James, a trustee for the Randolph estate, decided to use some of the trust money to build a private business for himself because he honestly believed that the slowdown in the property market in the UK meant that if he bought some property now, he would make a large profit in a few years from now and be able to pay back the trust. So he went to John, his good friend and banker, and told him that he needed the money to sort out his personal problems which John knew about and sympathized with. John invested the money and lost heavily. A few years later, Thomas and Jan, both beneficiaries under the trust, sued James and John to make good the loss. Advise John.

Suggested Answer

The first issue is whether there is any form of trust or fiduciary relationship, because that is essential for an "equitable remedy", such as a constructive trust: *Westdeutsche Landesbank v Islington BC*. James is a trustee, so there clearly is a fiduciary relationship. The Privy Council in AG *for Hong Kong v Reid* took the view that fiduciaries hold a "secret profit" under a constructive trust. In 2014 the Supreme Court extended this approach in *FHR European Ventures v Cedar Capital Partners*. If a fiduciary makes any kind of secret profit, whether from misusing trust property taking a bribe, receiving unauthorised commission or exploiting a business opportunity learned from their fiduciary position, it is held on constructive trust. That allows the beneficiaries, Thomas and Jan to use their proprietary interests to follow or trace the money taken from their trust and recover it from third parties such as John.

If James is a fiduciary, he has a strict duty not to profit from his fiduciary position and must not have conflicting loyalties: *Bristol & West BS v Mothew*. He should have promoted the interests of the trust and not taken money for himself, outside of his normal salary: *Boardman v Phipps*. According to *Reid* and *Phipps*, above, James has a duty to account and holds any money that he has made from the investments on constructive trust for Thomas and Jan.

So Thomas and Jan could probably successfully sue James, but as he might no longer have the money, they might wish to sue the other party involved, John. *Barnes v Addy* requires either knowing receipt of trust property (category 2) or knowing assistance in a dishonest and fraudulent design (category 3).

John has clearly assisted James, but which category in *Barnes v Addy* does this place John in? John may not have made any claim to the money for himself and no longer has the money, so this puts him into the third category of constructive trust in *Barnes v Addy* according to *AGIP (Africa) v Jackson*. The fact that John may no longer have the money does not matter for this category of constructive trust. That is why cases such as *Selangor v. Cradock* and *Central Bank of Nigeria v Williams* suggest that these are not true trusts.

Liability for dishonest assistance used to depend upon proving that defendants such as John had knowledge of the breach of trust, but there was confusion as to whether the knowledge had to be actual or constructive, as in *Selangor v Cradock*. Because of that difficulty the courts changed the test of liability and, nowadays, the case law centres on the meaning of “dishonesty”. The new test has also caused problems! *Royal Brunei v Tan*, a Privy Council case, set an objective standard of dishonesty, as did another case from the same court, *Barlow Clowes v Eurotrust*. By this standard John would probably be liable. The House of Lords required more in *Twinsectra v Yardley*. John would also have to be aware that what he did was wrong, a subjective standard of dishonesty, a kind of mens rea borrowed from criminal law. Under this test he might escape liability. So it depends which line of authority the courts follow. The Court of Appeal case, *Abou-Rahmah v Abacha*, suggests that the courts of England and Wales will follow *Royal Brunei v Tan* making John liable. Another Court of Appeal case *Sinclair Investments v Versailles Trade*, supports the same interpretation of the dishonesty test.

It is also possible that John has received money for his own use and therefore also falls under the second category in *Barnes v Addy*, The test of liability under this category is not “dishonesty”, but “knowledge”. He must have knowledge that the money was obtained through a breach of trust to be liable. Older cases, such as *Re Polly Peck No.2*, were willing to assume, from the circumstances, that defendants must have known what was going on. More modern cases, such as *Re Montague* and *BCCI v Akindele*, require Thomas and Jan to prove that John actually knew where the money came from. From the facts, it seems likely that John did know, so in the words of *Akindele*, it is “unconscionable” for him to keep the money.

As a trustee, James is clearly liable for a breach of his fiduciary duty. John might also be liable as a constructive trustee, if he knew that James was not entitled to remove the money form the trust.