Michaelmas Term
[2022] UKPC 36
Privy Council Appeal No 0119 of 2019

JUDGMENT

Equity Trust (Jersey) Ltd (Respondent) *v* Halabi (in his capacity as Executor of the Estate of the late Madam Intisar Nouri) (Appellant) (Jersey)

ITG Ltd and others (Respondents) *v* Fort Trustees Ltd and another (Appellants) (Guernsey)

From the Court of Appeal of Jersey and the Court of Appeal of Guernsey

before

Lord Reed
Lord Briggs
Lady Arden
Lord Stephens
Lady Rose
Lord Richards
Sir Nicholas Patten

JUDGMENT GIVEN ON
13 October 2022

Heard on 15, 16 and 17 June 2021

Appellant (Halabi)
Shân Warnock-Smith KC
Clare Stanley KC
Damian James
Simon Hurry
(Instructed by Collas Crill LLP (Jersey) and Sinclair Gibson LLP)

Appellants (Fort Trustees Ltd and another)
John Machell KC
Nicholas Robison
(Instructed by Babbé LLP and Lee Bolton Monier-Williams)

Respondent (Equity Trust (Jersey) Ltd)
Emma Jordan
James Goodwin
(Instructed by Taylor Wessing LLP (London))

Respondents (ITG Ltd and Bayeux Ltd)
Simon Taube KC
Jeremy Wessels
James Brightwell
Thomas Fletcher
(Instructed by Macfarlanes LLP)

Appellants
(1) Fort Trustees Ltd
(2) Balchan Management Ltd

Respondents
(1) ITG Ltd
(2) Bayeux Ltd
(3) [Glenalla Properties Ltd]
(4) [Thorson Investments Ltd]
(5) [Eliza Ltd]
(6) [Oscatello Investments Ltd]
(7) [Geneva Trust Company]
(8) [Helen Green and Kelvin Hudson (Joint Receivers)]

LORD REED:

1. As is more fully explained in the judgment of Lord Richards and Sir Nicholas Patten, these appeals raise a number of issues, principally concerning the nature and scope of the right of a trustee under Jersey law to recover from or be indemnified out of the trust assets in respect of liabilities and expenditure which he or she has incurred in the capacity of trustee.

2. The principal issues can be summarised as follows:

    1. Does the right of indemnity confer on the trustee a proprietary interest in the trust assets?

    2. If so, does the proprietary interest of a trustee survive the transfer of the trust assets to a successor trustee?

    3. If so, does a former trustee's proprietary interest in the trust assets take priority over the equivalent interests of successor trustees?

    4. Does a trustee's indemnity extend to the costs of proving its claim against the trust if the trust is "insolvent", in the sense that trustees' claims to indemnity exceed the value of the trust fund?

3. The Board's account of the background circumstances, and its reasoning and conclusions in relation to the first, second and fourth issues, are set out in paras 5-166, 214-224 and 233-237 of the judgment of Lord Richards and Sir Nicholas Patten: that is to say, the whole of their judgment, apart from the sections concerning the third issue. All the members of the Board agree with their judgment to that extent.

4. In relation to the third issue, the members of the Board are divided. One view, favouring the prioritisation of trustees' claims according to the chronological order in which they were appointed, is expressed in the judgment of Lord Richards and Sir Nicholas Patten, with whom Lord Stephens agrees. Another view, favouring the pari passu ranking of trustees' claims to be indemnified out of the trust fund, is expressed in the judgment of Lord Briggs, with whom Lady Rose and I agree. Lady Arden, in a concurring judgment on this issue, also favours pari passu ranking, for reasons which are largely but not entirely consistent with those of Lord Briggs. The decision of the Board on the third issue is therefore that the trustees' claims rank pari passu. The

reasoning in support of that decision is set out in the judgment of Lord Briggs, in so far as it is consistent with Lady Arden's judgment. As I understand their judgments, that means that the reasoning of the majority is set out in Lord Briggs's judgment at paras 238-240, 254-268, 270 and 272-278.

LORD RICHARDS AND SIR NICHOLAS PATTEN (with whom Lord Stephens agrees, and Lord Reed, Lord Briggs, Lady Arden and Lady Rose agree in part):

5. This judgment concerns two unconnected appeals which have been heard together. They raise common issues about the nature and scope of the right of a trustee under Jersey law to recover from or be indemnified out of the trust assets in respect of liabilities and other expenditure properly incurred by the trustee. Although the proceedings giving rise to the appeals have been brought, in one case, in Jersey and, in the other case, in Guernsey, the trusts in both cases are governed by Jersey law and it is common ground that, on these appeals, no issues of Guernsey law arise. We will refer, as appropriate, to the Jersey appeal and to the Guernsey appeal.

6. Although a trustee's right of indemnity is well established in English law and is confirmed by section 26(2) of the Trusts (Jersey) Law 1984 ("the TJL"), the particular context which has given rise to controversy in the present appeals is that of insolvency in the sense of the assets of the trusts being insufficient in amount to permit the reimbursement of all of the legitimate expenditure and liabilities of the relevant trustees.

7. In both cases there is a contest between successive trustees as to their respective entitlement to be indemnified out of the available assets. This has given rise to argument as to what is the correct method under Jersey law of dealing with trust liabilities in such circumstances and in particular with whether the trustee who is first in time enjoys priority for its claim over those of subsequent trustees and their creditors.

8. Much of the argument on this issue centres on the nature (and even the existence) of what in the English authorities is commonly referred to as the trustee's lien. This is relied on by the respondents in both appeals as giving the trustee a form of proprietary interest in the trust assets which ranks in priority to those of the beneficiaries and any subsequent trustees. The appellants' primary case is that a former trustee has no proprietary or security interest in the trust assets, except to the extent that it has negotiated and obtained some specific security interest as a means of protecting its position in respect of future or undischarged liabilities prior to transferring the assets to its successor trustee. Any subsisting rights of indemnity must

be pursued against the trustee for the time being and will rank pari passu with all other relevant claims for indemnity and reimbursement.

9. The appellants' position is inconsistent with what was said in an earlier judgment of the Board in one of the two cases under appeal. In *Investec Trust (Guernsey) Ltd v Glenalla Properties Ltd* [2019] AC 271 ("*Investec 1*") the Board had to consider the extent to which the unlimited personal liability of a trustee under English law for claims by creditors has been modified by article 32 of the TJL (as substituted by article 11 of the Trusts (Amendment No 4) (Jersey) Law 2006). This provides:

> "32. Trustee's liability to third parties
>
> (1) Where a trustee is a party to any transaction or matter affecting the trust -
>
> (a) if the other party knows that the trustee is acting as trustee, any claim by the other party shall be against the trustee as trustee and shall extend only to the trust property;
>
> (b) if the other party does not know that the trustee is acting as trustee, any claim by the other party may be made against the trustee personally (though, without prejudice to his or her personal liability, the trustee shall have a right of recourse to the trust property by way of indemnity).
>
> (2) Paragraph (1) shall not affect any liability the trustee may have for breach of trust."

10. The Board held that article 32(1)(a) has the effect, in the case of liabilities to parties who know that the trustee is acting as trustee, of abrogating the rule of English law that the liability is enforceable against the trustee personally. For claims falling within article 32(1)(a), the trustee becomes liable only in his fiduciary capacity and they are enforceable only to the extent that there are trust assets sufficient to meet the claims. But a creditor does not obtain any right which he can pursue in rem against the trust assets. It continues to be the position that he can access the trust assets only by way of the trustee's right of indemnity.

11. As part of the judgment of the Board, Lord Hodge summarised some principles of English law, relevant to the issues of liability then under consideration. At [59](v) he said:

> "(v) A trustee is entitled to procure debts properly incurred as trustee to be paid out of the trust estate or, if he pays it in the first instance from his own pocket, to be indemnified out of the trust estate: *In re Blundell* (1888) 40 Ch D 370, 376. To secure his right of indemnity, the trustee has an equitable lien on the trust assets: *Lewin on Trusts*, 19th ed (2015), para 21-043. Because an equitable lien does not depend on possession, it normally survives after he has ceased to be a trustee: *In re Johnson; Shearman v Robinson* (1880) 15 Ch D 548, 552."

12. The appellants on these appeals do not take issue with the principles set out by Lord Hodge at para 59, except that they invite the Board to re-consider what is said in the second and third sentences of para 59(v), which they submit is not supported by authority and is wrong.

The appeals

13. Before turning to the issues, it is necessary to set out a brief summary of the facts and procedural history in the two appeals and to explain some of the more peripheral issues peculiar to each appeal which may also need to be considered.

Halabi v Equity Trust (Jersey) Limited (the Jersey appeal)

14. Eight discretionary trusts governed by Jersey law were established by the late Madam Intisar Nouri. Two of those trusts, the Ironzar II Trust and the Ironzar III Trusts, are relevant to the Jersey appeal. The respondent to this appeal, Equity Trust (Jersey) Ltd ("ETJL"), was the original sole trustee of the Ironzar II Trust from 10 December 2004 until it retired on 11 October 2006, and of the Ironzar III Trust from 23 December 2005 until its retirement on 26 October 2006.

15. The principal issues, relating to the nature and priority of a former trustee's right of indemnity, arise in respect of ETJL as the trustee of the Ironzar II Trust. Another issue, whether a trustee's indemnity extends to the costs of proving its claim against

the trust if the trust is "insolvent", arises in relation to ETJL as trustee of the Ironzar III Trust.

16. Under the provisions of the TJL as it stood in 2006 ETJL was obliged to transfer the trust assets to the new trustee: see articles 19(5) and 34(1). But it was also entitled to be provided with reasonable security for existing, future and contingent liabilities before surrendering the trust property: see article 34(2) (now article 43A(1)) of the TJL and clause 16(e) of the Ironzar II trust deed. Clause 18(b) of the trust deed also provides that an outgoing trustee is entitled to be indemnified out of the trust fund for all obligations and liabilities for which he would have been entitled to an indemnity had he still been a trustee and the incoming trustee is empowered to provide such an indemnity and to charge or deposit the whole or any part of the trust fund as security for it.

17. Pursuant to these provisions ETJL entered into a Deed of Appointment and Removal dated 11 October 2006 ("the DORA") with its successor Volaw Corporate Trustee Ltd ("Volaw") as trustee of the Ironzar II Trust. The DORA contained a release and indemnity in favour of ETJL and provided for the sum of £2.5m to be held by Volaw as security for the liability. Under clause 8 ETJL was to enter into all documentation to transfer and novate to Volaw all the assets and liabilities of the trust.

18. In July 2012 the liquidators of Angelmist Limited ("Angelmist"), a company within the Ironzar II Trust structure, brought proceedings for breach of fiduciary duty against two of its former directors who had also been employees of ETJL at the relevant time. ETJL was made a defendant to the claim on the basis that it was vicariously liable for the acts of its employees. The claim (with interest) totalled some £53m.

19. On 22 April 2013 ETJL gave notice to Volaw that it intended to rely upon the indemnities contained in the DORA. Volaw subsequently sought directions from the Royal Court in relation to the winding-up of the trust on the basis that its liabilities exceeded the value of the trust assets. In October 2015 Volaw retired as trustee and was replaced by Rawlinson & Hunter Trustees SA, now called Geneva Trust Company SA ("GTC").

20. In December 2015 the parties to the Angelmist proceedings entered into a settlement under which ETJL has paid £16.5 m to the liquidators of Angelmist. It was a term of the settlement that each party to the proceedings would bear their own costs. ETJL seeks to recover, from the assets of the Ironzar II Trust, a total of £18.9m, made

up of the £16.5m paid to Angelmist and some £2.4m in respect of its costs of the proceedings.

21. On 20 October 2015 the Royal Court had directed the trial of the issue whether ETJL had priority in relation to its indemnity claim which at that time was contingent on the outcome of the Angelmist proceedings ("the priority issue"), both as regards its own creditors and as regards the subsequent trustees. On 23 May 2017 the Royal Court directed that further questions should be dealt with, including whether a trustee of an insolvent trust should bear its own costs of proving its claim ("the recoverable costs issue").

22. The Royal Court directed that the priority issue should be determined on the basis of three principal assumptions:

(i) ETJL was and is entitled to be indemnified from the assets of the Ironzar II Trust in relation to all liabilities and costs arising from or in relation to the Angelmist proceedings.

(ii) In relation to the claim in the Angelmist proceedings, ETJL did not enjoy the protection of article 32(1)(a) of the TJL so as to limit the claims to the available trust assets.

(iii) All of the other liabilities incurred by the successive trustees fell within article 32(1)(a).

23. The trial of the priority issue took place in March 2018 and in a judgment handed down on 3 July 2018 ((2018) (2) JLR 81) the Royal Court (Clyde-Smith Commr) determined the issue as follows:

(i) As between a trustee and its own trust creditors:

(i) the claims of article 32(1)(a) creditors to the trust assets rank pari passu inter se;

(ii) in the case of a solvent trustee, the claims of article 32(1)(a) creditors to the trust assets rank pari passu with the trustee's claims for its article 32(1)(b) liabilities; and

(iii) in the case of an insolvent trustee, the claims of article 32(1)(a) and (b) creditors to the trust assets rank pari passu.

(ii) As between former and successor trustees and their respective creditors, the claims against all trustees and the liabilities of all trustees rank pari passu.

(iii) Alternatively, a trustee's right of indemnity and lien arise on a liability by liability basis with the trustee acquiring successive rights of indemnity and lien as it incurs liabilities.

24. In a further judgment handed down on 10 September 2018 ((2018) JRC 164) on the recoverable costs issue, the Royal Court held that a former trustee claiming under its right of indemnity was not entitled to claim the costs of proving its claim.

25. ETJL appealed with the leave of the Royal Court and in a judgment handed down on 28 June 2019 ((2019) JCA 106) the Court of Appeal (Sir William Bailhache, Bailiff, Martin JA and Logan Martin JA) reversed the decision of the Royal Court and held on the priority issue that:

(i) A trustee has a single right of indemnity and lien which arises as an incident of it taking office and covers all liabilities which a trustee may properly incur in its office;

(ii) As between successive trustees, a former trustee's right of indemnity and lien ranks ahead of a successor trustee's right of indemnity and lien on a first in time basis.

26. Although the ranking of the claims of trust creditors inter se and the ranking of the claims of a trustee and its trust creditors were live issues decided at first instance,

they had ceased to be so by the time of the hearing before the Court of Appeal. Logan Martin JA said at para 125 that it was "in practical terms academic in the circumstances of this case" and at para 212 that it was "the subject of much less attention before this court". However, because these issues had been the subject of some submissions to the court, he expressed what he described as obiter conclusions. These are not issues that arise in the Jersey appeal, because there are no longer any relevant trust creditors. No submissions were made to the Board on these issues and the Board expresses no views on them. Nor are there any creditors of the respondent former trustees in the Guernsey appeal, although there are, as we understand it, creditors of the appellant trustees. In view of the Board's decision in the Guernsey appeal, it is also not an issue arising for decision in that appeal, and the Board accordingly expresses no view on it.

27. On the recoverable costs issue, the Court of Appeal held that ETJL's costs of proving its claim fell within its right of indemnity and associated lien and that it was entitled to recover them from the trust fund in priority to other creditors.

28. Unconditional leave to appeal to the Board was granted on 23 September 2019 both in relation to the priority issues as between successive trustees (and as between a trustee and its own creditors) and also in relation to the recoverability of a trustee's costs of proving its claim.

Investec Trust (Guernsey) Ltd v Glenalla Properties Ltd (the Guernsey appeal)

29. A detailed summary of the background facts in these proceedings is contained in the judgment of the Board in *Investec 1*. What follows is a summary of the facts and procedural history relevant to the issues which have given rise to this further appeal.

30. These proceedings concern the Tchenguiz Discretionary Trust ("the TDT"). This is a discretionary trust which was established on 26 March 2007 under the laws of Jersey. The principal beneficiaries are Mr Robert Tchenguiz and his children and remoter issue. Mr Tchenguiz is also the protector of the TDT.

31. Investec Trust (Guernsey) Ltd ("ITG") was appointed as the original trustee of the TDT on 26 March 2007, and on 21 August 2007 Bayeux Trustees Ltd ("Bayeux") was appointed as a co-trustee (together "I&B"). Both were removed by the protector on 2 July 2010 and replaced by Geneva Trust Company SA ("GTC"). On 3 October 2017 GTC was also removed by the protector and replaced by Fort Trustees Limited and Balchan Management Limited ("F&B") which are the current trustees.

32. On 20 August 2007 ITG as trustee of the TDT entered into a short-term loan agreement with Kaupthing Bank HF ("Kaupthing") in the sum of £100m. On 24 August ITG as the trustee of the Tchenguiz Family Trust ("the TFT"), a trust governed by the law of the British Virgin Islands, appointed various assets notionally allocated to Mr Tchenguiz under the TFT to itself and Bayeux ("I&B") to be held on the trusts of the TDT. These included shares in 30 companies incorporated in the British Virgin Islands and various loans owed to the TFT. At the same time a deed of novation was entered into between ITG as the trustee of the TFT, I&B as trustees of the TDT and Kaupthing, under which I&B assumed the liability under the 20 August 2007 loan agreement.

33. Further liabilities were novated to I&B under these arrangements, including loans due to two companies, Glenalla Properties Ltd ("Glenalla") and Thorson Investments Limited ("Thorson") (together "the BVI companies"). These loans were stated to be in the sums of €78.825m and £80.541m respectively.

34. On 26 April 2010 the liquidators of the BVI companies demanded repayment of the sums due to them from I&B. Prior to that, on 12 March 2010, I&B had issued proceedings in Guernsey seeking the determination by the court of whether they had incurred liabilities to Glenalla and Thorson. They also sought declarations against the BVI companies that pursuant to article 32(1)(a) of the TJL they had no personal liability in respect of the claims of the BVI companies so that the claims extended only to the assets of the TDT that remained available to satisfy them.

35. In July 2010 I&B were given permission to amend the application by joining GTC, which had by then replaced them as trustee, as a defendant and adding a claim for an indemnity against the assets of the TDT. I&B asserted a lien over all of the assets of the TDT that were in their possession at the time of their replacement as trustees and the right to retain the trust assets pursuant to clause 10.4 of the trust instrument.

36. On 23 December 2013 an order was made appointing joint receivers over various trust assets including the shares in some 30 companies and an amount of cash. The order provided that the BVI companies were subrogated to the rights of I&B to retain, get in and realise the assets of the TDT and that the appointment of the joint receivers was without prejudice to such rights of indemnity as I&B and GTC might be entitled to under article 26(2) of the TJL.

37. In judgments delivered on 27 June and 29 October 2014, the Guernsey Court of Appeal (McNeill JA, Martin JA, and Logan Martin JA) (2014) GLR 121; (2014) GLR 371) held that I&B were entitled to rely on article 32(1)(a) in respect of the claims by the BVI companies.

