Problem scenario

Mr Sleeson, a solicitor, is a sole practitioner with access to his clients' accounts. He withdraws money from 'the client account' and places it in his own private bank account which he holds with the Nelson Westminster bank. Later, he withdraws monies from his private account and plays it at a casino in the city. He places the winnings and the original withdrawals in his private account at the bank. This happens regularly and the bank manager suspects that something may be amiss, but turns a blind eye to Mr Sleeson's activities.

Eventually, Mr Sleeson 'went for the big gamble', lost all his money, and was declared bankrupt. The casino manager had accepted his bets because he 'knew that solicitors made a lot of money'.

Advise Mr Sleeson's clients who now seek to recover their lost funds.

Guidance Mr Sleeson held his clients' monies on trust for his clients. It follows that he has breached this trust by placing those monies in his private bank account to be subsequently used to satisfy his gambling habit. The question for determination is whether the Nelson Westminster Bank, through the agency of Mr Sleeson's branch manager, could be held liable in equity to meet the claims of Mr Sleeson's defrauded clients.

The bank is a stranger to, and a commercial agent of, the trust. The courts have always been reluctant to visit such commercial agents with equitable liability based on trusts the existence of which was not reasonably apparent. The traditional reason for this reluctance is the fear that liability of this sort might discourage agents from offering their services, or else the fear that the free markets of the commercial world would become stultified by the need to make extensive and inappropriate enquiries of every party to every dealing. Nevertheless, a stranger to a trust might become liable to the beneficiaries of the trust in a number of ways. We shall consider some of these in turn.

First, trusteeship *de son tort*. This is a form of constructive trusteeship imposed upon a stranger, such as a bank, which deliberately takes it upon itself to intermeddle in the

affairs of a trust in such a way that the stranger can be said to have interposed itself into the position of trustee (*Mara* v *Browne*). Such a scenario is a far cry from the present case.

Secondly, a stranger might be held liable as a constructive trustee for the knowing receipt of trust property. This complicated head of liability may apply in the present case. We will consider it in detail next. Related to it is liability for inconsistent dealing with trust property.

Thirdly, and finally, a stranger might be held liable in equity for dishonestly assisting in a breach of trust. We shall consider this head of liability last.

Knowing Receipt

For the bank to be liable under this head it must be shown that the bank has 'received' trust property, and it must be shown that the bank knew that the trust property it had received had come to it in breach of trust. According to Millett J in *Agip (Africa) Ltd* v *Jackson* [1989] 3 WLR 1367 'receipt' necessitates that 'the recipient must have received the property for his own use and benefit'. Accordingly, if a bank acts as a mere conduit for monies the appropriation of the monies by the bank will not be relevant to the loss to the beneficiaries and the bank will not be said to have 'received' trust monies. On the other hand, if the bank uses the monies for its own ends, perhaps by reducing the debit balance of an overdrawn account, the bank will be said to have 'received' the property for the purpose of liability for 'knowing receipt'. Applying this to the present case, it follows that the bank will probably not be liable for knowing receipt if Mr Sleeson's account has always been maintained with a healthy credit balance. Assuming, however, that the bank has, at some time, received the trust monies in reduction of an overdraft, or in some other way for its own benefit, the next question is whether the bank can be said to have 'known' that it was receiving trust monies in breach of the trust. Certainly the bank will not be taken to know something merely because it has heard rumours or disputed claims (Carl Zeiss Stiftung), but the bank will be liable if its agent, the bank manager, should have been suspicious. According to Peter Gibson J in *Baden* v *Société Générale* [1983] BCLC 325 knowledge for the purpose of knowing receipt could be of five types:

(1) actual knowledge;
(2) wilfully shutting ones eyes to the obvious;
(3) wilfully and recklessly failing to make such enquiries as an honest and reasonable man would make;
(4) knowledge of circumstances which would indicate the facts to an honest and reasonable man; and
(5) knowledge of circumstances which would have put an honest and reasonable man on enquiry.

