of the legal title for value without notice, so as to defeat the equitable rights of the beneficiaries in default of appointment.

The same principles apply in the context of directors' dealings; but their application is affected and shaped by the different context. Directors act as agents for their company in bringing about corporate transactions:[121] they are not trustees in the sense that they do not own property on behalf of the company.[122] Once again, acts of a director beyond his authority are *prima facie* void, not voidable, though various rules of law may nevertheless render those acts binding on the company. But in certain cases, for very specific reasons, the transaction is voidable rather than void. So, where a director makes a contract that is

[118] See, *e.g.*, *Turner* v. *Harvey* (1821) Jac. 169 at p. 178, 37 E.R. 814 at pp. 817–818 *per* Lord Eldon C., and *Dunn* v. *Flood* (1885) 28 Ch.D. 586 at pp. 594–595 *per* Fry L.J.

[119] See, generally, R.C. Nolan, "Understanding the Limits of Equitable Property" (2006) 1 Journal of Equity 18, drawing on C. Harpum, "Overreaching, Trustees' Powers and the Reform of the 1925 Legislation" [1990] C.L.J. 277.

[120] [1911] 1 Ch. 18. See in particular the judgment of Farwell L.J. at pp. 30–31.

[121] See, *e.g.*, *Hely-Hutchinson* v. *Brayhead Ltd.* [1968] 1 Q.B. 549 at p. 583, *per* Lord Denning M.R.

[122] See, *e.g.*, *Re Lands Allotment Co.* [1894] 1 Ch. 616 at p. 631 and p. 638, *per* Lindley and Kay L.J.J.

beyond his authority, it does not bind the company unless by operation of law, most likely through the doctrine of ostensible authority.[123]

Where the director abuses his powers in purporting to make a contract, the abuse is still relevant to the existence of his authority, though not in quite the same way.[124] If the counterparty to the purported contract knows about, or is put on inquiry as to, the director's bad faith or improper purposes, the purported contract does not bind the company:[125] it is then void, not voidable.[126] Otherwise, a contract made within the terms of the director's authority will bind the company, even though the director acted in bad faith or for improper purposes.[127] But in those circumstances the director cannot have actual authority to bind the company, because such action is not lawful as between the director and the company: "[a]ctual authority, express or implied, is binding as between the company and the agent, and also as between the company and others, whether they are within the company or outside it."[128] Nevertheless, the counterparty's rights do not necessarily stem from the doctrine of ostensible authority. Unless the counterparty knows of the director's breach of duty, or is put on inquiry about it, the counterparty is allowed to proceed on a footing (contrary to the facts) that the director still had actual authority at the relevant time.[129] Of course, the counterparty may still put forward a case based on the director's ostensible authority.[130]

There are perfectly good reasons why the law is more willing to uphold transactions made in abuse of authority than those made in excess of authority. In cases of excess, the flaw in the transaction deal could

[123] *Freeman & Lockyer* v. *Buckhurst Park Properties (Mangal) Ltd.* [1964] 2 Q.B. 480; *Hely-Hutchinson* v. *Brayhead Ltd.* [1968] 1 Q.B. 549.

[124] See, generally, P. Watts, "Deeds and the Principles of Authority in Agency Law" (2002) 2 Oxford University Commonwealth Law Journal 93 at pp. 96–98.

[125] *Bryant, Powis & Bryant, Ltd.* v. *Quebec Bank* [1893] A.C. 170 at p. 180, *per* Lord Macnaghten; *Hambro* v. *Burnand* [1904] 2 K.B. 10 at p. 25, *per* Romer L.J.; *Reckitt* v. *Barnett, Pembroke & Slater Ltd.* [1928] 2 K.B. 244 at pp. 257–260, *per* Scrutton L.J. (who refers to "clear notice of fraud" at p. 260), and at p. 262–265, *per* Sankey L.J. (reversed by the House of Lords, [1929] A.C. 176, holding that the scope of the agent's authority did not include the actions in question).