38. Leave was given to appeal to the Board in relation, inter alia, to the decision of the Court of Appeal that article 32(1)(a) applied to the claims by the BVI companies. The appeal was dismissed in accordance with the advice of the Board in *Investec 1*.

39. On 15 October 2018, in proceedings commenced by the BVI companies for the identification and determination of various claims against the assets of the TDT, the Royal Court directed that any party who wished to make such a claim should submit a proof of debt to the joint receivers by 25 January 2019. Proofs of debt were submitted by a number of parties including I&B, GTC, F&B and the BVI companies. I&B's proof of debt relates to the legal costs incurred in the proceedings against the BVI companies together with unpaid remuneration. The proof of debt submitted by the BVI companies relates to the judgment debts and costs orders in the proceedings against I&B.

40. On 22 March 2019, as part of a confidential settlement with Kaupthing, F&B as trustees of the TDT took an assignment from the BVI companies of the debts due to them from I&B ("the BVI debts") and gave formal notice of the assignment to I&B and the joint receivers. On 28 March 2019 they submitted proofs of debt in their capacity as trustees in respect of the assigned debts. As at 28 June 2019 the value of the realisable assets of the TDT was stated by the joint receivers to be between £55m and £60m.

41. On 2 May 2019 the Royal Court identified various issues for determination. These included the effect of the 22 March 2019 assignment on the recoverability of the BVI debts; the order of priority for the payment of these liabilities as between a former trustee (and its creditors) and a successor trustee (and its creditors); and the order of priority as between a trustee and its own trust creditors. Orders were subsequently made for the transfer of £41,500,000 (later amended to £36,726,550.90) out of the trust assets into accounts controlled by the joint receivers in order to secure the third-party claims. The joint receivers were ordered to transfer the other trust assets within their control to F&B without prejudice to the indemnity claims by I&B and GTC.

42. In a judgment handed down on 9 December 2019 Lieutenant Bailiff Marshall QC held that:

> (i) The claims of a former trustee and its trust creditors take priority over those of a successor trustee in accordance with the decision of the Jersey Court of Appeal in *In re Z 11 Trust* (2019) JCA 106 (later upheld by the Board in *Investec 1*).

(ii) The claims of a trustee or former trustee in exercise of its right of indemnity against the trust assets take priority over unpaid creditors of the trustee claiming by way of subrogation to the trustee's right of indemnity. The claim for unpaid remuneration also ranks ahead of the claims of the creditors.

(iii) The effect of the March 2019 assignment to F&B was to extinguish the BVI debts because of the merger of identity between the party holding the right to receive the debt and the party with the obligation to pay them.

43. The judgment of the Lieutenant Bailiff was upheld by the Guernsey Court of Appeal (the Bailiff of Guernsey, McNeill JA and Sir Michael Birt QC) in a judgment handed down on 21 August 2020. The issue concerning the effect of the assignment of the BVI debts is not the subject of appeal to the Board with the result that there are no outstanding creditor claims against I&B. The right of indemnity is pursued by I&B in relation to their very substantial costs of the earlier proceedings and their unpaid remuneration.

44. The issue of priority as between trustees and trust creditors was argued and decided below exclusively on the basis of the priority between a trustee and *its* trust creditors. As I&B do not have any trust creditors, that issue no longer affects I&B. In their written case, the Guernsey appellants raised as an issue for decision the separate question whether the claims of all trustees (past and current) collectively rank pari passu with the claims of all their trust creditors collectively, or in priority to them. Although there are no trust creditors of I&B, it appears there are some trust creditors of GTC and F&B. This is not an issue that was argued before or considered by either of the courts below, nor was it advanced as a ground of appeal. Leave to raise the issue was not sought. In those circumstances, we do not think that it is an issue which should be decided on this appeal. The question of priority as between trustees and trust creditors is potentially important and it is not straightforward, particularly in the light of article 32. In our view, it is an issue that the Board should consider only after full argument and, save in exceptional circumstances, only after it has been fully considered by the courts below.

45. The Guernsey respondents also sought to argue an issue that had not been argued or considered in the courts below. They submitted, as an alternative case, that where a former trustee retained trust assets, its right of indemnity against those assets ranked in priority to the rights of successor trustees by virtue of their retention of the assets. It appears that I&B retained trust assets after their removal as trustees. As this was not an issue raised below, no findings were made as to the circumstances in which I&B retained trust assets or as to the effect of the order appointing receivers and the resulting transfer of assets to the receivers, nor of course was there any consideration

by the courts below of the legal issues involved in this alternative case. Accordingly, we do not consider that this an issue which can properly be raised for the first time on this appeal.

The issues

46. The principal issues for consideration by the Board in both appeals reflect the submissions made in support of the appeals, which were:

(i) A trustee's lien confers no proprietary interest in the trust assets in favour of the trustee, but is essentially a possessory lien only.

(ii) If that is wrong, while it is accepted that the right of indemnity continues as a personal right after the trustee has ceased to hold office, the lien enjoyed by a trustee is dependent on the trustee's possession or legal ownership of the trust assets and any proprietary interest therefore ceases once those assets are transferred to, or vested in, a successor trustee.

(iii) If both (1) and (2) are wrong, and a trustee enjoys a proprietary interest in the trust assets which survives the transfer of assets to a new trustee, such interest does not enjoy priority over the equivalent interests of the successor trustee or trustees but ranks pari passu with them or is subject to the court's jurisdiction in the administration of trusts, empowering the court to formulate a scheme of distribution on a pari passu basis which recognises the justice of the particular case.

(iv) If (1)-(3) are wrong, a trustee's proprietary interest is created not when the trustee is appointed but as and when it incurs liabilities for which it is entitled to be indemnified.

(v) While (1)-(4) are advanced as propositions of English as well as Jersey law, the appellants further submit that, even if the propositions are correct as a matter of English law, they do not form part of Jersey law, on grounds that they are inconsistent with or modified by Jersey customary law and provisions of the TJL and of the respective trust deeds. Further, the priority of the claims of successive trustees are subject to the court's jurisdiction in the administration of trusts, which empowers the court to formulate a scheme of distribution on such basis, including a pari passu basis, as the court considers just in all the

circumstances. In any event, as regards the Jersey appeal, the survival of any interest of ETJL is inconsistent with the terms of the DORA.

47. In the Jersey appeal there is also the issue as to whether a trustee of an insolvent trust is entitled to recover the costs of proving its claim from the fund.

The judgments under appeal

48. The leading judgment in the Court of Appeal of Jersey was given by Logan Martin JA. Having summarised the factual and procedural background, the judgment of the Commissioner under appeal, the grounds of appeal, and the contentions of the parties and their submissions to the court, he addressed the issue of the priority claims as between the successive trustees at paras 125 to 211. Although he treated the statement of trust law principles at para 59 in *Investec 1*, including para 59(v), as "a statement of the law of trusts in Jersey which is exists in accordance with the customary law subject only to the effects of the Trusts Law" (see para 132), he proceeded to examine in detail many of the relevant English, Australian and other authorities and textbooks, as well as provisions of the TJL, before concluding at para 211 that "under the law of Jersey a trustee has a right of indemnification which is enforceable by a right of lien which ranks in priority over any right of indemnification and right of lien of a successor trustee which takes up office at a later date".

49. Martin JA gave a short concurring judgment, addressing some of the points of Jersey law raised by the Bailiff in his judgment.

50. The Bailiff gave a reasoned judgment, in which he concurred in the result that the appeal should be allowed, but only on the basis that he was in practice bound by *Investec 1*: see para 251. He then made "some observations in case either this present case or some future case comes before the Judicial Committee for consideration". The issues discussed by the Bailiff were of Jersey law, calling into question whether the statements in *Investec 1* at para 59(v) accurately stated the position in Jersey, having regard both to the customary law prohibition on non-possessory security over movable property and to provisions of the TJL.

51. In the Guernsey proceedings, the Court of Appeal dismissed the appeal against Lieutenant Bailiff Marshall's decisions that the trustee's lien extended to all the trust assets, even after the trustee had been replaced and that, as between successive trustees, their rights to an indemnity rank in the order of their respective appointments. The court held that, as the TDT was governed by Jersey law, it should apply the law as held by the Court of Appeal of Jersey in the Jersey proceedings.

Investec 1

52. So far as relevant to the present appeals, the issue for decision for the Board in *Investec 1* was the meaning and effect of article 32 of the TJL. We have earlier set out article 32 and summarised the Board's decision. Of direct relevance to the present appeals are the "preliminary observations" of Lord Hodge at paras 57-59. He said:

> "57. … The international appeal of Jersey trusts is to a significant extent dependent on the certainty which it derives from the English case law. Naturally, English trust law must be modified where it conflicts with established principles of Jersey customary law, and it has also been modified by Jersey statutes. These general remarks apply equally to the trust law of Guernsey.
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> 58. The TJL is the principal indigenous source of Jersey trust law. It is not a complete code of the law of trusts. But it gives statutory effect to some principles already well established in England and significantly modifies other principles. English trust law therefore serves as the background against which the provisions of the TJL fall to be construed."

53. At para 59 Lord Hodge set out "some well-established principles of English trust law which are relevant to the present issue". Omitting references to authorities, the principles are stated as follows:

> "(i) A trust is not a legal person. Its assets are vested in trustees, who are the only entities capable of assuming legal rights and liabilities in relation to the trust. In particular, they are not agents for the beneficiaries, since their duty is to act independently.
>
> (ii) English law does not look further than the legal person (natural or corporate) having the relevant rights and liabilities…
>
> (iii) The legal personality of a trustee is unitary. Although a trustee has duties specific to his status as such, when it

comes to the consequences English law does not distinguish between his personal and his fiduciary capacity. It follows that the trustee assumes those liabilities personally and without limit, thus engaging not only the trust assets but his personal estate…

(iv) This liability may be limited by contract, but the mere fact of contracting expressly as trustee is not enough to limit it… There must be words negativing the personal liability which is an ordinary incident of trusteeship…

(v) A trustee is entitled to procure debts properly incurred as trustee to be paid out of the trust estate or, if he pays it in the first instance from his own pocket, to be indemnified out of the trust estate… To secure his right of indemnity, the trustee has an equitable lien on the trust assets…Because an equitable lien does not depend on possession, it normally survives after he has ceased to be a trustee.

(vi) A creditor has no direct access to the trust assets to enforce his debt. His action is against the trustee, who is the only person whose liability is engaged and the only one capable of being sued. A judgment against the trustee, even for a liability incurred for the benefit of the trust, cannot be enforced directly against trust assets, which the trustee does not beneficially own. The creditor's recourse against the trust assets is only by way of subrogation to the trustee's right of indemnity.

(vii) Because the creditor's recourse to the assets is derived from the trustee's right of indemnity, it is vulnerable. It is exercisable only to the extent that that right exists. It may be defeated if there are insufficient trust assets to satisfy his debt, or if the trustee's right of indemnity is defeated, for example because the debt was unreasonably or improperly incurred and the indemnity does not extend to such debts, or because the trust deed excludes it on account of the trustee's wilful default or gross negligence. More generally a breach of trust by the trustee, even in relation to a matter unconnected with the incurring of the relevant liability, will, to the extent that it creates a liability to account on the part of the trustee,

> stand in the way of the enforcement of the indemnity. As has frequently been observed, this can be hard on the creditor, who will usually have no knowledge of the state of account between the trustee and the beneficiaries. But the creditor can in principle protect his position, for example by taking a fixed charge over the trust assets, or, as in the present case, by stipulating for a personal guarantee from the principal beneficiary. It appears to the Board that all of these principles must be regarded as having been part of the law of Jersey before the enactment of the TJL or its statutory predecessors."

54. At para 61 Lord Hodge stated the Board's view that the effect of article 32(1) was to abrogate the rule of English law that the law looks no further than the legal entity which has assumed the liability and introduces a legal distinction between the personal and fiduciary capacities of a trustee. In the circumstances of knowledge set out in article 32(1)(a), a trustee is treated as incurring liabilities not personally but "as trustee" and therefore without recourse to his personal estate. At para 62 Lord Hodge went on to say that this was "the only relevant respect in which the pre-existing law is altered by article 32" and that there was nothing in article 32 which modified the rule that a creditor could access the trust assets only by way of the trustee's right of indemnity and subject to the limits on that right imposed by the trust deed or the general law.

55. It follows from the Board's approach in *Investec 1* that the issues as to the nature and priority of a trustee's right of indemnity and lien should first be approached as matters of English law. If the appellants' submissions on English law, as summarised above, are correct, the appellants will succeed in these appeals. It is not suggested by the respondents that there are any rules of Jersey law which would provide ETJL or I&B with greater rights than those which they would enjoy under English law. If, however, the appellants' case on those issues is rejected as a matter of English law, it is necessary then to consider whether the English law principles require modification in the light of Jersey customary law or provisions of the TJL. We will therefore first consider the position as a matter of English law.

The trustee's right of indemnity in English law

56. The right of indemnity entitles a trustee both to be reimbursed for any liabilities properly incurred in the execution of the trust which it has paid from its own resources and to pay or seek payment of such liabilities from the trust assets without first making payment out of its own resources. These two aspects of the right of indemnity are

commonly described as a right of reimbursement (or recoupment) and a right of exoneration.

57. There is some common ground as to the nature and characteristics of the right of indemnity.

58. First, the need for the right arises because, in English law, a trustee is personally liable for all debts and obligations incurred by it in the course of acting as a trustee. Its liability is no different from its liability for debts incurred for its personal benefit. This necessarily follows from the nature of a trust in English law. The trustee is in law the absolute owner of assets but, by virtue of what equity recognises as obligations undertaken by or imposed on the trustee in respect of the assets and enforceable in equity against the trustee, the trustee cannot treat those assets as its own but must deal with them in accordance with those obligations. A trust is not an institution, still less a legal person, separate from the trustee. A trust is essentially the obligations enforceable in equity against the trustee. Leaving aside the special circumstances of charitable and other purpose trusts, equity will enforce those obligations on the application of the persons to whom the obligations are owed, generally the beneficiaries. Equity will enforce them against the trustee and against third parties who become legal owners of trust assets or otherwise interested in them, except for "equity's darling", the bona fide purchaser of the legal title to the assets without notice of the trustee's equitable obligations.

59. It follows that liabilities incurred by a trustee acting as such are enforceable at the suit of the creditor against the trustee personally and judgments may be executed against the trustee's personal assets. A judgment creditor may not, however, execute the judgment against assets held on trust, even if the judgment is in respect of a properly incurred "trust debt", the reason being that the judgment is against the trustee personally in respect of a liability for which it is personally liable and such a judgment cannot be executed against assets held for others. The judgment creditor's right of recourse to such assets is by way of subrogation to any unexercised right of the trustee to exoneration from the trust assets. (More indirectly, a creditor could apply for the appointment of a receiver of the right by way of equitable execution, but this is rarely, if ever, done.) The proceeds of such a subrogated right are payable to, or in a formal insolvency of the trustee distributable among, trust creditors.

60. These features were summarised by Lord Hodge in *Investec I* at para 59(i)-(iv) and (vi).

61. Second, it follows from the first proposition that it is inaccurate to speak of an insolvent trust. Since a trust is not a legal person and all liabilities incurred by the trustee acting as such are personal liabilities of the trustee, it is only the trustee who can become insolvent, whether on account of trust liabilities or its personal liabilities or both. It is likewise inaccurate to speak of "trust creditors". An "insolvent trust" is nonetheless a convenient description of a situation where the trust assets are insufficient to meet the amount due under the trustee's right of indemnity, and "trust creditors" is a convenient description of the persons to whom the trustee has properly incurred liabilities in the course of acting as trustee. Whether the insolvency of the trust affects only the trustee or also affects the "trust creditors" will depend on whether the trustee's personal assets are sufficient to ensure that all its liabilities, including those to "trust creditors", are met in full.

62. Third, the right of indemnity arises by operation of law, in the sense that it is a right conferred by equity on all trustees. In *Worrall v Harford* (1802) 8 Ves Jun 4, 8; 32 ER 250, 252 Lord Eldon LC said: "It is in the nature of the office of a trustee, whether expressed in the instrument or not, that the trust property shall reimburse him all the charges and expenses incurred in the execution of the trust. That is implied in every such deed." In *In re The Exhall Coal Co Ltd* (1866) 35 Beav 449, 453; 55 ER 970, 971-972 ("*Exhall Coal*"), Lord Romilly MR said that the right of indemnity was "a right incidental to the character of trustee and inseparable from it".

63. Fourth, the right of indemnity does not impose any personal liability on any person. Neither the beneficiaries (except in the case of a trust where all of the beneficiaries are sui juris and the liabilities are incurred with the consent of the beneficiaries) nor any successor trustees are under any personal liability to indemnify a trustee. The right of indemnity is a right to payment out of the trust assets, which is enforceable where the assets have vested in a new trustee by an application to the court to which the current trustee, as the legal owner of the trust assets, is a necessary party.

64. Fifth, a trustee's right of indemnity, whatever its nature, is not lost when a trustee ceases to be a trustee. Whether or not it is a purely personal right, it remains enforceable by the former trustee and, in the case of a formal insolvency of the trustee or the death of an individual trustee, it remains enforceable for the benefit of the trustee's estate. The appellants accepted that a former trustee retained its right to indemnity out of the trust assets, not only after it ceased to be a trustee but also after it ceased to hold any trust assets. It was the appellants' submission that the former trustee continued to enjoy a personal right to seek, if necessary by court order, reimbursement or exoneration out of the trust assets but that right conferred no

proprietary interest in the trust property and the trustee's own right to use the trust assets for this purpose necessarily ceased once it no longer held any trust assets.

65. Sixth, a trustee's right of indemnity is not for the gross amount of trust liabilities incurred by it, but for a net sum determined by reference to those liabilities after deduction of any amounts for which the trustee is accountable to the trust. If any such amounts exceed those liabilities, no indemnity is available to the trustee.

66. Seventh, the right of subrogation of "trust creditors" is to such right, if any, as the trustee may enjoy. If the state of the trustee's account is such that its gross indemnity claim is reduced or eliminated by amounts for which it is accountable, the "trust creditor's" claim by way of subrogation is no better than the trustee's claim. In our view, although this cannot be said to have been common ground between the parties, this demonstrates the purpose of the indemnity as being protection of the trustee, not of its trust or indeed personal creditors. The trust creditors' rights of subrogation provide protection to them only to the extent of any net recovery permissible under the right of exoneration, just as the right of any creditor of the trustee, whether a trust or a personal creditor, to enforce a claim against the trustee's right of reimbursement is necessarily limited to the net amount, if any, due under that right.