More recently, Megarry VC has stated that only types 1, 2 and 3 would suffice (Re Montagu's ST). He rejected types 4 and 5 because they did not evince 'want of probity' (dishonesty), which his lordship felt ought to be pre-requisite to the onerous nature of liability under this head. More recently still, Scott LJ in *Polly Peck International plc v Nadir (No. 2)* [1992] 4 All ER 769 stated that the Baden categories are not 'rigid categories with clear and precise boundaries. One category may merge imperceptibly with another'. For Scott LJ the real question which we ought to ask of the bank manager in the present case is whether he should have been suspicious. If he should have been, the bank will be liable, provided that 'receipt' is proven. A similarly pragmatic approach was taken by the Court of Appeal in *B.C.C.I. (Overseas) Ltd v Akindele* [2001] Ch 437, where their lordships held that it need not be established that the defendant had acted dishonestly, but merely that his conscience was affected by what he knew, so that it at some stage he retained the money for his own benefit in a way that was unconscionable. Whether the bank manager should have been suspicious is a question that is difficult to answer on the bare facts as we have them. We are told that he suspects 'something' may be amiss, but the authorities are fairly clear in agreeing that liability will not arise unless the bank manager had suspected something in the nature of a breach of trust. For this it is not, of course, necessary to show that the bank manager knew the precise terms of the trust. Perhaps the bank manager genuinely believed that Mr Sleeson had only ever used his own monies, perhaps in suspecting that something might have been 'amiss' he meant only that he feared Mr Sleeson's gambling would lead to a crisis in Mr Sleeson's own financial circumstances, and not that of trust beneficiaries.

If the bank is guilty of 'knowing receipt' it will be held liable as a constructive trustee, which means, *inter alia*, that it will have a duty to account to the beneficiaries, from the moment it knew of the breach of trust, for the monies it had received, and may have to pay compound interest thereon (see **Chapter 15**). In the present case the breach of trust occurred before the monies reached the bank and therefore it would be otiose to consider the possibility of liability for inconsistent dealing.

Dishonest Assistance

We now move on to consider the possibility that the bank might be liable for dishonestly assisting in Mr Sleeson's breach of trust. In the usual case this head of liability will only be considered if knowing receipt cannot be proved. Liability for dishonest assistance is also said to be liability 'as a constructive trustee', but in the light of the fact that accessories (almost by definition) do not hold or control trust property it is arguable that dishonest assistance should, in the future, give rise to tortious liability, by analogy to the tort of procurement of a breach of contract.

This head of liability was previously labelled 'knowing assistance in a dishonest design', the dishonesty being that of the fiduciary. Since *Tan* (see below) the conscientious scrutiny has been shifted onto the accessory, (the bank, and possibly the bank manager, in our case) who will be liable only if he has 'dishonestly assisted in a breach of trust'.
The four ingredients of this head of liability are:

(1) the existence of a trust;
(2) breach of that trust;
(3) assistance in the breach (a simple question of fact); and
(4) dishonesty.

The first three being undoubtedly satisfied in the present case, the crucial question is whether the bank manager has been dishonest, if he has been his dishonesty will almost certainly be imputed to the bank.

In the leading case of *Royal Brunei Airlines Sdn Bhd* v *Philip Tan Kok Ming* [1995] 3 WLR 64, an opinion of the Judicial Committee of the Privy Council, Lord Nicholls purported to apply an 'objective standard' of honesty, with the result that an accessory will be unable to escape liability on the ground that he sees nothing wrong in his behaviour. However, Lord Nicholls went on to introduce personal considerations into the test. He said that, 'when called upon to decide whether a person was acting honestly, a court will look at all the circumstances known to the third party at the time. The court will have regard to personal attributes of the third party such as his experience and intelligence, and the reason why he acted as he did'. In *Twinsectra* v *Yardley* [2002] 2 AC 164 the House of Lords (Lord Millett dissenting) held that this test is not wholly objective. On the contrary, their lordships held that the test allows the defendant to escape liability if *he did not realise* that his conduct would be considered dishonest by an objective onlooker. The Privy Council purported to follow *Twinsectra* in *Barlow Clowes International Ltd (in liquidation) v Eurotrust International Ltd* [2005] UKPC 37, but their lordships' reasoning in Barlow Clowes actually returns the law to the state it was in as a result of the Royal Brunei case, since it confirms that the test for dishonesty is essentially an objective one. It remains to be seen if the (misguided) *Twinsectra* attempt to introduce a subjective test of dishonesty will regain any ground in the future. The early signs are that it will not. Thus In *Starglade Properties Ltd v Nash* [2010] EWCA Civ 1314, the Court of Appeal confirmed that the standard by which 'dishonesty' is tested does not vary just because some people might think that the standard is set too high: 'There is a single standard of honesty objectively determined by the court. That standard is applied to specific conduct of a specific individual possessing the knowledge and qualities he actually enjoyed' [para.25]

The bank manager in the present case has given a reason why he acted as he did, it would fall to the court which hears his case to decide whether his failure to act on his suspicions was dishonest or not. Whether dishonesty is tested objectively or subjectively, a definitive finding of dishonesty cannot be reached on the brief facts before us.