[126] *Heinl* v. *Jyske Bank* [1999] Lloyd's Rep. Bank. 511 (C.A.). In Australia, note *The Bell Group Ltd. (in liquidation)* v. *Westpac Banking Corporation* [2008] WASC 239 at [4462], *per* Owen J., who does not make the necessary distinction between cases involving contracts and cases involving allotments (as to which, see the text to note 134 below), citing authority concerning allotments (*Whitehouse* v. *Carlton Hotel Pty Ltd.* [1987] HCA 11, (1987) 162 C.L.R. 285 at [10], *per* Mason, Dean and Dawson J.J.) for a general proposition it does not support.

[127] *Bryant, Powis & Bryant, Ltd.* v. *Quebec Bank* [1893] A.C. 170 at p. 180, *per* Lord Macnaghten; *Hambro* v. *Burnand* [1904] 2 K.B. 10 at pp. 19–22, *per* Collins M.R., and at pp. 23–25, *per* Romer L.J.; *Reckitt* v. *Barnett, Pembroke & Slater Ltd.* [1928] 2 K.B. 244 at pp. 257–260, *per* Scrutton L.J.

[128] *Hely-Hutchinson* v. *Brayhead Ltd.* [1968] 1 Q.B. 549 at p. 583, *per* Lord Denning M.R. See also *Hopkins* v. *TL Dallas Group Ltd.* [2004] EWHC 1379 (Ch), [2005] 1 BCLC 543 at [88]–[89], *per* Lightman J.

[129] See above note 127.

[130] *Hopkins* v. *TL Dallas Group Ltd.* [2004] EWHC 1379 (Ch), [2005] 1 BCLC 543; *Criterion Properties plc* v. *Stratford UK Properties LLC* [2004] UKHL 28, [2004] 1 W.L.R. 1846. Indeed, the current edition of *Bowstead & Reynolds on Agency* (London 2006) seeks to use the doctrine of offensible authority to explain all these cases where the company (principal) is bound notwithstanding the director's (agent's) breach of fiduciary duty: §3-009.

have been discovered by looking at facts other than the agent's mental state: that is, by looking at the terms of the agent's power and comparing those terms with the agent's acts. In cases of abuse, the agent's mental state is the key fact: that is, his bad faith or his intention to use the power for purposes that are (objectively) improper. It is very difficult for the counterparty to discover the agent's mental state; so he should not be affected by it unless he knew about it, or had very good reason to suspect it. Unless the counterparty did know that the agent committed such a breach of duty, the risk of the agent's behaviour should fall on the principal: he entrusted his affairs to the agent in the first place and is much better placed than the counterparty to control the agent.

Where a director of a company disposes of legal title to the company's assets without authority, a simple trust is raised over those assets in favour of the company.[131] The company can then seek remedies founded on this trust, subject always to defences, such as an order that legal title to the assets be transferred back to the company. The same principles apply to a disposal made by the director in bad faith,[132] or for improper purposes.[133]

There are, however, some cases where directors have abused their powers which do not appear to conform to this pattern. In cases where directors have allotted and issued shares for improper purposes, the resulting issue of shares has been held to be voidable, not void.[134] In fact, these cases are perfectly intelligible in context.

What was at issue in the relevant cases was an issue of shares in a company by its directors. The directors' power to allot and issue shares is a statutory, legal, power granted to the company and vested in the directors.[135] Any exercise of that power operates to create an asset recognised as the object of legal property rights (*i.e.*, shares).[136] Equitable

[131] See, *e.g.*, *Russell* v. *Wakefield Waterworks Co.* (1875) L.R. 20 Eq. 474; *Selangor United Rubber Estates Ltd.* v. *Cradock (No. 3)* [1968] 1 W.L.R. 1555; *Belmont Finance Corporation* v. *Williams Furniture* [1979] Ch. 250, *(No. 2)* [1980] 1 All E.R. 393; *Rolled Steel Products (Holdings) Ltd.* v. *British Steel Corporation* [1986] Ch. 246; *Clark* v. *Cutland* [2003] EWCA Civ 810, [2003] 2 BCLC 393.