67. Eighth, each trustee enjoys its own right of indemnity, consistently with the fifth proposition. The indemnity is in respect of those liabilities incurred by the trustee and its amount is reduced by amounts for which that trustee is accountable to the trust. If a liability were incurred by two joint trustees, A and B, but only A was accountable to the trust for any sums, B (but not A) would be entitled to an indemnity for the full amount of the liability: *In re Frith*, *Newton v Rolfe* [1902] 1 Ch 342.

68. An issue on which there was not agreement is the rationale for the trustee's right of indemnity. The appellants submitted that its purpose is to prevent the unjust enrichment of the beneficiaries, pointing for example to Lord Lindley's statement, in giving the advice of the Board in *Hardoon v Belilos* [1901] AC 118 , 123, that the "plainest principles of justice require that the cestui que trust who gets all the benefit of the property should bear its burden unless he can shew some good reason why his trustee should bear them himself".

69. The prevention of unjust enrichment is a necessary consequence of the indemnity, but the authorities show that its principal purpose is to ensure, as far as the trust assets permit, that the trustee is not required to bear liabilities which are not incurred for the trustee's personal benefit. It is a right for the protection of the trustee.

In *Exhall Coal*, Lord Romilly MR said in the passage quoted in part above that the indemnity is "a right incidental to the character of trustee and inseparable from it, that he should be saved harmless from obligations which are attached inseparably to his office". In *Jennings v Mather* [1901] 1 KB 1, 6-7, Stirling LJ said:

> "A trustee is prohibited by law from making any profit for himself out of the trust estate, a rule which is enforced with great stringency; it is only just that, on the other hand, he should be legally protected against all liabilities properly incurred by him in the administration of the trust estate."

Does the right of indemnity confer on the trustee a proprietary interest in the trust assets?

70. We turn now to consider the first principal submission of the appellants, that the right of indemnity is a purely personal right and that a trustee's lien is no more than a possessory right, entitling the trustee to retain trust assets pending satisfaction of its indemnity while the trustee remains the legal owner of those assets.

71. In many of the English authorities, it is said that the trustee's right of indemnity involves or is supported by a lien or charge over the trust fund.

72. It is well established that, although the word "lien" is used both at common law and in equity, it connotes very different rights. A lien at common law is possessory and does no more than entitle the lienholder to retain possession of the assets in its possession. An equitable lien does not depend on possession but entitles the lienholder to have the property over which the lien exists applied in discharge of amounts due to the lienholder. Because this right is enforceable in equity, the lien gives the lienholder a proprietary interest in the relevant property. Where its purpose is to secure a debt due to the lienholder, as for example in the case of an unpaid vendor's lien, it is in effect a charge, but one arising by operation of law rather than consensually between the parties. In *Gavin Edmondson Solicitors Ltd v Haven Insurance Co Ltd* [2018] UKSC 21; [2018] 1 WLR 2052, a case concerning a solicitor's equitable lien over the proceeds of successful litigation, Lord Briggs (with whom the other members of the Court agreed) said at para 35:

> "*Barker v St Quinton* (1844) 12 M&W 441 shows, better than any other, that the equitable lien operates by way of security or charge. Parke B said at p 451:

> ‘The lien which an attorney is said to have on a judgment (which is, perhaps, an incorrect expression) is merely a claim to the equitable interference of the court to have that judgment held as security for his debt.’”

73. As the citation from Parke B’s judgment shows, the underlying principle is that the solicitor’s security interest - itself a form of proprietary interest - arises from the solicitor’s right to apply to the court for equitable enforcement.

74. The position is stated in Goff & Jones, *The Law of Unjust Enrichment*, 9th ed, (2016) at paras 38-49:

> “Unlike a common law lien, an equitable lien is an equitable proprietary right that in accordance with general principles is capable of binding third parties unless they are bona fide purchasers for value of a legal interest without notice of the equitable lien”.

75. In *Hewett v Court* [1983] HCA 7; 149 CLR 639, a decision of the High Court of Australia, Deane J, speaking of equitable liens generally, said, at para 9:

> “An equitable lien is a right against property which arises automatically by implication of equity to secure the discharge of an actual or potential indebtedness … Though called a lien, it is, in truth, a form of equitable charge over the subject property … in that it does not depend upon possession and may, in general, be enforced in the same way as any other equitable charge, namely, by sale in pursuance of court order or, where the lien is over a fund, by an order for payment thereout.” (149 CLR 639 at 663)

76. Deane J further said, at para 11:

> “The word ‘lien’ is used somewhat imprecisely in the phrase ‘equitable lien’ to describe not a negative right of retention of some legal or equitable interest but what is essentially a positive right to obtain, in certain circumstances, an order for

> the sale of the subject property or for actual payment from the subject fund." (149 CLR 639 at 664)

77. As the word "lien" has been repeatedly used by equity judges in relation to the equitable right of indemnity enjoyed by trustees, it may be thought likely that the judges were using "lien" in a way consistent with its use in equity. This is only strengthened by the use of "charge" as an alternative description which likewise, because it is enforceable in equity, confers on the chargee a proprietary interest in the charged property (see *Palmer v Carey* [1926] AC 703).

78. In *Exhall Coal*, the property of a company, which included the leasehold interest in a mine, was held by a trustee on its behalf. The lessor demanded payment of the rent due from the trustee as lessee for periods after the company had gone into insolvent liquidation. The trustee paid money into court in respect of the rent and sought an indemnity out of the proceeds of sale of fixtures, plant and machinery at the mine. His application was resisted by the holders of debentures issued by the company.

79. Lord Romilly MR held that the trustee was entitled to be indemnified. He said at p 452-453 that Mr Bleckley:

> "was the trustee of the mine, including the fixtures, the plant and machinery; he is the owner of this property at law, and when called upon to account in equity, he is entitled to deduct, out of the trust property in him, all that is necessary for the purpose of repaying him the sums he has properly paid, and of indemnifying him against such sums as he is liable to pay in discharge of his trust; and, in my opinion, this liability to repay and indemnify him is the first charge on the property."

80. In the authorities cited to the Board, this is the earliest statement of the character of a trustee's right of indemnity. The "liability to repay and indemnify" the trustee does not refer to a liability of any person; there is no such personal liability. It refers to the right of the trustee to be repaid and indemnified out of the trust property, which Lord Romilly described as a first charge on the property. It is properly described as a charge because it is enforceable in equity, although recourse to proceedings will not always be necessary because, if the trustee is in possession of the property, it may be entitled to exercise a self-help remedy.

81. The appellants submitted that *Exhall Coal* is authority only for the proposition that the right of indemnity takes precedence over the beneficiaries, not over third party creditors of the trustee or subsequent trustees. But, third party creditors are creditors of the trustee, not of the trust. Necessarily their claim is a personal one against the trustee and they have no rights in respect of the trust property except by way of subrogation to the trustee's right of indemnity. It is, however, fair to say that the case did not raise any issue as to the rights of a former trustee.

82. In the course of his judgment in *In Re Chennell*, *Jones v Chennell* (1878) 8 Ch D 492, 503, Cotton LJ said that the trustee claimed to enforce his charges and expenses "by means of a lien upon the property, that is, a right to retain it until they are paid". The appellants relied on this as authority that the trustee's lien is possessory in nature, being no more than a right to retain trust property. However, the nature of the trustee's rights in this respect was not an issue in the case and no argument was addressed to it. Cotton LJ was not, in this obiter comment, analysing the nature or characteristics of a trustee's right of indemnity.

83. *In re Johnson; Shearman v Robinson* (1880) 15 Ch D 548, the case to which Lord Hodge referred in *Investec 1* at para 59(v), concerned the rights of creditors in respect of liabilities incurred by a trustee while carrying on a testator's business. The trustee had become insolvent. Sir George Jessel MR, sitting at first instance, dismissed the claims of three creditors for payment out of the testator's estate. At p 552, he stated the doctrine as being that a creditor has a personal claim against the trustee who incurred the liability and "a right to be put in his place against the trust assets; that is … a right to the benefit of the indemnity or lien which [the trustee] has against the assets devoted to the purposes of the trade".

84. It is convenient to note here the appellants' submission that *In re Johnson* does not deal with the survival of the trustee's lien after transfer of the fund. We consider this to be correct, and that it does not stand as authority for the proposition stated in the last sentence of para 59(v) in *Investec 1* that the lien normally survives after the trustee has ceased to hold office.

85. In *In re Pumphrey*, *dec'd*, *The Worcester City and County Banking Co v Blick* (1882) 22 Ch D 255, the trustees of a marriage settlement, at the request of the husband and wife, purchased a property as their residence. The trust assets were insufficient to pay the full price and, at the request of the husband and wife, one of the trustees borrowed the balance from a bank. The trustee's personal representative claimed to be entitled to be indemnified out of the trust assets for the amount borrowed by him. Kay J upheld the claim, saying at p 262:

> "His right of indemnity gives him a right of charge or lien upon the trust estate, he has a right to come at any time and say, 'I claim to have my right of indemnity … out of the trust estate, and that gives me the right in equity to have a charge against the estate, and to have the charge enforced by the process of the Court of Equity.'"

86. This was said in the context of whether the trustee had to wait until the trust assets had been realised or whether the trustee could apply to the court for an order for sale. Kay J held that the trustee did not have to wait but "if a trustee has a right of indemnity he has a right to come to this Court to enforce it".

87. In *Stott v Milne* (1884) 25 Ch D 710, 715 Lord Selborne LC, with whom Cotton and Lindley LJJ agreed, said:

> "The right of trustees to indemnity against all costs and expenses properly incurred by them in the execution of the trust is a first charge on all the trust property, both income and corpus. The trustees, *therefore*, had a right to retain the costs out of the income until provision could be made for raising them out of the corpus". (Emphasis added)

88. As the emphasised "therefore" in the second sentence indicates, the right of retention is itself the consequence of the trustee's right to an indemnity by way of a first charge on the trust property.

89. In *Jennings v Mather* [1901] 1 QB 108, Mather was the trustee under an arrangement with the creditors of an insolvent trader, whereby Mather would continue the trade and pay dividends to the creditors out of the profits. In the course of his duties as trustee, Mather bought goods from Jennings but failed to pay for them. Jennings obtained judgment against Mather, who was personally liable for the debt, and levied execution on goods forming part of the trust estate. The county court upheld Jennings' right to levy execution on the goods. On appeal, a Divisional Court of the Queen's Bench Division held that, as the goods were held by Mather on trust, they were not available for execution to enforce the judgment against him.

90. The Divisional Court went on to consider Mather's right of indemnity in respect of debts properly incurred by him as trustee. Kennedy J, with whom Lawrance J agreed, said at pp 113-114:

> "While there can be no right of a creditor created in the course of the trading to treat as goods of the trustee goods which form part of the trust estate, still it is equally clear that the trustee has a right and interest in those goods, because he has a right to an indemnity in the nature of a lien over those goods. It necessarily follows, as it seems to me, that the trustee has a right to prevent any person from carrying away those goods, and to say to everybody, including the cestuis que trust, 'I am entitled to an indemnity out of those goods, and have, therefore, a pecuniary interest in them'. Of course, when the accounts come to be made up, if it should appear that nothing is due to the trustee on the trading, there is nothing in respect of which he needs to be indemnified, and his lien over the goods is gone; but until the accounts are made up he is entitled to a lien over all the assets of the estate. A lien … has always been held to be sufficient title as against the world to hold the goods until that lien is satisfied, or is proved not to exist."

91. The position was complicated by the fact of Mather's own bankruptcy. Kennedy J said at p 116-117 that, while it was plain under section 44 of the Bankruptcy Act 1883 that Mather's legal title to the trust assets did not pass to his trustee in bankruptcy, his right of indemnity and equitable lien did pass to his trustee in bankruptcy who was entitled to maintain the lien. In that case, the trustee in bankruptcy had the relevant goods in his possession and was not required to release them while the lien subsisted. There was no consideration of the position if the trust property in question had been incorporeal and therefore incapable of physical possession by the trustee in bankruptcy.

92. The decision was upheld on appeal: [1902] 1 KB 1, 6. Stirling LJ said:

> "A trustee has for his protection a right to have costs and expenses properly incurred by him in the administration of the trust paid out of the trust property, and the amount of such costs and expenses constitutes a first charge upon that property. A Court of Equity will never take trust property out of the hands of a trustee without seeing that such costs and expenses are reimbursed to him, and that he is relieved from personal liability in respect of them; and when the legal title to trust property is vested in the trustee, he has a right to resort to that property, without the assistance of the Court,

> for the purpose of indemnity against liabilities properly incurred by him in the administration of the trust."

93. The appellants submitted that these and other statements in the authorities demonstrated that, insofar as the right of indemnity involves a lien, it was no more than a right to retain trust assets pending the taking of accounts and payment of the amount due under the indemnity. We do not accept that the authorities can be read in this way. The characterisation of the lien as essentially possessory is inconsistent with the nature of an equitable lien and is incompatible with those statements in the judgments which speak of the trustee's right of indemnity as being a first charge on the trust assets. The distinction between a lien or charge over the trust property and the self-help remedy of reaching into trust assets in the trustee's possession is apparent in a number of the judgments. We do not accept the ambitious submission of Miss Stanley, who argued this part of the case for the Jersey appellants, that the references to a charge, or a first charge, were loose language on the part of Lord Selborne and the other judges.

94. The English courts have not explicitly addressed the question whether the trustee's equitable right of indemnity gives the trustee a proprietary interest in the trust property over which the right exists. Nonetheless, we consider that the analysis in the authorities that the right confers or constitutes a charge or lien over that property, enforceable by a court of equity, leads inevitably to the conclusion that it does create a proprietary interest in favour of the trustee.

95. There has been significant consideration by courts in Australia of the nature of the trustee's right of indemnity. For the most part, these cases have arisen in the context of trading trusts, which are not a feature of commercial life in the United Kingdom but which for many years have been widely used in Australia. The essential character of a trading trust is that a trustee (usually, perhaps invariably, a company) carries on a business not on its own account but on trust for others pursuant to the terms of a trust deed.

96. The principles relating to the trustee's right of indemnity developed by the English courts, principally in the cases referred to above, have long been accepted as part of Australian law: see *Vacuum Oil Co Pty Ltd v Wiltshire* [1945] HCA 7; (1945) 72 CLR 319.

97. In a series of further decisions, the High Court and other Australian courts have considered whether the right of indemnity confers on the trustee a proprietary interest in the trust assets. They have consistently held that it does. It will be necessary

to consider some of these decisions but, for the purposes of the first issue, it is enough to note that this is the unanimous conclusion reached by the Australian courts.

98. Basing themselves principally on the English and Australian authorities, the leading textbooks take the position that the right of indemnity confers on the trustee a proprietary interest in the trust property: see *Lewin on Trusts*, 20th ed, (2020) at paras 19-044-19-045, *Underhill & Hayton: Law of Trusts and Trustees*, 19th ed, (2022) at para 81.1.

99. In arguing that the right of indemnity is essentially possessory, not proprietary, in character, we understood the appellants to lay stress on the ability of a trustee or former trustee who is in possession of trust property, or in whom the legal title remains vested, to exercise self-help remedies by "reaching into" the trust property to exonerate or reimburse itself.

100. There are, however, circumstances in which a self-help remedy will not be available to a trustee.

101. First, if there is more than one trustee but only one trustee has a right of indemnity (because, for example, it alone has paid the liability in question, or because the other trustee(s) are accountable to the trust for amounts in excess of the liability in question), that trustee will not be able to "reach into" the trust property without the cooperation of the other trustee(s), failing which it will need to apply to court to enforce its right of indemnity.

102. Second, the lien or equitable charge conferred by the right of indemnity does not itself confer a power to sell any trust property: *Hewett v Court* (supra): *Jones (Liquidator) v Matrix Partners Pty Ltd*, *in the matter of Killarnee Civil & Concrete Contractors Pty Ltd (in liq)* [2018] FCA 40 (the Full Court of the Federal Court of Australia) at para 44 per Allsop CJ. If the trust assets include liquid assets, a trustee, or a former trustee still in possession of such liquid assets, can itself apply those liquid assets in exoneration or reimbursement. In respect of other assets, the trustee or former trustee must have a power of sale from some other source which it can use for this purpose. This will not usually present a problem for a trustee who is in office, who will normally be able to rely on powers conferred by the trust instrument or by statute. If, however, the trustee has ceased to hold office, it will no longer have those powers available to it, even though it remains in possession of, or the legal owner of, trust property. In those circumstances, the former trustee will have to apply to court for an order for sale or for the appointment of a receiver with a power of sale. For a discussion of these issues, see *Apostolou v VA Corpn Aust Pty Ltd* [2010] FCA 64

(Finkelstein J) at paras 38-48, *Jones (Liquidator) v Matrix Partners Pty Ltd* (supra) at paras 89-91.

103. As an alternative to their primary case, the Jersey appellants argued in their oral submissions in reply that, if the right of indemnity conferred anything more than a possessory right, it was akin to a "mere equity".

104. In contrast to equitable interests in property, such as those of a beneficiary under a trust or of an equitable chargee, a mere equity is "an inchoate right binding on specific property" which requires the claimant first to perform some legal act, such as rescinding a transfer of property or rectifying a document, to cause the claim to crystallise as an equitable interest: see *Snell's Equity*, 34th ed, (2021) at 2-006. If, as the authorities establish, a right of indemnity confers a lien or charge, there is no further legal act required for the crystallisation of an equitable interest. There is no support in the authorities for the submission that the right of indemnity is akin to a mere equity, and we reject it.

105. As regards the first main issue on these appeals, we conclude that the right of indemnity confers a proprietary interest in the trust property in favour of the trustee. The English and Australian authorities are inconsistent with the appellants' contention that equity confers no more than a possessory lien, enjoyed for so long as the trustee retains trust assets. There is no doubt that a trustee is entitled to apply, or to seek an order of the court to apply, trust assets in its possession in payment of amounts due under its right of indemnity, and that a trustee is or may be entitled to retain sufficient assets, or require security, before a transfer to a new trustee. Those rights are not, however, inconsistent with a charge over, and proprietary interest in, the trust assets, but are practical means by which such charge or interest may be enforced or protected.

Does the proprietary interest of a trustee survive the transfer of the trust assets to a replacement trustee?

106. The appellants submit that, if the right of indemnity confers a proprietary interest on the trustee, it endures after the replacement of the trustee only for so long as legal title to, or possession of, the trust property is retained by the former trustee.

107. Before any further consideration of the authorities, it is important to note that this is not an issue which, it appears, has ever arisen for consideration or decision by the English courts. The examination of the nature of the trustee's right of indemnity

has for the most part arisen only for the purpose of the effect of the right while the trust property remains in the legal ownership or possession of the trustee.

108. Although the references to the trustee having an equitable lien or charge over the trust assets convey much of the essential nature of the trustee's right of indemnity, they are liable to deflect attention from the fundamental character of that right.