[132] See, *e.g.*, *J.J. Harrison (Properties) Ltd.* v. *Harrison* [2001] EWCA Civ 1467, [2002] 1 BCLC 162.

[133] See, *e.g.*, *Rolled Steel Products (Holdings) Ltd.* v. *British Steel Corporation* [1986] Ch. 246; *Eagle Trust plc* v. *SBC Securities Ltd.* [1993] 1 W.L.R. 484, *Eagle Trust plc* v. *SBC Securities Ltd. (No. 2)* [1996] 1 B.C.L.C. 121.

[134] *Hogg* v. *Cramphorn Ltd.* [1967] Ch. 254; *Bamford* v. *Bamford* [1970] Ch. 212. The voidable allotment may be ratified by ordinary resolution of the company in English law (*ibid.*), though *semble* not under Australian law according to *Residues Treatment & Trading Co Ltd* v. *Southern Resources Ltd (No. 4)* (1988) 51 S.A.S.R. 196.

[135] As regards the power itself, see Companies Act 2006, s. 617(2)(a), re-enacting earlier legislation, given effect through a company's constitution (see, *e.g.*, the model articles of association in the Companies (Model Articles) Regulations 2008 (SI 2008/3229), Schedule 1, Art. 22 (private company articles) and Schedule 3, Art. 43 (public company articles)). As regards vesting the power in the company's directors, see its constitution (*e.g.*, model articles, Art. 2 (private company articles and public company articles)).

[136] Companies Act 2006, s. 541, re-enacting earlier legislation.

doctrine has nothing to say about the nature and scope of a statutory power. Once the statutory power is exercised, and in consequence a person is put on the register of members, he becomes a member of the company, again by virtue of statute,[137] even though the directors' decision to allot and issue the shares would be void as taken in breach of fiduciary duty.[138] Equally, equity cannot remedy the situation by continuing to recognise a pre-existing equitable right to the shares, in order to justify reversing the transaction at law: there neither was, nor could be, any such right because the shares are a new item of property created by the allotment and issue. Nor can equity treat the shares as property improperly lost to the company and consequently held on trust for it: the shares never were, and never could lawfully be, issued to the company.[139] So the best equity could do was to hold that the transaction could be reversed – that is, to render it voidable.[140]

In fact, this is the consequence precisely presaged in *Cloutte* v. *Storey*.[141] That case considered (albeit strictly *obiter*) the exercise of a power to appoint a legal estate in land, as was possible before 1926,[142] rather than a power to allot and issue shares. Still, the key point for present purposes is that Farwell L.J. explicitly addressed the improper exercise of a *legal* power – a power which operates to create a legal proprietary interest. He confirmed that such an exercise of the power would be *voidable*: as a matter of authority, equitable doctrine did not go to define the scope of the power, so equity had to recognise the effect of the power to create new legal property and then reverse that effect.

The principle, therefore, is this. The basic response of equitable doctrine to a fiduciary who acts beyond the scope of his power is to regard his decision, and his consequent action, as a nullity, but only in so far as that is possible given the context. Sometimes the scope of a power is not limited by equitable doctrine: for example, where the power is conferred by statute. Sometimes a power may allow the creation of new legal property. If a power has both of these characteristics, and it is exercised within its terms, it will create new legal property. Even if the power was exercised improperly by equitable standards, those standards do not limit its scope and effect at law. So a

[137] See Companies Act 2006, s. 112, re-enacting earlier legislation.
[138] *Colin Gwyer & Associates Ltd.* v. *London Wharf (Limehouse) Ltd.* [2002] EWHC 2748 (Ch), [2003] 2 BCLC 153 at [91]–[93], *per* Leslie Kosmin Q.C.
[139] Companies Act 2006, ss. 658–659, repeating earlier legislation.
[140] See *Harlowe's Nominees Pty. Ltd.* v. *Woodside (Lakes Entrance) Oil Company NL* [1968] HCA 37, (1968) 121 C.L.R. 483 at p. 500, *per* Barwick C.J., McTiernan and Kitto J.J.
[141] [1911] 1 Ch. 18 at pp. 30–31.
[142] The possibility of a legal power of appointment over land was abolished in England and Wales by Law of Property Act 1925, s. 1(7). As to the effect of such legal powers, see *Coke on Littleton*, 271b note VII.

court cannot ignore what has happened; nor can it treat the property as subject to continuing rights or rights raised in favour of former owners. All it can do is to render what has happened voidable.