109. The right of indemnity enjoyed by a trustee does not, as already noted and as all parties agree, impose any personal obligation on any party to make payment. The trustee's right is to payment out of the trust fund. It is a right to have the fund applied in reimbursement of liabilities already paid by the trustee or in exoneration of liabilities which the trustee is required to pay, net in either case of any amounts for which the trustee is accountable. It is a right that the court will enforce by an order for payment out of the fund, in effect an order for specific performance.

110. It is the consequence of that right to equitable enforcement of the indemnity out of the trust property that the trustee has a proprietary interest in the trust property. This is not security for the payment of a debt, as in the case of an unpaid vendor's lien or a solicitor's lien, because there is no debt payable by any party to the trustee. The trustee's right, enforceable in equity, is no more and no less than the right to have the trust property applied in indemnifying the trustee against liabilities properly incurred. Where such a right exists for payment out of a fund, which the court will enforce, the fund is subject to an equitable charge in favour of the person entitled to payment and it will in equity create a proprietary interest in the fund in favour of that person. This is a longstanding equitable principle, summarised by the Privy Council in *Palmer v Carey* [1926] AC 703, 706-707 where Lord Wrenbury, giving the advice of the Board and in a passage cited by Lord Wilberforce in *Swiss Bank Corpn v Lloyds Bank Ltd* [1982] AC 584, 613, referred to the "familiar doctrine of equity that a contract for valuable consideration to transfer or charge a subject matter passes a beneficial interest by way of property in that subject matter if the contract is one of which a court of equity will decree specific performance".

111. The context of those decisions was an agreement between two parties for payment of a debt due from one to the other to be made out of a specific fund belonging to the debtor. The same principle applies to a case such as the present where there is neither an agreement nor a debt due from one person to another, but where, by operation of law, a party (the trustee) is entitled to payment out of a specified fund (the trust fund). It is for that reason that the judges in the English authorities cited above referred to a first charge on the trust fund in favour of the trustee for payment of the amount due under the indemnity. The fact that judges have

referred to “a charge or lien”, or simply to a lien, is not significant in view of the characteristics of an equitable lien outlined above.

112. Once it is established that the right of indemnity confers in equity a proprietary interest in the trust property in favour of the trustee, it would be very surprising, as a matter of principle, if this proprietary interest automatically ceased to exist when legal title to, or possession of, the trust property ceased to be held by the trustee or former trustee and was vested in the replacement trustee. It is usually an essential feature of an equitable interest that it survives a transfer of legal ownership, save in the case of a bona fide purchaser of the legal estate without notice of the interest.

113. The appellants accept that a trustee’s right to an indemnity survives the vesting of the trust property in a new trustee but submit that it ceases to confer or carry with it any proprietary interest in the trust property. However, the nature of the right of indemnity does not alter on the vesting of trust property in a new trustee. It remains a right to exoneration or reimbursement out of the trust property and it remains a right that does not impose any personal liability or obligation to indemnify on any person. In particular, it does not impose any personal liability on the replacement trustee, beyond its obligation as trustee to apply the trust property in accordance with the rights of, among others, a former trustee with a right of indemnity.

114. The right remains as it was while the trustee was in office, namely a right, enforceable in equity, to have the trust property applied in reimbursing or exonerating the trustee. Just as it then created a proprietary interest in favour of the trustee, so in principle it continues to do so after the trustee has ceased to hold the trust property.

115. The appellants relied on the rights of trustees to retain trust property, or to require the provision of security over trust property, when ceasing to hold office as showing that no proprietary interest survived the vesting of trust property in a new trustee. Whether these are absolute rights of trustees, or whether retention or security is a matter for the discretion of the court, is not material for present purposes. It is clear that, at the very least, the court will be astute to protect the position of a trustee as regards the trustee’s exposure to liabilities properly incurred by it. We do not, however, understand why it follows that the trustee’s proprietary interest should be taken as being extinguished on the vesting of the property in a new trustee. Retention of assets, or the creation of express security such as the setting aside of a specific fund, provide a degree of practical protection which is in no way inconsistent with a continuing equitable proprietary interest in the trust property.

116. Reliance was placed by the appellants on the decision of Wilberforce J in *In re Pauling's Settlement*, *Young v Coutts & Co (No 2)* [1963] Ch 576 (more fully reported at [1963] 1 All ER 857). The defendant bank was the trustee of a family settlement. Following a trial, it had been held liable to restore to the trust fund capital improperly advanced to beneficiaries, but it was appealing the order. Wilberforce J refused an application to remove the bank and appoint new trustees in its place, in view of the possibility that its appeal would succeed and it might then become entitled to its costs of the proceedings. It was also exposed to a possible future liability for estate duty. He said ([1963] 1 All ER 857, 860) that

> "It is inevitable that some security should be held by the bank, as trustees, for their costs … any trustee is entitled to have security as regards his costs, if those costs are properly incurred, and there is great difficulty in ordering the bank to part with the trust fund in their hands until it can be seen what rights the bank may have against the trust fund in respect of costs …There is, therefore, considerable objection to making an order by which the possession of that fund would be transferred at this stage out of the bank's possession."

117. The appellants submit that this shows that Wilberforce J considered that the bank would not have a lien or charge over, or any proprietary interest in, the trust property if it were vested in new trustees. This, however, seeks to read too much into what Wilberforce J said. The report of counsel's argument in the official Law Reports ([1963] Ch 576) records no submissions on that subject and it was not addressed in the judgment. The practical advantages of the protection to the bank of retention of the trust property, pending the decision on appeal, were a sufficient basis for the decision not to appoint new trustees at that stage.

118. It is appropriate at this stage to consider the leading Australian cases which, because of the prevalence of trading trusts in Australia, have extended the analysis beyond the point reached in the English cases.

119. Starting with *Octavo Investments Pty Ltd v Knight* [1979] HCA 61; (1979) 144 CLR 360 ("*Octavo*"), the High Court of Australia has consistently analysed the trustee's right of indemnity and lien as giving the trustee a proprietary interest in the trust assets.

120. The facts of *Octavo* were that, under the terms of a settlement, Coastline Distributors Pty Limited (Coastline) carried on the business of distributing frozen food

as trustee for five named companies, which were the family trust companies of its five directors. The business was not a success and within about two years Coastline was wound up by order of the court. Within the period of six months before the making of the order, Coastline made payments to Octavo Investments Pty Limited (Octavo), one of the family trust companies. The liquidators of Coastline commenced proceedings to recover those payments from Octavo on the grounds that they were void as preferences under section 122 of the Bankruptcy Act.

121. The principal ground of Octavo's appeal to the High Court was that all the property in Coastline's hands was trust property which was not therefore property falling within the insolvent estate or property from which a preferential payment could be made.

122. It is important to set out the High Court's unanimous reasoning in rejecting this submission. They set out the general principles at paras 13-16:

> "13. We do not understand the general principles concerning the bankruptcy of a trading trustee to be in dispute. It is common ground that a trustee who in discharge of this trust enters into business transactions is personally liable for any debts that are incurred in the course of those transactions: *Vacuum Oil Co Pty Ltd v Wiltshire* [1945] HCA 37; (1945) 72 CLR 319. However, he is entitled to be indemnified against those liabilities *from the trust assets held by him* and for the purpose of enforcing the indemnity the trustee possesses a charge or right of lien *over those assets*: *Vacuum Oil Co Pty Ltd v Wiltshire*. The charge is not capable of differential application to certain only of such assets. It applies to *the whole range of trust assets in the trustee's possession* except for those assets, if any, which under the terms of the trust deed the trustee is not authorised to use for the purposes of carrying on the business: *Dowse v Gorton* [1891] AC 190. [Emphasis added]
>
> 14. In such a case there are then two classes of persons having a beneficial interest in the trust assets: first, the cestuis que trust, those for whose benefit the business was being carried on; and secondly, the trustee in respect of his right to be indemnified out of the trust assets against personal liabilities incurred in the performance of the trust. The latter interest will be preferred to the former, so that the

cestuis que trust are not entitled to call for a distribution of trust assets which are subject to a charge in favour of the trustee until the charge has been satisfied: *Vacuum Oil Pty Ltd v Wiltshire*.

15. The creditors of the trustee have limited rights with respect to the trust assets. The assets may not be taken in execution (*Savage v Union Bank of Australia Ltd* [1906] HCA 37; (1906) 3 CLR 1170, at p 1186; *In re Morgan: Pillgrem v Pillgrem* (1881) 18 Ch D 93) but in the event of the trustee's bankruptcy the creditors will be subrogated to the beneficial interest enjoyed by the trustee: *Vacuum Oil Pty Ltd v Wiltshire; Ex parte Garland* [1804] ER 336; (1804) 10 Ves Jun 110, 120; [1804] ER 336; (32 ER 786, 789).

16. These principles lead naturally to the conclusion that the beneficial interests which, by subrogation, the creditors whose claims arise from the carrying on of the business have in the assets held by a bankrupt trustee form part of the property of the bankrupt divisible amongst his creditors: *Savage v Union Bank of Australia* (1906) 3 CLR at p 1188; *Jennings v Mather* [1901] 1 QB 108, at p 116; *Governors of St Thomas's Hospital v Richardson* [1910] 1 KB 271. The definitions of both 'property' and 'property of the bankrupt' in section 5 of the Bankruptcy Act are apt to include such a beneficial interest."

123. At para 29, the High Court said:

"Property which is an asset of a trading estate carried on by a trustee is properly described as trust property: *Dowse v Gorton* [1891] AC 190; *Jennings v Mather* [1901] 1 QB, at p 111. However, as we have already indicated, that does not mean that the cestuis que trust are necessarily entitled to call for the delivery of the property. If the trustee has incurred liabilities in the performance of the trust then he is entitled to be indemnified against those liabilities out of the trust property and for that purpose *he is entitled to retain possession of the property* as against the beneficiaries. The trustee's interest in the trust property amounts to a proprietary interest, and is sufficient to render the bald

> description of the property as 'trust property' inadequate. It is no longer property held solely in the interests of the beneficiaries of the trust and the trustee's interest in that property will pass to the trustee in bankruptcy for the benefit of the creditors of the trust trading operation should the trustee become bankrupt." (Emphasis added)

124. The appellants rely on the emphasised words in paras 13 and 29 as showing that the trustee's proprietary interest is limited to trust assets only while they are held by the trustee. We will return to this submission.

125. In *Octavo*, it was further submitted that, in the case of an individual trustee declared bankrupt, the legal estate in the trust property did not pass to the trustee in bankruptcy but remained vested in the trustee, with the result that any repayment would be made to the bankrupt trustee, not to the trustee in bankruptcy. Such a result, it was submitted, would be wholly inconsistent with the purpose of the statutory regime and showed that it did not apply to payments out of trust property.

126. The High Court observed that there were conflicting views as to whether trust property held by a bankrupt trustee vested in their trustee in bankruptcy but considered it did not have to resolve that issue. The Court said at para 35:

> "We take the view that the passing to the trustee in bankruptcy of the trustee's beneficial interest in the trust estate, even if that is all that passes, is sufficient to attract the operation of section 122 of the Bankruptcy Act. Once it is recognized that a trustee may enjoy a right of indemnity over trust property in respect of liabilities incurred by him in the administration of the trust, it follows that the creditors of a trust business may have resort to the assets of the trust to the extent of the liabilities incurred by the trustee."

127. The High Court's decision in *Octavo* firmly established, as a matter of Australian law, that the trustee's right of indemnity gave it a proprietary interest in the trust property, which was described as a beneficial interest. It also established that the proprietary interest was capable of transmission to a trustee in bankruptcy, whether or not the trust property as a whole vested in the trustee in bankruptcy. Its continued existence did not depend on continued legal ownership of the trust property, but it could exist independently of legal ownership of that property.

128. The High Court revisited the nature of a trustee's right of indemnity in *Chief Commissioner of Stamp Duties for New South Wales v Buckle* [1998] HCA 4; (1998) 192 CLR 226 ("*Buckle*") . The residuary trusts of a discretionary family settlement were altered by a supplemental deed, which was subject to ad valorem stamp duty as a conveyance of property made without consideration. Duty was chargeable on "the unencumbered value of the property". The Commissioner charged duty on the value of all the assets of the fund and, in arriving at that value, took the position that the trustee's indemnity in respect of properly incurred liabilities was an encumbrance on the fund and should therefore be ignored.

129. The assessment was successfully appealed and the Commissioner's appeals to the New South Wales Court of Appeal and to the High Court were dismissed. The ratio of the High Court's decision did not depend on the meaning of "unencumbered value" and whether a trustee's right of indemnity constituted an encumbrance, but the issue had been fully considered both in the judgments below and in submissions to the High Court. Accordingly, the court stated at para 42 that they would "shortly indicate our conclusions upon these matters".

130. The court said:

> "47. … In aid of that right to reimbursement or exoneration for liabilities properly incurred in the administration of the trust, the trustee cannot be compelled to surrender the trust property to the beneficiaries until the claim has been satisfied. In that sense, the entitlement to reimbursement or exoneration confers a priority in the further administration of the trust. Accordingly, in an administration action, if it appears probable that the trust fund will be insufficient for the full recoupment of the trustee, the trustee is entitled to the insertion in the order for administration of a direction that there be payment in the appropriate order of priority.
>
> 48. Until the right to reimbursement or exoneration has been satisfied, 'it is impossible to say what the trust fund is'. The entitlement of the beneficiaries in respect of the assets held by the trustee which constitutes the 'property' to which the beneficiaries are entitled in equity is to be distinguished from the assets themselves. The entitlement of the beneficiaries is confined to so much of those assets as is available after the liabilities in question have been discharged or provision has been made for them. To the extent that the

> assets held by the trustee are subject to their application to reimburse or exonerate the trustee, they are not 'trust assets' or 'trust property' in the sense that they are held solely upon trusts imposing fiduciary duties which bind the trustee in favour of the beneficiaries."

131. Having referred at para 49 to descriptions of the nature of the trustee's right of indemnity in English authorities and in *Octavo* as a first charge on the assets vested in the trustee and as a proprietary interest in the trust property, the Court said at para 50:

> "… A court of equity may authorise the sale of assets held by the trustee so as to satisfy the right to reimbursement or exoneration. In that sense, there is an equitable charge over the 'trust assets' which may be enforced in the same way as any other equitable charge. However, the enforcement of the charge is an exercise of the prior rights conferred upon the trustee as a necessary incident of the office of trustee. It is not a security interest or right which has been created, whether consensually or by operation of law, over the interests of the beneficiaries so as to encumber them in the sense required by section 66(1) of the Act."

132. As with *Octavo*, the appellants rely on these passages as showing that the proprietary interest of a trustee in the trust property conferred by its right of indemnity exists only while the trustee holds the trust property and does not survive the transfer or vesting of the trust property in a new trustee.

133. We do not, however, consider that this submission is borne out by *Octavo* or *Buckle*. Neither of these cases was concerned with, or discussed, the position on a transfer of the trust property to a new trustee. No question of such a transfer arose in either case. *Buckle* was concerned with the right of the trustee as against the beneficiaries. It is likely that by making a distribution to beneficiaries, a trustee is taken to have waived its right of indemnity: see *Lewin on Trusts*, 20th ed, (2020) at para 24-041. It is therefore imperative to establish the rights of a trustee before a distribution is made. A transfer of the trust property to a new trustee does not affect the rights of the beneficiaries and there is no reason why the principles discussed and established in *Octavo* and *Buckle* should apply in the case of such a transfer.

134. The High Court again considered the nature of a trustee's right of indemnity, in Re Amerind Pty Ltd (in liq), Carter Holt Harvey Woodproducts Australia Pty Ltd v The Commonwealth of Australia [2019] HCA 20; 268 CLR 524 ("Amerind") . Like Octavo and Buckle before it, this was not a case concerned with the rights (if any) of a former trustee against trust assets once transferred to a new trustee, and there is no discussion of that issue in any of the judgments.

135. *Amerind* also concerned a trading trust. The trustee company became insolvent and went into receivership, and subsequently into liquidation. The issue was whether the priority in the distribution of assets enjoyed by employees of the company, over other creditors including the holders of a circulating security interest (formerly called a floating charge), applied where the property to be distributed was trust property. This issue, as analysed by the High Court, turned on whether, to the extent that such property was to be applied in meeting the trustee's right of indemnity, it was property of the trust company for the purposes of the relevant legislation.

136. The federal government (the Commonwealth) advanced some AUD$3.8m to pay accrued wages and other entitlements to Amerind's former employees under a statutory scheme. The Commonwealth was subrogated to the employees' claims which, it argued, ranked for payment out of the receivership surplus, remaining after the discharge of fixed charges, in priority to other creditors.

137. The High Court unanimously affirmed the decision of the Supreme Court of Victoria that the Commonwealth was entitled to payment out of the receivership surplus in priority to other creditors. It rejected the submissions of Carter Holt that assets held on trust by Amerind were not to any extent its property for the purposes of the relevant statutory provision and that Amerind's only property was its right of exoneration out of the trust assets which was not itself circulating property and could not therefore be subject to a circulating security interest in favour of the bank.

138. While the result was unanimous, there were some differences in the reasoning of the Justices. For present purposes, the importance of the case lies not in the resolution of the central issue but in the analysis of the nature of a trustee's right of indemnity.

139. The majority judgment is that of Bell, Gageler and Nettle JJ, with whom Gordon J agreed in a concurring judgment. At para 80, they restated the position in Australian law, as stated in *Octavo* and confirmed in *Buckle*, that where a trustee has incurred liabilities "the trustee is entitled to be indemnified (whether by recoupment or exoneration) out of the trust assets against such liabilities, and *thus* enjoys a beneficial

interest in those assets" (emphasis added). At para 83, they stated that until the trustee's right of indemnity has been satisfied,

> "the beneficiaries cannot compel the trustee to exercise the trustee's powers as legal owners of the trust assets for their benefit. A court of equity will assist the trustee to realise trust assets to satisfy the trustee's right of indemnity, in priority to the beneficiaries' interests, and thus it is said that the trustee has an equitable charge or lien over the trust assets. It is not, however, a charge or lien comparable to a synallagmatic security interest over property of another. It arises endogenously as an incident of the office of trustee in respect of the trust assets."

140. At para 84, they said: "The trustee's right to apply trust assets in satisfaction of trust liabilities is proprietary in that it may be exercised in priority to the beneficial interests of the beneficiaries" and at para 85 that "the trustee's right of indemnity confers a beneficial interest in the trust assets".

141. In her concurring judgment, Gordon J said at para 142:

> "The trustee's right of exoneration confers a proprietary interest in the trust fund which takes priority over competing interests of beneficiaries. The right of exoneration and the trustee's proprietary interest in the trust fund are inextricably linked; the trustee's interest in the fund rises and falls as debts are incurred on behalf of the trust, and satisfied out of the fund, and, of course, the right of exoneration is the basis for the existence of the trustee's fluctuating proprietary interest in the trust fund."