(ii) Techniques which concern Decision-Making

If a fiduciary did have authority to do what he did, but acted on the basis of a flawed decision, then his action should be voidable, rather than void, as a result. In private law at least, a flawed exercise of authority is still an exercise of authority unless and until set aside.

The self-dealing rule is a clear example of this approach. If trustees contract with one of their number and within their powers, the rule makes the contract voidable.[143] If trustees have a sufficiently wide power of sale and sell a trust asset to one of their number, but without due authorisation, then the sale is voidable at the instance of the beneficiaries, not void, subject always to the operation of available defences. The sale is a real sale at law; and the trustees have power in equity to make that sale, but they made it in circumstances where the conflict between their duty and self-interest creates such temptations that the sale must be regarded as flawed, unless duly authorised, and consequently voidable rather than void.[144] The same principle holds good for a company director who deals with his company: unless duly authorised, the resulting transaction is voidable, not void.[145]

If, as has been argued earlier,[146] the principle in *Re Hastings-Bass* concerns the flawed process by which the decision is reached, rather than a lack of authority, and these two concepts are not deliberately conflated, then action taken pursuant to a such a flawed decision should be voidable in equity, rather than void. This was the somewhat controversial conclusion reached by Lightman J. in *Abacus Trust (Isle of Man) Ltd.* v. *Barr*.[147] That conclusion found support in *Hunter* v.

[143] See, *e.g.*, *Dover* v. *Buck* (1865) 5 Giff. 57 at p. 63, 66 E.R. 921 at p. 924, *per* Stuart V.-C. and *Guinness plc* v. *Saunders* [1990] 2 A.C. 663 at pp. 697–698, *per* Lord Goff. Suggestions to the contrary in D. O'Sullivan *et al*, *The Law of Rescission* (Oxford 2008), at [1.65]–[1.69] are wrong. For a fuller refutation, see M. Conaglen, *Fiduciary Loyalty* (above note 71), Chapter 4, Part III.A.

[144] See, *e.g.*, *Campbell* v. *Walker* (1800) 5 Ves. 678 at p. 682, 31 E.R. 801 at p. 803, *per* Arden M.R.; *Dover* v. *Buck* (1865) 5 Giff. 57 at p. 63, 66 E.R. 921 at p. 924, *per* Stuart V.-C. Occasionally, no transaction ever occurs at law, because there was only one party involved, and he cannot transact with himself. However, this situation is rare, given the effect of Law of Property Act 1925, s. 72. Also, a power of sale cannot be exercised by a sole trustee in favour of himself because there is no genuine arm's length sale, within the terms of the power. In either such a case, the self-dealing rule cannot apply: there is no transaction to which it can respond. See the dissenting judgment of Millett L.J. in *Ingram* v. *IRC*, [1997] 4 All E.R. 395 at pp. 424–425, subsequently vindicated by the House of Lords, [2000] 1 A.C. 293.

[145] *Guinness plc* v. *Saunders* [1990] 2 A.C. 663 at pp. 697–698, *per* Lord Goff.

[146] See Part D(ii) above.

[147] [2003] EWHC 114 (Ch), [2003] Ch. 409. This decision was followed in *Gallaher Ltd.* v. *Gallaher Pensions Ltd.* [2005] EWHC 42 (Ch).