142. The decisions of the High Court in these three cases establish that a trustee's right of indemnity generates an equitable proprietary interest in the trust property. None of them was concerned with, or considered, whether a trustee's proprietary interest survived after the trustee had been replaced by, and the trust property transferred to, a new trustee, but they are not inconsistent with the survival of the proprietary interest.

143. It will be seen that the Australian courts have characterised the trustee's proprietary interest as a beneficial interest in the trust assets. Nothing turns on the

precise language used in this respect, but we consider that it is more in keeping with equitable principles as applied by the English courts to describe it simply as a proprietary interest.

144. Although the survival of a trustee's proprietary interest after it has ceased to be a trustee and the trust property has been transferred to a new trustee has not been considered by the High Court, it has been considered by other courts in Australia in a number of cases, both before and after the High Court's decision in *Buckle*.

145. *Coates v McInerney* (1992) 6 ACSR 748 was a first instance decision of the Supreme Court of Western Australia. It concerned a company in liquidation, whose sole business had been to act as trustee of a family trading trust. Its assets comprised four small aircraft, two of which were leased, and book debts. The liquidator sought to enforce the trustee company's indemnity. The beneficiaries submitted that such indemnity ceased on termination of the trusteeship. The judge rejected this submission, referring to "abundant authority that it is not so lost".

146. It is clear from the report that the company and the liquidator did not retain possession of the trust assets. It was argued by the beneficiaries that the replacement trustee "should be permitted to retain possession and use of the assets for the benefit of the trust". The judge rejected the submission. He ordered the defendants to deliver up the two unencumbered aircraft and he appointed the liquidator as receiver of the book debts for the purpose of realising them.

147. In *Dimos (trading as Leo Dimos & Associates v Dikeakos Nominees Pty Ltd* [1996] FCA 590; (1997) 149 ALR 113, a decision on appeal of the Full Court of the Federal Court of Australia, the trustee claiming an indemnity had been replaced but at the date of the hearing properties belonging to the trust were still registered in the former trustee's name. The question whether the trustee's proprietary interest would have survived a transfer to the new trustee did not therefore arise for decision, but Heerey J (with whom Olney J agreed) said:

> "Although the right of indemnity undoubtedly confers a right to retain possession of the trust property, it is also a proprietary right equivalent to (and ranking ahead of) the interest of the beneficiaries. As such it is probably not dependent on the retention of possession. In any event, in the present case the respondent retains the legal ownership of the properties and can thus exercise a lien in the strict sense."

148. Jenkinson J (with whom Olney J also agreed) appears also to have considered that possession was not essential to the former trustee's proprietary interest, saying:

> "In my opinion, a trustee's right of indemnity out of trust property survives the trustee's loss of office … According to the evidence before Northrop J it so happened that the legal estate in a piece of land subject to the trust, of which the respondent had been trustee when the debt alleged by the appellant was incurred, was still at the hearing of the petition in the respondent …"

149. *Rothmore Farms Pty Ltd (in provisional liquidation) v Belgravia Pty Ltd* [1999] FCA 745; (1999) 2 ITELR 159 was a first instance decision of the Federal Court of Australia. The plaintiff company (Rothmore Farms) had been the trustee of a family trust carrying on a farming business. In 1993, it ceased to be the trustee and a replacement trustee was appointed and became the legal owner of the trust assets. The judge referred to this as "the first transaction". Rothmore Farms claimed an indemnity in respect of liabilities properly incurred by it as trustee and the right to enforce the indemnity against the trust assets. Relying on *Octavo* and other authorities, the judge held that Rothmore Farm's right of indemnity gave it a first charge on the trust assets. The judge said:

> "36. The next issue to address is whether the removal of Rothmore Farms as trustee, so that it relinquished its possession of the assets of the trust, resulted in that lien or charge being lost. In my judgment, it did not. It would be a strange result if that equitable interest were capable of being lost by a transaction such as the first transaction. The persons controlling Rothmore Farms and the main beneficiaries under the trust were the Cooper Family. Mrs Cooper alone under the trust deed had power to change trustees. The transfer of assets in many cases (as in this case) could be effected by a notional change in possession or by book entries. The ease with which that equitable interest could thus be lost if the respondents are correct tends to suggest that the proposition urged by the respondents should be carefully scrutinised.
>
> 37. Authority also indicates that the equitable interest of the trustee in trust assets, to the extent of the trustee's right of indemnity against the trust assets, is not lost by a change of trustee or by giving up of possession of the trust assets by

> that former trustee." [The judge then referred to *Jennings v Mather* and to *Re Suco Gold Pty Ltd (in liq)* (1982) 33 SASR 99, a decision of the Full Court of the Supreme Court of South Australia, quoting King CJ at p 109: 'The trustee's lien is an equitable lien which confers on him a charge over the trust property, whether in his possession or not, for the purpose of protecting and enforcing the right of indemnity.']"

150. *Southern Wine Corporation Ltd (in liq) v Frankland River Olive Co Ltd* [2005] WASCA 236 was a decision of the Court of Appeal of Western Australia, allowing by a majority an appeal against an order striking out proceedings as disclosing no reasonable cause of action. The issue was whether it was arguable that a trustee/manager had, by virtue of the terms of the arrangements in question, an equitable charge over the trust assets to secure its entitlement to remuneration. The relevance for present purposes lies in a passage at para 30 in the majority judgment of McLure JA, stating general principles as regards a trustee's right of indemnity, that

> "The trustee with a right of recoupment and exoneration has an equitable charge or lien which arises by operation of law and which gives to the trustee an equitable proprietary interest in the trust assets: *Octavo Investments Pty Ltd v Knight* (1979) 144 CLR 360 at 367; *Commissioner of Stamp Duties v Buckle* at 247. Accordingly, a former trustee can claim against persons to whom title to the trust assets has passed. Loss of office does not deprive a trustee of an accrued right of indemnity: *Coates v McInerney* (1992) 7 WAR 537."

151. In *Glazier Holdings Pty Ltd (in liq) v Australian Men's Health Pty Ltd (in liq)* [2006] NSWSC 1240, a decision at first instance in the Equity Division of the Supreme Court of New South Wales, the respondent had been the trustee of a trust operating medical clinics on a substantial scale. In 1997, it was removed as trustee by a consent order, and the court made orders vesting the trust assets in the replacement trustee. It ceased to hold any trust assets. Subsequently, the new trustee sold the trust assets and lodged the proceeds of sale in court. The respondent had incurred substantial liabilities as trustee, and it claimed a lien in respect of those liabilities over the proceeds of sale in court. White J held that the respondent was entitled to the funds in court in priority to the beneficiaries, saying at para 38 that the "trustee's right to be indemnified, by exoneration or recoupment, out of the trust assets for liabilities properly incurred in execution of the trust is not lost if the trustee is removed".

152. White J's statement at para 38 was cited with approval by Allsop J (now Allsop CJ) at first instance in the Federal Court in *Bruton Holdings Pty Ltd v Commissioner of Taxation* (2007) 244 ALR 177. Allsop J's order was reversed by the Full Court but restored on appeal by the High Court, on grounds which do not concern the right of indemnity. In its unanimous judgment ([2009] HCA 32; 239 CLR 3460), the High Court said at para 43:

> "… by force of cl 13 of the Trust Deed, the appellant has a lien on the trust assets for all liabilities, costs and expenses properly incurred by it in administration of the Trust. Further, even without that express provision, the appellant has rights of recoupment or exoneration in respect of all obligations incurred by it in that administration. These rights were supported by a lien over the whole of the trust assets which amounted to a proprietary interest therein (*Chief Commissioner of Stamp Duties (NSW) v Buckle* (1998) 192 CLR 226 at 245-246, paras 47-49; [1998] HCA 4) and they survived the appellant's loss of office as trustee (*Dimeos v Dikeados Nominees Pty Ltd* (1996) 68 FCR 39; *Glazier Holdings Pty Ltd (in liq) v Australian Men's Health Pty Ltd (in liq)* [2006] NSWSC 1240)."

153. In *Ronori Pty Ltd v ACN 101 071 998 Pty Ltd* [2008] NSWSC 246, a decision at first instance of the Supreme Court of New South Wales, the defendant had been the trustee of a unit trust. It ceased to be the trustee on being wound up, pursuant to the terms of the trust deed. Although it was under an obligation to transfer the trust property to the replacement trustee, it was reluctant to do so because of concerns that it might then be unable to enforce its right to an indemnity. In the circumstances of the case Barrett J did not make a vesting order, leaving it to the former trustee to transfer the trust assets, as it was required to do. However, he set out the legal position as follows:

> "15. In the present case, therefore, the former trustee continues to enjoy a beneficial interest in the trust property commensurate with its right of indemnity out of that property. Although the trustee's right to resort to trust property is sometimes described as a lien, it is not essential for the enjoyment and effectuation of the right that possession of the trust property be retained. The right entails, as I have said, a beneficial interest in the property. It is not in the nature of a possessory security.

> 16. Where there is a change of trustee, the former trustee's interest remains enforceable against the trust property …
>
> 18. It is thus clear that, even though the trust assets have passed out of the former trustee's possession, the vindication of that person's beneficial interest remains available by way of an appropriately constituted claim against the new trustee. There need therefore be no concern on the part of the court about recognising immediately the right of the new trustee to have the trust property vested in it."

154. In *Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd* [2008] NSWSC 1344, another first instance decision of the Supreme Court of New South Wales, the trustee of a discretionary trust was ordered to be wound up and thereupon, pursuant to the terms of the trust deed, ceased to be the trustee. The replacement trustee applied for an order vesting the trust assets in it, which was resisted by the former trustee on the grounds that it was entitled to retain them as security for its rights of indemnity. Brereton J said at para 21 that if trust property was transferred to a new trustee, the new trustee took subject to the former trustee's lien. On this basis, he held that a former trustee does not have a right to retain trust assets as against a new trustee, unlike its right to retain trust assets as against beneficiaries. While that decision has since been criticised at first instance in the Federal Court of Australia (*Apostolou v VA Corporation Aust Pty Ltd* [2010] FCA 64), the statement at para 21 has not been challenged. It was approved at first instance by the Supreme Court of Victoria in *Pitard Consortium Pty Ltd v Les Denny Pty Ltd* [2019] VSC 614. McDonald J said at para 15:

> "The former trustee's equitable lien is not a right of possession. It is a security which survives the transfer of trust property to a new trustee. Further, it can be enforced against trust property in the hands of the new trustee. The new trustee receives the trust property subject to the former trustee's equitable lien."

155. Finally, the Court of Appeal of New South Wales in *Agusta Pty Ltd v Provident Capital Ltd* [2012] NSWCA 26 held, as part of the ratio of the decision, that a former trustee's proprietary interest continues to bind trust property after a transfer of the legal title to a replacement trustee. Barrett JA, with whom the other members of the court agreed, said at para 44: "After such a transfer, the original trustee's preferred

beneficial interest continues to subsist in the trust property in the new trustee's hands". At para 83, he said:

> "Both before and after the alienation, execution at law was not open to trust creditors but they were entitled to assert Agusta's preferred beneficial interest and thereby obtain equitable execution through the sale of trust property by a receiver appointed by the court. The fact that Agusta's preferred beneficial interest and the creditors' rights of subrogation in relation to it subsisted in the trust assets after they became vested in the new trustee meant that it was not incumbent upon Agusta to obtain from Riva any particular undertaking to protect those creditors."

156. These judgments represent a substantial body of authority in Australia that a trustee's proprietary interest in the trust property is not lost by a transfer of the property to a new trustee.

157. The appellants relied on two authorities in support of a submission that this was not the position in Australian, or English, law, and that the interest depended on continued possession.

158. First, the appellants relied on a statement of King CJ in *In re Suco Gold Pty Ltd (in liq)* [1982] SASR 99, a decision of the Full Court of the Supreme Court of South Australia, at p 109 that "[t]he right of possession of the trustee, until his right of indemnity is exercised, is superior to those of a new trustee". It is, however, important to read that sentence in context. King CJ said:

> "The trustee's lien is an equitable lien which confers on him a charge over the trust property, *whether in his possession or not*, for the purpose of protecting and enforcing the right of indemnity. It *also* confers on the trustee a right to possession of the trust property for the purpose of protecting and enforcing the right of indemnity, *Jennings v Mather* [1902] 1 KB 2. The right of possession of the trustee, until his right of indemnity is exercised, is superior to those of a new trustee or the cestuis que trust." (Emphasis added)

159. As it appears to us, this passage supports the proposition that a trustee's proprietary interest survives a transfer to a new trustee.

160. Second, the appellants relied on a unanimous decision of the Court of Appeal of Queensland in *Belar Pty Ltd (in liq) v Mahaffey* [1999] QCA 2. Belar Pty Limited (Belar) had been the trustee of a family trust. It was wound up on the ground of its insolvency, following which it was replaced as the trustee. Belar, acting by its liquidators, brought proceedings against the five beneficiaries, seeking declarations that certain loans were trust assets and that it was entitled to be indemnified from the loans in respect of liabilities incurred by it as trustee. The trial judge held that Belar failed to establish the existence of the loans and, in any event, they would not have been trust assets. Despite these findings, the judge made a declaration that Belar was entitled to be indemnified from the loans. The Court of Appeal held that, in view of the judge's findings, the declaration should not have been made and set it aside.

161. The passage from the court's judgment on which the appellants rely, which was necessarily obiter, was:

> "19. A trustee's right to an indemnity against trust assets in respect of expenses properly incurred by the trustee in the conduct of the business of the trust is well recognised. In conducting the business of the trust, the trustee becomes personally liable for debts incurred.
>
> > 'However, he is entitled to be indemnified against those liabilities from the trust assets held by him and for the purpose of enforcing the indemnity the trustee possesses a charge or lien over those assets.' [*Octavo* at p 367]
>
> That is a reference to trust assets in the trustee's possession. When there is a change of trustee with the trust assets being vested in the new trustee, the former trustee no longer has direct access to such assets, and should make the necessary claim for indemnity against the trustee who represents the trust.
>
> 20. The trustee's right of indemnity out of the trust assets is in the nature of a charge or lien in favour of the trustee and as such takes preference or priority over the claims by the cestuis que trust. But of course when the assets have passed out of the trustee's possession the necessary claim for a

> trustee's indemnity should be made against the new trustee."

162. The court made clear what it meant by "the necessary claim for a trustee's indemnity … against the new trustee" at para 24:

> "A former trustee may assert its claim for indemnity against the continuing trustee, and in that respect may assert the right of the new trustee to indemnity by bringing an action against him."

163. With respect to the court, we are unable to accept that it would be open to the former trustee to bring such a claim against the new trustee. The new trustee incurs no personal liability to the former trustee in respect of the expenses incurred by the latter while it was the trustee. The new trustee therefore has no claim of its own, in respect of such expenses, for indemnity out of the trust property and therefore there is no such claim to which the former trustee could be subrogated. We do not therefore consider that the court's obiter analysis of the termination of a trustee's proprietary interest when the trust assets pass out of its hands can be treated as authoritative.

164. We conclude that the numerous Australian authorities in which the survival of a trustee's proprietary interest in the trust assets after transfer to a new trustee has been considered provide substantial support that such interest is not lost on transfer of the assets to a new trustee.

165. As on the first issue, the leading textbooks take the position that the trustee's proprietary interest does not cease once the trust assets are vested in a replacement trustee but continues to bind the trust assets. See *Underhill & Hayton: Law of Trusts and Trustees*, 19th ed, at para 81.1; *Snell's Equity*, 34th ed, at para 44-004; *Lewin on Trusts*, 20th ed, at 17-057 and 17-058.

166. On the second issue, for the reasons given above, we consider that the proprietary interest generated by the trustee's right of indemnity survives the transfer of the trust property to a new trustee.

Priority as between the proprietary interests of successive trustees

167. The third issue is whether the former trustee's proprietary interest in the trust property takes priority over the claims of subsequent trustees under their rights of indemnity.

168. This is not an issue which has arisen for decision in any authority to which the Board was referred. Nor does it appear to have been the subject of any discussion or submissions in any of those authorities, apart from obiter statements in two Australian decisions which suggest that a former trustee enjoys priority over a subsequent trustee (*Lemery Holdings Pty Ltd v Reliance Financial Services Pty Ltd* (supra) at para 21 and *In re Suco Gold Pty Ltd (in liq)* (supra) at p 109). The issue has simply not arisen, and it is not therefore surprising that the authorities are silent on it. In our view, this almost complete absence of comment cannot assist any of the parties before the Board.

169. It is therefore an issue which requires a clear understanding of the nature of the proprietary rights created by the right of indemnity. In this connection, we would emphasise a number of the characteristics of the right of indemnity discussed above.

170. First, it does not create any personal liability to indemnify a trustee or former trustee. There is no person, including a subsequent trustee, against whom the trustee or former trustee can obtain judgment for any amount due under the indemnity. It is instead a right to have the trust property applied in payment of such amount.

171. It follows that the right to have the trust property so applied is not security for the payment of a debt. We do not consider that it is right to speak of a lien or charge over the trust property as securing or supporting the right of indemnity. This language would be appropriate if there were a separate liability imposed on a person to pay amounts due under the indemnity, but there is no such liability. There is simply the right to have the trust assets applied in the exoneration or reimbursement of the trustee. It is that equitable right, enforceable by an order of the court requiring the trust fund to be so applied, that creates the trustee's proprietary interest. There is, in other words, no difference between the right of indemnity and the proprietary interest. The right of indemnity and the application of the fund in providing the necessary exoneration or reimbursement are one and the same thing.

172. Second, the remedy to enforce that right is an order that the trust property be applied in paying the amount due under the right of indemnity. It is the availability of this remedy which underlies the characterisation of the right of indemnity as

conferring on a trustee or former trustee an equitable proprietary interest in the trust property, akin to that created by a conventional equitable charge. Equity acts in personam, so the order is not an order in rem but an order that the person holding the property must apply it so as to indemnify the trustee, but the effect is to create an equitable interest in the property. The position is analogous to the effect of specific performance as a remedy to enforce a contract of sale, which is to confer on the purchaser an equitable proprietary interest in the subject property.

173. This point was made, in a context which did not involve a transfer to a new trustee, by McPherson J in *Kemtron Industries Pty Ltd v Commissioner of Stamp Duties* [1984] 1 QdR 576, a decision of the Full Court of the Supreme Court of Queensland, at p 585 where he said that the trustee's right over or in respect of the trust assets

> "is often spoken of as a 'charge' over the assets; but this is really a conclusion deriving from the fact that in proceedings in court for administration of the trust, the claim of the trustee to be indemnified will be given effect by directing that liabilities properly incurred by him are paid out of the trust assets in priority to the claims of beneficiaries to their interests in the trust property."

174. A similar point was made by the majority in *Amerind* at para 83:

> "A court of equity will assist the trustee to realise trust assets to satisfy the trustee's right of indemnity, in priority to the beneficiaries' interests, and thus it is said that the trustee has an equitable charge or lien over the trust assets."

175. Third, for the reasons discussed earlier, a trustee's right of indemnity is a personal right enjoyed by a trustee for its own benefit and protection.

176. The general rule as to the priority of equitable interests is determined by the order of their creation. As Millett J said in *Macmillan Inc v Bishopsgate Investment Trust (No 3)* [1995] 1 WLR 978, 999-1000:

> "In English law the order of priority between two competing interests in the same property depends primarily on whether they are legal or merely equitable interests. Where both interests are equitable - or both legal, for that matter - the

> basic rule is that the two interests rank in the order of their creation. In the case of equitable interests the order of priority may be reversed in special circumstances, but 'where the equities are equal, the first in time prevails'. The absence of notice of the earlier interest by the party who acquired the later interest is irrelevant, even if he gave value."

177. In our view, the proprietary interests of successive trustees in the trust assets are clearly competing or equal. The interest of each trustee arises so as to protect the personal position of that trustee against the liabilities which it has incurred and for which it is liable. These are personal interests of each trustee and it is difficult to see that they can be regarded as not equal or competing, in the absence of special circumstances which would make it inequitable for an earlier appointed trustee to rely on its priority (see *Abigail v Lapin* [1934] AC 491). No such circumstances are suggested in either of the present appeals.

178. The appellants, through Mr Machell whose arguments on this issue on behalf of the Guernsey appellants were adopted by the Jersey appellants, submitted that the "first-in-time" rule is only a general rule and that it is open to the court, in exercise of its equitable jurisdiction, to develop a different rule applicable to the order of priority as between the rights of indemnity of successive trustees, so as to produce a fair outcome in the light of the particular position of trustees and creditors claiming through them. Such rights are sui generis and so the court should not feel bound to apply a general rule developed to meet other categories of equitable interests.

179. Mr Machell submitted that in the case of some competing equitable interests, a different order of priority has been developed by the courts. Examples he gave included the rule in *Dearle v Hall* (1828) 3 Russ 1, governing the order of priority as between dealings with equitable interests in personal property, which is determined by reference to the order in which notice is given to the legal owner of the property, and solicitors' liens. Mr Taube, appearing for the Guernsey respondents, disputed whether these were examples of competing interests. It is unnecessary to resolve that issue, as we do not doubt that it is open to the court to develop a rule other than the first-in-time for a particular category of interests. The question is whether the court should do so with regard to the equitable interests in trust property generated by trustees' rights of indemnity.

180. In this respect, the appellants drew attention to features of the equitable interest created by the right of indemnity. First, it arises by operation of law, rather than as a result of consensual dealings between parties, as in the case of conventional equitable charges. Second, it does not secure a debt because there is no obligor and no

debt. While these are indeed features of some significance, we cannot see that they provide a basis for departing from the general rule. The fact that there is no personal claim against a debtor is an important distinguishing feature of the trustee's right of indemnity, but the right nonetheless generates successive interests in the trust assets and its purpose is to hold each successive trustee harmless against liabilities which it has incurred. It is conceptually different from a secured debt but in economic terms it is closely analogous. We do not therefore consider that there is something in the nature of the right of indemnity which suggests that the general equitable rule as to priorities should not apply.

181. It was further submitted that the right of indemnity was conferred by equity not only for the benefit of the trustee, but also for the benefit of its trust creditors, and that this feature pointed to the adoption of a different approach to the "first-in-time" rule.

182. We do not accept the premise of this submission. As earlier discussed, the authorities show that the purpose of the right of indemnity, the reason why equity confers it, is the personal protection of the trustee. It is to ensure, so far as the trust assets permit, that the trustee is not out of pocket as a result of liabilities for which it is responsible but which are incurred not for its benefit but for the proper purposes of the trust. It is true, of course, that the trustee's creditors can, as its creditors, gain access to its right of indemnity in order to obtain payment of the debts due to them. If the trustee has paid a trust debt and has a resulting right of reimbursement from the trust property, that is property which is available for execution by *any* creditor of the trustee, including creditors whose debts are unconnected with the trust. If the trustee has not paid a trust debt but has a right of exoneration from the trust property, it is only unpaid trust creditors who may enforce such right by way of subrogation. It is, however, important to remember that it is the trustee's own right of exoneration to which the creditor is subrogated. That right is to payment of only such amount as is due after account is taken of any amounts for which the trustee is accountable to the trust. This underlines that the right arises for the benefit of the trustee, and that any benefit to trust creditors is both limited and indirect. We do not consider that the authorities establishing the trustee's right of indemnity contain anything to suggest that the purpose of the right is, even in part, to benefit "trust creditors".

183. Even if it were accepted that part of the purpose of a trustee's right of indemnity is to provide protection to its trust creditors, that is not, in our view, a factor which suggests that the priority given by the "first-in-time" rule should not apply.

184. While acknowledging the separate liability of trustees for the debts which they respectively incur and the absence of any separate legal personality for a trust, it was

submitted that, in a commercial or stewardship sense, a trust can properly be seen as a continuum, even as an institution. It was submitted that trusteeship, for this purpose, should be seen as a continuum, unbroken by changes in the person holding the office. Given that the liabilities covered by the right of indemnity are necessarily incurred for the purposes of the trust, there is, it was submitted, no reason why liabilities incurred by one trustee should be regarded as more deserving of protection than liabilities incurred by a subsequent trustee. Allied to this, the appellants submitted that "equality is equity" is the principle that underlies the pari passu distribution of insolvent estates, whether of individuals or companies.

185. This submission prioritises common economic characteristics of a trust over the legal nature of a trust. The trustee's right of indemnity is to provide the trustee with protection against liabilities which it incurs and, as regards liabilities, a trust is not a continuum. It is the current trustees, not the trust nor the successor trustees, which incur liabilities. The position is fundamentally different from that of an insolvent individual or company. An individual or a company is, in the sense used by Mr Machell, a continuum. All the relevant liabilities are incurred by that individual or company, and most legal systems have regarded the pari passu distribution of the available assets among the creditors of *that* individual or company as just and fair in the event of the insolvency of the individual or company. Further, the pari passu distribution of available assets is a principle of distribution among unsecured creditors. A trustee, in respect of its right of indemnity, is not a creditor because it has no personal claim against anyone but instead it has a proprietary interest in the trust assets.

186. By way of further development of this submission, it was said that, as regards "trust creditors", a pari passu distribution was the principled and fair outcome where there were insufficient assets available to meet all their claims. Again, this treats "trust creditors" as creditors of the trust, rather than as creditors of the trustee with whom they dealt. It also wrongly suggests that the trust assets would be distributed on an equal basis among all the creditors, much as happens with distributions among the unsecured creditors of an insolvent individual or company. The share of trust assets distributed to the creditors of different trustees would depend entirely on the state of account between each trustee and the trust, meaning that the creditors of one trustee might receive a larger dividend in the £ than the creditors of another trustee. Subrogation, as the indirect means whereby creditors of trustees can gain access to trust assets, is not designed to produce a pari passu distribution among all "trust creditors". It would be a happenstance if it did so.

187. A further submission advanced for not applying the "first-in-time" rule was that, assuming the equitable interest of a trustee arises on appointment, surprising consequences follow where, for example, current trustees were appointed on different

dates or a current trustee was appointed before a former trustee. It is said that the first-appointed trustee would gain an unjustified advantage over the later-appointed trustee or trustees.

188. No problem arises in such cases where trustee A incurs a liability before the appointment of trustee B. Equally, it will rarely cause a problem as regards liabilities incurred while they are all in office, as such liabilities are usually joint liabilities of the trustees, so that discharge by one trustee will discharge them all. While it would be true to say that, in those cases where trustee A alone incurred a liability while trustee B was also a trustee, trustee A would have priority over trustee B, we consider any concern in this respect to be largely theoretical. As regards trusts with individuals as trustees, typically family settlements, the issue has never arisen so far as is known, certainly in England and Wales or in Jersey or Guernsey. This no doubt reflects the conservative way in which such trusts are typically managed. In reality, the problem arises in those cases, including trading trusts found in Australia, where the trustees take on liabilities of a type and on a scale normally found in commercial businesses. The trustees will almost inevitably be companies, as in the Australian cases and the present appeals. If there is at any time more than one trustee, they will frequently be appointed simultaneously but, if not, they will be able to negotiate arrangements which are satisfactory to them. We see no practical basis for Mr Machell's submission that application of the first in time rule would undermine the collegial and co-operative manner in which trustees should operate and the collective endeavour in which they are engaged.

189. The appellants pointed to a number of suggested consequences of the application of the "first in time" rule to the rights of indemnity of successive trustees which, it was said, would be detrimental to the proper and efficient administration of trusts. First, creditors might be unwilling to agree to a novation of their claims to a new trustee, as they would rank behind the claim of the former trustee as regards debts which were not novated. Second, there could be difficulties for a successor trustee seeking to raise finance secured on trust assets, given the prior claim of the former trustee. Third, the successor trustee may not be aware of the full extent of the liabilities of the former trustee, potentially making it difficult for the successor trustee to assess whether liabilities which it incurs will be paid. Considerations like these were described by the Commissioner as "inimical to the good administration of trusts" in his judgment at first instance at para 128. Sir Michael Birt also drew attention to these difficulties in an article, *Priority of Claims to the Assets of an "Insolvent Trust"* (2020) 24 Jersey and Guernsey Law Review 5. It is also said that the former trustee can protect its position by requiring security or retaining trust assets pending determination and settlement of claims against it.

190. We are not persuaded that considerations of this sort can or should lead to the application of a different priority regime for trustees' rights of indemnity. There are numerous counter-balancing considerations. First, the former trustee can be required to provide all information known to it as regards actual, disputed or contingent liabilities. It is of course possible that the former trustee might be unaware of a particular liability, but equally the successor trustee could be unaware of a liability it has incurred. The possibility of unknown liabilities is an inherent risk for all trustees, just as it is for all businesses. Second, leaving aside the problem of unknown liabilities, any assessment of contingent liabilities for the purpose of fixing the amount of security over trust assets taken on the change of trustees may well prove to be inadequate. Third, the former trustee has no control over, or even knowledge of, the successor trustee's administration of the trust and is therefore exposed to the risk of the trust becoming "insolvent", against which "first in time" priority provides some protection. In particular, the former trustee is exposed to the risk of successor trustees managing the trust assets on a more speculative basis, increasing the trust liabilities relative to the assets and thereby increasing the risk of insolvency. Provided that the successor trustees did not act in breach of trust, their interest by way of indemnity would on the appellants' case rank pari passu with the former trustee's interest. Fourth, the Jersey courts have since the Board's decision in *Investec 1* taken into account the priority of the former trustee's right of indemnity in determining the amount of "reasonable security" to which it is entitled under what is now article 43A of the TJL: see *In re The Velloz Settlement* [2021] JRC 140 at para 36. This assists the administration of trusts by reducing the need for the retention or ring-fencing of trust assets.

191. We have earlier referred to the protections provided to outgoing trustees as regards their rights of indemnity: see para 113 above. In our view, this is a significant factor when considering whether the usual equitable principle of priority of interests applies. The provision of such protection is inconsistent with the rights of indemnity of successive trustees for properly incurred liabilities ranking pari passu. If those rights rank pari passu, it is difficult to identify any principled reason for providing protection to outgoing trustees.

192. As the judgment of Wilberforce J in *In re Pauling's Settlement (No 2)* makes clear, the English courts have been astute to protect outgoing trustees, in that case by refusing to appoint new trustees while the liability of the existing trustee for the costs of proceedings and for estate duty remained uncertain. Wilberforce J said as regards the costs of the proceedings:

> "It is inevitable that some security should be held by the bank, as trustees, for their costs…any trustee is entitled to have security as regards his costs, if those costs are properly

> incurred, and there is great difficulty in ordering the bank to part with the trust fund in their hands until it can be seen what rights the bank may have against the trust fund in respect of costs…the security for the payment of those costs would be the £20,000 odd, to which I have already referred as forming the remnant of the trust fund. There is, therefore, considerable objection to making an order by which the possession of that fund would be transferred at this stage out of the bank's possession." ([1963] 1 All ER 857 at 860.)

Wilberforce J applied a similar approach to the contingent liability for estate duty; see p.863.

193. The Jersey appellants submitted that, on the replacement of a trustee, the outgoing trustee can insist on retaining possession of the trust property or that part of it which is reasonably estimated to reflect the value of its indemnity rights. They also submitted that, in the ordinary course of a trustee's retirement and replacement, the outgoing trustee may require security to be given. While there are Australian authorities to the effect that an outgoing trustee has a *right* to retain sufficient trust assets to meet the trust liabilities incurred by it, the position is not clear.

194. However, on any basis, an outgoing trustee is entitled to seek, by agreement or by court order, the retention of sufficient trust assets or the provision of sufficient security to meet its trust liabilities. If any liabilities are contingent or uncertain in amount, a reasonable estimate will be made for these purposes. As Lewin on Trusts states at 17-004, "an outgoing trustee has an obligation, subject to reasonable protection in respect of liabilities in accordance with his rights of indemnity, to do everything to vest the trust property" in the new trustees.

195. This entitlement to the provision of reasonable protection is made express in section 19(3) of the Trusts of Land and Appointment of Trustees Act 1996 in the cases to which it applies. A trustee who is directed by all the beneficiaries to retire and appoint a new trustee must comply with the direction where (among other things) "reasonable arrangements have been made for the protection of any rights of his in connection with the trust".

196. More generally, under Jersey law, the TJL in art 34(2) (now replaced by art 43A) provided that a trustee "who resigns, retires or is removed may require to be provided with reasonable security for liabilities whether existing, future, contingent or otherwise before surrendering trust property". Where there are possible outstanding

liabilities, such as disputed fees, the Jersey courts have held that retiring trustees are entitled to security and have, for example, ordered funds to be held in an escrow account or a ring-fenced account: see *In re Carafe Trust* [2005] JRC 063, *In re Caversham Trustees Ltd* [2008] JRC 065.

197. Given that such security is provided in place of the outgoing trustee's possession of the trust assets, and with a view to securing the outgoing trustee's right to obtain exoneration or reimbursement from the trust assets, it follows that this is security in the full sense of the word. It is not, as Mr Machell suggested, loosely analogous to a freezing injunction which would do no more than restrict the new trustee's right to deal with the assets concerned.

198. Where liabilities are contingent or uncertain in amount, an estimate will be made, by the court if necessary, of their value with a view to determining the amount of security to be provided to the outgoing trustee.

199. The position is therefore that, if the existence of such contingent or unascertained liabilities is known when the change in trustees is made, the outgoing trustee will or may have the benefit of express security, putting it to that extent ahead of, not pari passu with, successor trustees. Not only is this inconsistent with the pari passu principle for which the appellants argue, but adoption of the pari passu principle would produce capricious results. Whether an outgoing trustee enjoyed security or priority for its trust liabilities, and the extent of it, would depend, first, on knowledge that the liability existed and, second, on the accuracy of the estimate made of it.

200. Adoption of the pari passu approach will result in outgoing trustees insisting on increased security to guard against future liabilities and a subsequent inadequacy of the fund, creating greater difficulties in the administration of the trust. By contrast, if the first in time approach applies, the priority of the outgoing trustee's proprietary interest will reduce the scope for argument as to what is needed to provide "reasonable security". First in time not only accords with principle but provides a coherent approach with commercial and administrative advantages.

201. Before leaving the issue of priority, we wish to comment briefly on the support said to be derived from the way in which equity has approached the application of *Clayton's Case* (*Clayton's Case*, *Devayne v Noble* (1816) 1 Mer 572, 35 ER 781) to the distribution of mixed funds.

202. It was held in *Clayton's Case* that, where there was a running account between a bank and a customer, payments into the account were taken to be applied to

payments out of the account in the order in which the payments in had been made: first in, first out. The question subsequently arose as to whether and, if so, when this common law principle should be applied to mixed funds to which third parties had contributed and which were wholly or partly held on trust for those third parties. It was held by the Court of Appeal in Chancery in *Pennell v Deffell* (1853) 4 De GM & G 372, 43 ER 551 and affirmed by the Court of Appeal in *Hancock v Smith* (1889) 41 ChD 459 that, in general, the principle did apply to such funds. Its application was not, however, automatic. In *In re Hallett's Estate*, *Knatchbull v Hallett* (1880) 13 ChD 696, the Court of Appeal reiterated its general application but held that where the fund comprised both monies contributed personally by the account holder and monies held on trust by him for third parties, the trustee was presumed in keeping with basic equitable principles to have applied his own funds first to his personal outgoings. To that extent, the rule in *Clayton's Case* was not to be applied.

203. Although commonly referred to as a "rule", its true nature was accurately described by Jessel MR in *In re Hallett's Estate* (1880) 13 ChD 696, 728, in a passage cited with approval by Lord Macnaghten in *Cory Bros & Co Ltd v Turkish Steamship Mecca (owners)*, *The Mecca* [1897] AC 286, 295-296, where he said that it was:

> "a very convenient rule, and I have nothing to say against it unless there is evidence either of an agreement to the contrary or of circumstances from which a contrary intention must be presumed, and then of course that which is a mere presumption of law gives way to those other considerations."

204. In a number of subsequent cases, including *Barlow Clowes International Ltd (in liq) v Vaughan* [1992] 4 All ER 22, *Clayton's Case* was not applied but instead the fund was ordered to be distributed among the contributors on a pari passu basis, by reason of the existence of particular circumstances in those cases from which a contrary intention was to be presumed (the presumed intention being that of the contributors to the mixed fund).

205. By contrast, the present appeals are not concerned with the distribution of mixed funds among those who have contributed to them nor with a presumption based on convenience. These appeals are concerned with the issue of priority of successive equitable proprietary interests of trustees over the trust assets. Equity accords priority to proprietary interests in the property of another on the basis of first in time, not as a matter of convenience but as a matter of principle. We do not consider that the authorities dealing with *Clayton's Case* provide any assistance in determining the issue of priority arising in these appeals.

206. As an alternative to their principal submissions on the priority issue, the appellants submitted that the date of creation of the equitable interest generated by the right of indemnity was not the date of appointment of the trustee, but the date on which a liability arose. If there were a number of liabilities, the right of indemnity would rank in priority in respect of each liability according to the date of each liability. The Guernsey appellants accepted that this would give rise to very considerable practical difficulties while, in the Jersey proceedings, the Commissioner had referred to "a difficult and cumbersome inquiry" in his judgment at para 147.