Senate Support Services Ltd.,[148] a case which concerned the actions of company directors. But it also has its firm critics.[149]

The practical importance of this distinction between void and voidable should not be overstated, however. Protection for third parties concerned by the action impugned is often said to be the reason for preferring "voidable" over "void".[150] Certainly, third parties can be protected by the bars to rescission of voidable action. Still, even if action is void in equity there are at least three ways of protecting third parties.[151] First, the court does not have to grant a declaration that action is void, with consequential relief: remedies may be withheld on established equitable principles such as laches and clean hands. Secondly, in the exercise of its Chancery jurisdiction, the court can grant relief on terms, where appropriate.[152] Thirdly, even if an act is void in equity, the legal consequences of the act remain unless and until reversed, and a third party may be able to prevent any reversal of those consequences, for example because he is a *bona fide* purchaser of a legal interest in the assets concerned for value without notice of the equities.

(iii) The Interaction of Remedial Responses

Still, so long as there are different equitable responses to flawed action by a fiduciary, interesting questions can arise about how those responses relate to each other. The answer in any case turns crucially on whether the fiduciary ever brought about a transaction at law.

Sometimes, the fact that a purported exercise of power is rendered void by equitable doctrine may have consequences at law. If an agent acts in bad faith, or commits a fraud on a power, he will have no actual authority to bind his principal at law. That may mean that no transaction ever occurs at law, though a transaction may result from the operation of other doctrines (for example, ostensible authority) on the same facts. If there is no transaction at law, questions of voidability in equity simply cannot arise.

But if a transaction has occurred at law, and the transaction can be characterised in equity as both void and voidable, what then is the consequence? An example is where trustees sell shares forming part of the trust fund to one of their number, but they have neither power to make the sale nor their beneficiaries' consent to it. In such a case, the

[148] [2004] EWHC 1085 (Ch), [2005] 1 B.C.L.C. 175.

[149] See the discussion in Underhill & Hayton, *Law of Trusts and Trustees* (above note 5), §61.18. Also note *Sinclair* v. *Moss* [2006] VSC 130 (Supreme Court of Victoria) at [79]–[84], *per* Byrne J.

[150] See, *e.g.*, *Hunter* v. *Senate Support Services Ltd.* [2004] EWHC 1085 (Ch); [2005] 1 BCLC 175 at [179], *per* John Randall Q.C.

[151] *Cf. Abacus Trust (Isle of Man) Ltd.* v. *Barr* [2003] EWHC 114 (Ch), [2003] Ch. 409 at [30], *per* Lightman J.

[152] See, *e.g.*, *Boardman* v. *Phipps* [1967] 2 A.C. 67 and *Maguire* v. *Makaronis* [1997] HCA 23, (1997) 188 C.L.R. 449.

trustees effectively transfer property at law;[153] but for reasons examined earlier, the transfer will both fail to overreach the beneficiaries' interests and be subject to the self-dealing rule.

The better view is that a claimant should be able to make either argument and, if necessary, elect between the two. What is at issue here are two sets of *arguments* about the application of equitable doctrine, not two sets of *facts*. Any inconsistency between arguments is to be resolved by election at judgment, not by any misplaced suggestion that the arguments constitute facts.[154] Likewise, the two responses to the two arguments – void and voidable – may be inconsistent, but that inconsistency need only be resolved at judgment: responses, unlike facts, are open to election.

H. Conclusion

Amongst the topics addressed in this paper, it is clear that the self-dealing rule and its cognates – the conflicts rules – have attracted the most attention over time. More recently, the principle in *Re Hastings-Bass* has drawn a good deal of comment. But other means of controlling the powers held by fiduciaries are vital and deserve more study for reasons of principle and practice. In principle, they are no less constraints on fiduciaries' power than the conflicts rules; and in practice, they may be more important than the conflicts rules which are often so radically modified in consensually established fiduciary relationships as to provide little practical constraint on the fiduciaries in question. That makes a clear understanding of the rules, their nature and their consequences all the more valuable. This article has sought to provide just that.

[153] Law of Property Act 1925, s. 72(4).
[154] See note 72 above and its accompanying text.