207. It is clear from the earliest English authorities that the right of indemnity is an incident of appointment as a trustee. It is, as Lord Eldon said at p. 252 in *Worrall v Harford*, "in the nature of the office of trustee, whether expressed in the instrument or not, that the trust property shall reimburse him all the charges and expenses incurred in the execution of the trust. That is implied in every such deed." In *Exhall Coal*, Lord Romilly MR described it at p. 453 as "a right incidental to the character of trustee and inseparable from it". The right, and its concomitant interest, are thus created on appointment. It may be a contingent interest until a liability is incurred, but the interest exists from the trustee's appointment. As Mr Taube submitted on behalf of the Guernsey respondents, the appellant's submission conflates two distinct matters, the existence of the right of indemnity and its exercise.

208. The appellants point to a number of Australian authorities at first instance and one in the Court of Appeal of Western Australia (*Southern Wine Corpn Pty Ltd (in liq) v Frankland River Olive Co Ltd* [2005] WASC 236) containing obiter statements that the right of indemnity arises or accrues when a relevant trust-related liability is incurred. These statements are accurate in the sense that it is only then that the right becomes enforceable. The date of creation of the right and the equitable interest were not in issue in any of those cases.

209. We accordingly reject the appellants' alternative submission.

210. In our view, the priority ranking of successive trustees' equitable interests in the trust property should be governed in accordance with principle. The general rule applicable to competing equitable interests is that priority is determined by the order of creation, and we see no sufficient reason for developing and applying a different principle to the equitable interests of trustees in respect of their rights of indemnity.

211. We therefore conclude that, as a matter of English law, a trustee's right of indemnity creates in favour of the trustee an equitable proprietary interest in the trust property which continues to exist after the trustee has ceased to hold office and after

the trust property has been transferred to or vested in a new trustee. It is also our view that, as a matter of English law, the interests of successive trustees rank as between themselves in the order of their creation, that being the date of appointment of each trustee.

212. We therefore reject the submissions of the appellants as to the relevant principles of English law. For the reasons given above, the last two sentences of para 59(v) in *Investec 1* require some modification, rather than rejection. The trustee's right of indemnity creates in the trustee's favour an equitable proprietary interest in the trust assets, frequently referred to as an equitable lien or charge in the English authorities. Because such interest does not depend on possession, it survives the replacement of the trustee and the vesting of the trust assets in a new trustee. As we have already noted, we do not regard *Re Johnson* (supra) as authority for this proposition but there is substantial other authority to support it and it is, in any event, correct in principle.

213. It follows that these principles form part of the law of trusts in Jersey except to the extent, if any, to which they are inconsistent with Jersey customary law or provisions of the TJL.

Jersey law

214. As earlier observed and as decided by the Board in *Investec 1*, the principles of English trust law form part of Jersey law, save to the extent that they are inconsistent with or modified by Jersey customary law or the TJL. The appellants submitted that there were in a number of respects inconsistencies or modifications which, even accepting the English law analysis set out above, should result in their appeals being allowed. Some of these submissions on Jersey law had not been advanced in the courts below and thus require the Board's permission to be raised, which we would give. Although there is a particular importance and value in issues of local law being raised and decided by the local courts before consideration by the Board, none of these submissions required new evidence and they were fully argued before the Board.

215. First, the appellants submitted that a trustee's equitable lien was incompatible with the prohibition, or non-recognition, under Jersey customary law of any non-possessory security of movable property, which we understand to extend to any property other than land or interests in land. The established principle is *meuble n'a point de suite par hypothèque*. Although this submission was not made to the courts below, it was raised by the Bailiff in his judgment.

216. We are satisfied that, in the light of our analysis of the trustee's equitable lien, no inconsistency with this principle of customary law arises. For the reasons given above, the lien is not a form of security. There is no personal obligation to secure. The "lien" is the proprietary interest in trust assets which the right of indemnity gives to a trustee. Mrs Warnock Smith, who argued this part of the appeals, accepted that, if this was the correct analysis, there was no inconsistency with customary law.

217. Turning to the provisions of the TJL, the appellants submitted that the continued existence in favour of a trustee of a lien over or a proprietary interest in the trust assets after the trustee has ceased to hold office and after the trust assets have been transferred to a new trustee is incompatible with article 34(2) (now article 43A, inserted by the Trusts (Amendment No 7) (Jersey) Law 2018 with effect from 8 June 2018) of the TJL. The effect of enacting article 34(2) was therefore, in this respect, to alter by necessary implication the relevant principle of English trust law.

218. Article 34(1) and (2) provided:

> "(1) Subject to para (2), when a trustee resigns, retires or is removed, he or she shall duly surrender trust property in his or her possession or under his or her control.
>
> (2) A trustee who resigns, retires or is removed may require to be provided with reasonable security for liabilities whether existing, future, contingent or otherwise before surrendering trust property."

219. It is also relevant to refer to article 19 which makes provision for the resignation and removal of a trustee. Article 19(5) provides:

> "A person who ceases to be a trustee under this Article shall concur in executing all documents necessary for the vesting of the trust property in the new or continuing trustees."

220. The TJL does not contain a provision for the automatic vesting of trust property in new or continuing trustees, such as appears in section 40 of the Trustee Act 1925.

221. The appellants submitted that article 34(2) would be rendered otiose if a trustee's proprietary interest arising by reason of its right of indemnity were held to

survive the transfer of trust property to a new trustee. We have, for the reasons given above, rejected this submission as regards the rights of trustees under English law. The same reasons apply to reject this submission as regards Jersey law. In short, the enactment or existence of other protections for a former trustee is not incompatible with the survival of the trustee's proprietary interest which is not attended by the practical protection given by the provision of security. As well as having assets expressly charged or set aside, the security provided might well give the former trustee means of enforcement not available as regards its equitable proprietary interest. The restriction to "reasonable" security is likely to result in the trustee not receiving security for unforeseen or unlikely contingent liabilities, of which I&B's liability to the liquidators of Angelmist is an example. Any suggested conflict falls far short of what is required for a conclusion that, by necessary implication, the existing equitable right of a former trustee to a continuing proprietary interest is abrogated by article 34(2).

222. The Jersey appellants further submitted that the terms of the DORA negotiated and entered into by ETJL when it ceased to be the trustee left no room for ETJL to continue to enjoy any rights against or interest in the trust assets, other than as provided by the DORA. The continuation of any other rights or interest was so incompatible with the terms of the DORA that ETJL must be taken, by implication, to have waived them. This is not a submission available in the Guernsey appeal, because I&B did not enter into an equivalent agreement.

223. Mrs Warnock Smith drew the Board's attention, first, to some of the recitals to the DORA. Recital (E) stated that ETJL was willing to accede to the beneficiaries' request to resign "in consideration for certain releases and indemnities". Recital (F) stated that it was intended that, on execution of the DORA, ETJL would as soon as practicable transfer the trust assets to the new trustee. Clause 1 defined "the Indemnified Persons" so as to include not only ETJL but all companies in the same group and their respective officers and employees and their respective heirs, successors, personal representatives and estates. By clause 4, ETJL acknowledged that "reasonable security, inter alia in the form of the releases and indemnities herein contained, has been provided" to it. Clause 5 contains a covenant by the new trustee to "release and indemnify and save harmless the Indemnified Persons" against all claims against them in connection with the trust, whether or not enforceable in law. Clause 5 went on to provide that the indemnity was restricted to those liabilities as regards which ETJL would have been entitled to reimbursement or payment out of the trust fund and that the new trustee's liability was limited to the trust assets in its possession or control. The new trustee agreed to procure an equivalent indemnity from any beneficiary or new trustee to whom any capital sum was to be transferred. The new trustee also covenanted to keep £2.5m in a separate account to be used in the payment of existing trust liabilities. Clause 7 provided that the indemnity was valid for ten years for all claims other than taxation.

224. The key differences between the indemnity provided by the DORA and ETJL's equitable proprietary interest in the trust assets are that the latter, but not the former, gave ETJL direct access to the trust assets, gave it priority over the claims of the new trustee and any subsequent trustees, and was unlimited in time. The indemnity under the DORA was a covenant given by the new trustee, with its liability restricted to the trust assets in its possession or control. The language of limitation in the DORA is similar to that of article 32(1)(a), which was adopted at much the same time as the DORA was made. Consistently with the decision of the Board in *Investec 1* in relation at article 32 of the TJL, recovery by ETJL would be limited by the state of the new trustee's account when a claim under the DORA was made. There is no incompatibility between the contractual indemnity and the equitable proprietary interest. If it was intended that ETJL should waive valuable rights, superior as regards priority, the extent of recovery, and duration to the contractual rights conferred by the DORA, the expectation would be that it would do so in clear, express terms. We can see no basis, on any of the well-established bases for the implication of terms, for an implied waiver of such rights.

225. The appellants' final submission on Jersey law made or adopted in their written cases was that, if the Board should decide that a former trustee has a continuing proprietary interest in the trust assets ranking on a "first-in-time" basis, it should hold that the Royal Court has a wide supervisory jurisdiction which can enable it to fashion a pari passu scheme of distribution, in which former and successor trustees, and all creditors (if any) claiming through them, would be treated equally.

226. The appellants relied on two aspects of the Royal Court's jurisdiction. First, they submitted that it retains jurisdiction under the customary law of Désastre, existing alongside the statutory insolvency regime. The customary law of Désastre was, they submitted, developed as a response to the need to protect creditors and to ensure equality between them, subject only to preferential claims. In *In re Hickman* [2009] JRC 40, the Royal Court used its customary law jurisdiction to make orders in relation to an insolvent deceased's estate, so as to achieve equality among creditors.

227. We do not consider that the customary law of Désastre is of any assistance to the appellants. As we have earlier said with reference to pari passu distribution more generally, the customary law is concerned with the distribution of available assets among unsecured creditors. We were shown no judicial or academic authority to suggest that it could have any application to present or former trustees who are not creditors but who are entitled to proprietary interests in the trust assets.

228. Second, the appellants rely on the Royal Court's supervisory jurisdiction as regards the administration of trusts, which it submits is more far-reaching than the

English court's equivalent jurisdiction. They submitted that the Royal Court's jurisdiction permitted it to refuse to allow ETJL to enforce its proprietary rights except on condition that the proprietary interests stemming from the indemnity claims of successor trustees were treated on a pari passu basis. The Board was shown no authority which supported the improbable proposition that the Royal Court's customary jurisdiction would permit it to abrogate or materially alter vested property rights.

229. We would accordingly reject this appeal to the supervisory jurisdiction of the Royal Court.

230. Finally, there was discussion in the course of oral argument that the effect of article 32(1) was to pool trust assets for the purpose of meeting the claims of "trust creditors", which should accordingly be dealt with on a pari passu basis. However, as the Board held in *Investec 1*, article 32 does not confer on "trust creditors" any direct right against the trust assets. Their claims continue to be against the trustee who incurred the liability (either as trustee, in the case of liabilities to which article 32(1)(a) applies, or personally, in the case of liabilities to which article 32(1)(b) applies) and, in accordance with the English law principles discussed above, both categories of "trust creditors" are entitled only to be subrogated to that trustee's proprietary interest in the trust assets generated by its right of indemnity.

231. In their written submissions following the hearing, the appellants expressly disavowed any such pooling of assets. They did, however, submit that no trustee has a proprietary interest in a separately defined part of the assets but rather the rights of all the trustees were against the whole pool of assets from time to time. It has not, however, been suggested by the respondents that any trustee did, by virtue of its right of indemnity, have a proprietary interest in any separately defined part of the trust assets. As the appellants accepted in their written submissions, whether one trustee's interest in the trust assets has priority depends on the central issues in the appeals.

232. We therefore conclude that the principles of English law discussed above are fully applicable in the case of trusts governed by Jersey law and are not inconsistent with, or modified by, Jersey customary law or legislation.

The recoverable costs issue

233. As with the Ironzar II Trust, the Ironzar III Trust became "insolvent" in the sense that its assets were insufficient to meet in full all the liabilities incurred by its successive trustees in the proper administration of the trust. Directions were given for

claims against the trust assets to be proved and, as a former trustee, ETJL made a claim under its right of indemnity, and established its right to a sum slightly in excess of £90,000. Its untaxed costs of proving its claim are estimated at £247,000.

234. ETJL claimed to be entitled to recover those costs, subject to taxation, under its trustee's right of indemnity. In a judgment given on 10 September 2018, Commissioner Clyde-Smith rejected the claim but, in its judgment dated 28 June 2019, the Court of Appeal of Jersey allowed ETJL's appeal. For the reasons given below, we consider that it was right to do so.

235. It is well established that a trustee's right of indemnity extends to costs incurred in proceedings brought by or against a trustee in its capacity as trustee, provided only that there is no misconduct on the part of the trustee: see *In re Spurling's Will Trusts* [1966] 1 WLR 920, *Armitage v Nurse* [1998] Ch 241. There is no basis for suggesting that this principle does not apply to the costs of proceedings by a trustee to establish a right to indemnity in respect of particular liabilities. Nor is there any basis, given our conclusion on the survival of a former trustee's right of indemnity, for suggesting that it does not extend to such costs incurred after the replacement of a trustee.

236. In principle, therefore, ETJL is entitled to recover its costs through its right of indemnity. The Commissioner was inclined to accept that this was the case, describing it as supported by "powerful arguments" and referring to the decision of the Grand Court of the Cayman Islands (Smellie CJ) in *ATC (Cayman) Ltd v Rothschild Trust Cayman Ltd* (2012) 14 ITELR 523. However, he considered that this was not applicable in the case of an "insolvent" trust, given that he had decided in his main judgment that ETJL as a former trustee did not have priority over the claims of others and that a pari passu regime applied in the case of an insolvent trust. He held that, by analogy with the rule applicable to creditors in a Désastre (under article 30(2) of the Bankruptcy (Désastre) (Jersey) Law 1990), each creditor of an "insolvent" trust should bear the costs of proving its claim, subject to the court's discretion in any given case.

237. We agree with the Court of Appeal that no analogy can properly be made with the law applicable to Désastre, not only because it is statutory law which does not apply to trusts but also because, in proving its claim against a trust fund, a trustee or former trustee is not proving a claim as a creditor but is establishing the quantum of its proprietary interest in the fund. Like the Court of Appeal, we see no reason to qualify the trustee's right of indemnity, expressed in article 26(2) of the TJL as being in respect of "all expenses and liabilities reasonably incurred in connection with the trust".

LORD BRIGGS (with whom Lord Reed and Lady Rose agree, and Lady Arden agrees in part):

238. Subject to one important point, I agree with all the conclusions and reasoning in the joint opinion of Lord Richards and Sir Nicholas Patten ("the Joint Opinion"). I have unfortunately been unable to agree with them that, as between two or more trustees of the same Jersey trust, their proprietary rights as against the fund, which we call their liens, should rank for priority in the order in which they were appointed trustees. In my judgment, as against a fund which is insufficient to pay them all in full, they should rank pari passu. I acknowledge, as they do, that this question is not covered by any binding or even persuasive authority, anywhere in the common law world, so that (albeit strictly only for the purposes of the law of Jersey) the Board is called upon to decide it for the first time.

239. My reading of the Joint Opinion suggests that its authors would decide this question on the basis that (i) as between equitable proprietary interests, the general or default rule is that the first in time should prevail and (ii) that while the Board could decide otherwise, preferring some other rule such as *pari passu*, there are not sufficient grounds for doing so. I agree with (i). Prior to this appeal I would probably have agreed with (ii) as well. But the impressive arguments, coupled with lengthy ensuing debate and reflection, have caused me to change my mind. In my view there are sufficiently powerful reasons, of justice, equity, fairness and common sense for preferring a *pari passu* rule of priority to enable, indeed to require, the Board to prefer it to the first in time default rule.

240. The Joint Opinion proposes first in time as the general and only priority rule between trustees with entitlements by way of lien against an inadequate fund (i.e. a fund which is insufficient to pay all lien entitlements in full), as a matter both of English and Jersey trust law. It would apply therefore not only (as in the present case) where trustees are appointed and act in strict succession, with one (or one group) retiring before the successors begin to act, but also where trustees are appointed in quick succession and thereafter all act together, throughout the life of the trust. It would apply, for example, where the second to be appointed was the first to retire, and where all the relevant liabilities of the second appointee were incurred before the first appointee began to act, or to incur any liabilities. It would also mean that where two trustees, appointed one after the other, incurred joint liabilities but did not exonerate themselves by procuring that payment was made direct from the fund to the creditor before they left office, then the first to be appointed would be entitled to the inadequate fund by way of indemnity, to the exclusion of the other.

241. In recognising or fashioning a rule of priority between trustees' liens it is worth reflecting upon the function which the lien typically performs in the day to day operation of a trust, both in England and in Jersey. As Lord Richards and Sir Nicholas Patten have explained, the lien works by way of both exoneration and indemnity. For as long as trustees are in office it will operate for their benefit mainly by exoneration. Trustees will incur liabilities from time to time, both jointly and separately, and discharge them by paying the creditor direct from the fund which they control. In England they thereby relieve themselves of a genuine personal liability (unless they have contracted 'as trustee only'). In Jersey they incur no such personal liability at all (save to creditors who do not know that they are trustees).

242. Exoneration is thus a bit of a misnomer in Jersey. But it is the mechanism by which trust creditors usually get paid. It is also a bit of a misnomer to call them creditors at all. Just as the trustee has no personal claim against anyone for exoneration or indemnity, nor a fortiori does the supposed creditor. His only claim is to be subrogated to the trustee's lien, that is, to the lien or liens of the trustee or trustees who contracted with the creditor on behalf of, or rather for the benefit of, the trust.

243. Turning to indemnity, trustees in office may occasionally voluntarily discharge a liability from their own personal funds, such as the cost of a train fare from London to York, or a taxi fare from St Helier to Gorey, to visit a beneficiary, if they did not take with them the trust debit card. Then they will be entitled to reimburse themselves for the expense personally incurred and paid. But indemnity takes centre stage, at least in England, once the trustee leaves office and relinquishes control of the trust fund. If he is faced with a liability falling due after retirement he will probably have to pay it personally and then seek indemnity by the exercise of his lien. But in Jersey the retired trustee may simply leave it to the creditor to enforce his lien by way of subrogation, since the trustee will usually have no personal liability to force him to put his hand into his own pocket.

244. Nonetheless even the retired Jersey trustee may have no alternative than to incur personal expense, for which he may later have to seek indemnity from the fund. He may have to defend legal proceedings at great expense, and therefore contract and pay up front for legal services, which the lawyers may understandably be reluctant to provide on credit. The retired trustee may also have to bring legal proceedings against the successor trustees, if they either challenge his lien, or threaten to distribute or otherwise diminish the trust fund in a way which would impact upon its effectiveness.

245. In all these modes of the operation of the trustees' equitable lien, both in England and Jersey, it serves two main purposes, neither of which is necessarily concerned with the adequacy or otherwise of the trust fund. The first purpose is to

ensure that, as against the beneficiaries, the trustees are in their performance of their fiduciary duties of single-minded loyalty to them, relieved of personal expense and liability in priority to the beneficiaries' entitlements. The beneficiaries cannot for example together decide to distribute the fund to themselves, leaving the trustees unpaid. In short, as the authorities examined in the Joint Opinion make clear, the lien gives the trustees clear priority over the beneficial interests of the beneficiaries. The second purpose, of much greater importance in Jersey and perhaps Australia than in England, is to ensure that services can be obtained (including loans) for the better operation of the trust, with a normative basis (though not necessarily a secure basis) for the creditors getting paid, or for the trustees getting reimbursed if the supplier insists on being paid up front.

246. But in none of the authorities is there any perception that it is any part of the purposes of the lien to confer priority upon one trustee (or group of trustees or creditors) over another where, even without further distribution to beneficiaries, the fund becomes inadequate to pay them all in full. The absence of any such perception in any of the authorities before these appeals is striking. There is a marked contrast in this respect between the trustee's lien and other forms of what may loosely be called equitable proprietary interest by way of security. A fixed equitable charge is (subject to any relevant requirement for notice or registration) plainly designed to give the holder priority over any later charge or equitable interest, and prevents any dealing with the subject property by its owner, at least without the chargee's consent. It is common to find successive fixed charges establishing a clearly understood 'waterfall' of priority as between each other. A floating charge gives priority only over later floating charges, and permits later fixed charges to be granted over the subject property until crystallisation, with priority over the floating charge.

247. There are some similarities, but important differences, between each of these well-known forms of proprietary interest and the trustee's lien. It is least like a fixed charge because, until there is at least a threat of inadequacy of the fund, the lien of a retired trustee does not in any way inhibit the current trustees from exercising their own lien, paying unsecured creditors or even from making distributions and other authorised payments (e.g. paying up front for services) out of the trust fund. Furthermore the recipient of any authorised payment out of the fund takes free of the liens of retired and current trustees, even if the recipient has notice of them.

248. In those respects the trustee's lien more closely resembles a corporate floating charge, because it permits any later authorised dealings with the trust fund, and attaches as a proprietary interest to whatever property constitutes the trust fund from time to time. But it differs from a floating charge in at least two important respects. First, it appears to have no clear or fixed means or moment of crystallisation, the

operation of which is crucial to the efficacy of a floating charge as a form of security. Secondly the lien appears to constitute an immediate proprietary interest in the fund, whereas the floating charge does not do so until crystallisation, whereupon it takes on most of the characteristics of a fixed charge.

249. There is a further fundamental distinction between the trustee's lien and any form of legal or equitable security. There is, as the Joint Opinion has so tellingly explained, no primary liability of anyone to the trustee for which the lien stands as security. It is a means of payment, not a security for payment. The lien is like a security (as compared with a plain beneficial interest) only in the sense that the amount which may be obtained by its exercise is referable to an exterior state of account between the trustee and the trust estate, rather than being some kind of share in the fund which may go up and down in value with the growth or shrinkage of the fund. In this respect the trustee's equitable lien is further removed from conventional security than a solicitor's equitable lien, which is indeed security only for a specific contractual payment obligation of the client: see *Edmondson*. If there is no such obligation, there is no solicitor's equitable lien.

250. These differences between the trustee's lien and any other kind of recognised equitable interest do not of themselves point immediately to some priority rule as being more or less appropriate for recognition than the first in time rule. They merely demonstrate that this type of lien has no close parallel in the world of equitable proprietary interests from which a priority rule may be drawn by analogy; that it is truly sui generis. In *Amarind*, Bell, Gageler and Nettle JJ summed this up well in this passage already cited by the majority at para. (83):

> "it is said that the trustee has an equitable charge or lien over the trust assets. It is not, however, a charge or lien comparable to a synallagmatic security interest over property of another. It arises endogenously as an incident of the office of trustee in respect of the trust assets".

The trustee's lien is therefore worthy of a carefully worked-out priority rule of its own. That requires a faithful dedication to the fulfilment of the purposes for which the law confers this lien, a recognition of the nature of the fiduciary office of which it is an incident, a reflective consideration of its likely effects over the whole range of fact-situations in which it may be applied, not just the very unusual facts of these two appeals, and a stand-back appreciation of which, as between potential competitors, does better justice or equity.

251. Before doing that directly, it is worth noting the essentially pragmatic and flexible approach which equity takes to the resolution of problems of this kind, in resolving priority between proprietary claims or interests other than liens or charges. A telling example is the way in which equity has come to deal with the competing proprietary claims of contributors to a mixed fund which has become inadequate to repay them all in full. Originally equity adopted a 'first in first out' rule, as a relatively crude forensic tool for ascertaining to whom the money remaining in the fund actually belonged: see *Clayton's Case* (1816) 1 Mer 572. Despite its language it has precisely the opposite effect to the first in time rule, because it tends to appropriate the fund to the latest contributors, leaving the earliest contributors to receive nothing, on the basis that their contributions had already been lost or misappropriated before the balloon went up. Later, in *In re Hallett's Estate* (1880) 13 Ch D 696 the first in first out rule was held not to be capable of just application as between trust money and the trustee's own money in a mixed fund. The trustee was presumed to take his own money out first. The rule was further distinguished in the case of contributions to a non-charitable benevolent fund for purposes which had failed, in favour of pari passu distribution, on the basis that the first in first out rule was inconsistent with the contributors' presumed intentions: see *In re British Red Cross Balkan Fund* [1914] 2 Ch 419, and *In re Hobourn Aero Components Ltd's Air Raid Distress Fund* [1946] Ch 86 and [1946] Ch 194. Pari passu distribution was famously ordered in relation to that part of the remaining funds of an ultra vires banking business into which no contributors could trace in *Sinclair v Brougham* [1914] AC 398. First in first out was described in *Re Diplock* [1948] Ch 465, 553 by Lord Greene MR as "really a rule of convenience based upon so-called presumed intention".

252. This progression of equitable thinking was reviewed in detail by the Court of Appeal in *Vaughan v Barlow Clowes International Ltd* [1991] EWCA Civ 11, [1992] 4 All ER 22. Pari passu was applied to the distribution to investors of a deficient investment trust fund in preference to first in first out. Both Woolf and Leggatt LJJ cited with approval this passage from the judgment of Judge Learned Hand in *Re Walter J Schmidt & Co* (1923) 298 Fed 314, 316:

> "The rule in Clayton's case is to allocate the payments upon an account. Some rule had to be adopted, and though any presumption of intent was a fiction, priority in time was the most natural basis of allocation. It has no relevancy whatever to a case like this. Here two people are jointly interested in a fund held for them by a common trustee. There is no reason in law or justice why his depredations upon the fund should not be borne equally between them. To throw all the loss upon one, through the mere chance of his being earlier in time, is irrational and arbitrary, and is equally a fiction as the

> rule in Clayton's case, supra. When the law adopts a fiction, it is, or at least it should be, for some purpose of justice. To adopt it here is to apportion a common misfortune through a test which has no relation whatever to the justice of the case."

The Court of Appeal concluded that first in first out was no more than a rule of convenience, easily displaced by contrary intention and liable to give way to a preferable alternative if first in first out produced injustice: see e.g. per Woolf LJ at p. 39.

253. I acknowledge, as the authors of the Joint Opinion and Lady Arden all point out, that these cases are not about liens, security or even competition between separate and distinct proprietary interests. But they all concern equity's approach to the ranking of what are in substance proprietary claims, that is claims to be entitled to share in a fund, rather than personal claims in contract, debt or tort. They assist not because of the occasions when a pari passu solution has actually been adopted, no doubt on very different facts from the present, but because they display equity's flexible and pragmatic approach to the task of devising an appropriate solution where none has been identified before.

254. It is easy to see why the first in time rule probably evolved from a perception that, as between the holders of successive charges who compete to obtain them at arms' length from each other as security for payment of a loan or debt owed by the chargor, it fairly reflected the presumed intention of all concerned, and generally did substantive justice. But co-trustees of a single trust fund seem to me to come into an altogether different category, even if, as is frequently the case, they are not all appointed simultaneously. I agree that their liens are of course all equal, as the Joint Opinion says. But I do not consider it appropriate to describe them as being in any sense in competition with each other. A competition for priority between trustees' liens seems to me to be alien to the very nature of the office to which the lien is an incident. I cannot imagine for example why five trustees appointed on successive working days during a single week to carry out their duties together should be presumed to think it just or fair that, in the unlikely event that their fund later became insufficient to pay all their liabilities and expenses in full, then their respective dates of appointment should govern the distribution of the residue of the fund, such that the trustee appointed on a Monday should get paid in full , but the trustee (with perhaps a much larger claim) who happened to have been appointed on a Friday should get nothing. In short, why should fiduciaries who have worked as such together in a common enterprise, for the benefit of others rather than themselves, not be paid pari passu from a deficient fund? Their respective dates of appointment would be mere

happenstance, having no connection of any kind with equity or justice. It would be no more relevant than the dates when different contributors paid in to a non-charitable benevolent fund.

255. The point may be tested this way. Assume that the same five trustees were all appointed together by the same deed at the same time. No-one could doubt that they would all share in recoveries under their liens pari passu, regardless which of them actually signed the deed first. But suppose one of them was out of town on the day that the others all signed the deed and were appointed, only being himself appointed on his return on the following day. It would be absurd to think that any of them would regard their priority in the unexpected common misfortune that the fund later proved deficient as being any different. And the reason why not is nothing to do with the difference between a day, a week, a month, or even a year between their respective appointments, but because they all undertook as loyal and unselfish fiduciaries to perform the identical duties of a common office for the furtherance of a common enterprise, in which they were in no sense to be competitors. The notion that, in the event of an insufficiency in the fund they would share wholly unequally in the residue in the exercise of their liens, could not but be detrimental to their sense of common purpose as fiduciaries, in administering the fund for the benefit of the beneficiaries. The insufficiency of the fund to meet in full the value of their respective liens would be, to all of them, a common misfortune, in which their natural expectation would be to share the pain equally.

256. While I agree with the statement in the Joint Opinion that trustees do not share a single common lien, I respectfully disagree with the view that the trust of which they are all trustees has no relevant institutional or enduring quality of its own, or that to recognise any such enduring quality is wrongly to prefer economic over legal analysis. While a trust does not, even in Jersey, have a separate legal personality of its own, it is in my view relevantly to be regarded as a form of continuing institution or scheme under which a fluctuating body of assets (the fund) is administered by fiduciaries who may change over time, for the benefit of beneficiaries who may likewise change, subject to a set of rules contained in the trust deed and the general law, which may also change, by amendment of the trust deed, by judicial variation, by legislation or even by the ‘export’ of the trust into a different legal jurisdiction. Despite all these potential changes, the trust itself has an enduring character which is not dependent upon separate legal personality, any more than is a partnership or unincorporated association.

257. That perception that a trust, like a company, has an enduring quality of its own is central to my view that the insufficiency of the fund to meet all the trustees’ lien-based claims in full is a common misfortune for which a pari passu sharing of the

residue is the fairest, or least worst, general rule. To the extent that a trustee is liable to the trust fund for a breach of trust (which may or may not have contributed directly to the inadequacy of the fund), his lien is reduced accordingly since, as the Joint Opinion makes clear at para 61, a trustee's gross indemnity claim is reduced or eliminated by amounts for which he is accountable. The “trust creditor’s” claim by way of subrogation is in this respect no better than the trustee’s claim. It is the perception that the trustees are all (even if at different times) trustees of the same trust that makes the insufficiency of the fund to cover the net liability of the fund to the trustees a common misfortune. I have described above why this is the appropriate description of trustees who all serve together even if appointed on different dates. Whether it is equally applicable to trustees who serve on the basis of rolling or strict succession deserves closer analysis. By ‘rolling’ succession I mean where they are each appointed and retire on different dates, but without a clean break between the retirement of one group and the appointment of another, which I have already labelled ‘strict succession’. By ‘retire’ I include of course their removal, either by a protector, by the court or by any other lawful means.

258. It is convenient to look at rolling succession first. A trust may enjoy the services of ten trustees over fifty years, with never less than (say) five in office together at any one time. Save where (unusually) the trust deed prescribes a fixed or maximum period of service, it will be pure happenstance whether they retire in the same order as they were appointed. Many or all of trustees one to five will have served together with one or more of trustees six to ten, and thereby literally have worked together in a common enterprise. Their respective dates of appointment will usually have little to do with whether they have worked together in that sense. But all of them may well regard themselves as one of the same class of fiduciaries who worked for the furtherance of that trust, and whether they literally worked side by side may matter little in their perception of whether they all served that common enterprise. As I shall acknowledge in relation to strict succession, those who retired before the affairs of the trust fell upon hard times may well think it unfair that their continuing lien (if still relevant to them) should be adversely affected by what happened after they relinquished any share in the control of the fund and its fortunes, but this will have nothing at all to do with their respective dates of appointment. It may be that after the retirement of a particular trustee, all those who continued in office were appointed before he was. Under a first in time rule, the stayers would all have priority for satisfying their liens over the lien of the early retiree.

259. It follows in my view that nothing in the typical characteristics of a rolling succession suggests that a first in time rule would work better equity or justice, or even rational common sense, than a pari passu rule, if that does the best equity as between trustees who all work together after appointment on different dates, as I think it clearly does. Rolling succession is probably overwhelmingly the most common type of

trustee service pattern historically, and still is in England, even though the facts of the present appeals fall into the strict succession category.

260. Cases (like the present) of strict succession require a more earnest pause for thought. I will use for convenience the example of a trust in which trustees A and B were appointed on slightly different dates but to work together, being both removed at the same time and then replaced by trustees C and D, again on slightly different dates, to work together. There would be a clean break in the administration of the trust as between A and B, followed by C and D. I have already explained why, as between A and B (and for that matter as between C and D) their different dates of appointment could not sensibly be regarded as a just or equitable basis for prioritising one lien over another. They would be working together as fiduciaries in a common enterprise, and equal victims of a common misfortune.

261. But A and B might well think it most unfair in some circumstances that they should even have to share, in the enforcement of their liens, with C and D, with whom they had never worked together, and during whose period of office the trust fund had fallen on hard times. Mr Simon Taube KC for I&B made a vigorous submission about the iniquity of that misfortune for his clients. Why should I&B have to take the consequences of the administration of a fund of which they had relinquished control, he asked. And why should his clients (A and B in my example) have to share in recoveries against lien-based claims of their successors arising from costs which they incurred in resisting enforcement by his clients of their liens?

262. There are several answers to that eloquently expressed sense of outrage which arise from the particular facts of this case. In particular the main apparent cause of the 'hard times' experienced by the TDT was the huge liabilities undertaken by I&B to the BVI companies, from which, in the event, the TDT was almost miraculously rescued by the March 2019 assignment to their successors F&B. Secondly the litigation costs undertaken by F&B in resisting the lien-based claims of I&B were either incurred with court approval on a *Beddoe* application (*In re Beddoe* [1893] 1 Ch 547) or, if not, may have been incurred at F&B's own risk. More generally, and of greater relevance in the search for an appropriate general rule of priority, it will be happenstance whether the misfortunes which lead to a trust fund becoming inadequate to meet all trustees' claims in full owe their causes to events before or after the change of control between trustees acting in strict succession. Given that any liability of a trustee to account to the fund for breach of trust will already have been netted off when valuing his lien, a further investigation into whose conduct sowed the seeds of the problems that later overwhelmed the fund is likely to cause dissent and litigation, risking a further diminution in value of the fund left to satisfy the creditors. Of course the fund may be diminished after the retirement of A and B, by lawful payments, distributions and by

the exercise of their own liens by their successors, because of the lack of any clear basis for the crystallisation of the liens of their predecessors. By contrast it may well be that distributions to beneficiaries by C and D after the insufficiency becomes apparent will amount to breaches of trust by them (with a corresponding liability to account) since the liens of A and B are equitable proprietary rights with clear priority over the interests of the beneficiaries.

263. It was submitted that a first in time priority rule can be supported by the ability of later-appointed trustees to make their own choice whether or not to accept office, and to bargain with the settlor or with the beneficiaries for added security if concerned about the adequacy of their lien. But this assumes that the extent of outstanding future and contingent liabilities covered by A and B's liens is capable of being identified, let alone quantified, at the time when C and D are invited to take office. And the contrary argument, that A and B are in any event entitled to retain on retirement a sufficient part of the fund to meet such outstanding liabilities, under Article 43A(1) of the Jersey Trust Law, and are more likely than C and D to know what they might be, seems to me to carry equal if not greater weight.

264. The facts of the Jersey appeal are a case in point. EJTL was replaced by its successor Volaw in 2006. The liability which threatened the adequacy of the trust was first intimated to EJTL in 2012, and a potential claim under its lien notified to Volaw in April 2013. The 'hard times' were, as between EJTL and Volaw, entirely attributable to EJTL, (even if they did not involve any breach of trust) and Volaw can have had no inkling of them when it agreed to assume office.

265. The result of this analysis is that I am not persuaded, even in the case of a strict succession situation, that a first in time rule offers any more just or equitable priority rule than pari passu and the latter appears much more appropriate in the case of trustees all serving together, and where serving under a rolling succession.

266. I note that the Joint Opinion describes a pari passu general rule of priority between trustees as lying uneasily alongside the right of a retiring trustee to seek reasonable security for outstanding trust liabilities. While this point has real force as supporting a rule that priority should be determined by date of retirement (with which I deal below) there is no principled connection with that right of a retiring trustee and a first in time of appointment rule of priority. This is because it is by no means inevitable that trustees will retire in the same order as they were appointed. It may be a common feature of the history of Jersey business trusts, but the present search is for a general rule which applies to all trusts.

267. The apparent binary choice between first in time and pari passu as the appropriate general priority rule is only the consequence of there having been no other candidate put forward in the parties' submissions. It is worth briefly pausing to consider whether there are any others. One might be priority in the order in which trustees' liabilities are incurred. But that has no obvious correlation with justice or equity and would be formidably difficult and expensive to administer. Another might be that a trustee's lien crystallises (and thereby achieves priority over the liens of successor trustees) upon retirement. That would meet the submissions of Mr Taube in relation to strict succession, but would hardly work in the everyday world. It would mean that successor trustees could not make payments or distributions, or exercise their own lien-based rights until the retired trustee's lien-based claims had been settled in full. And it is hard to see how it would accommodate future or contingent trustee liabilities. Crystallisation is something which usually occurs on actual or threatened insolvency (here inadequacy) but that is likely to be unusual in the context of the transfer of control of a trust to new trustees. Short of crystallisation, priority might in theory be based on dates of retirement, but this has little more inherent logic or equity in it than first in time, and much less than pari passu. Furthermore it could provoke an unseemly rush for the exit by the trustees as the hard times approached, motivated by a wholly inappropriate desire to collect more from the wreckage than their colleagues.

268. A final alternative may be that the question of priority depends upon the court's discretion, so as to be fashioned to the justice of the infinitely variable particular facts of each case. But the uncertainties inherent in such a conclusion seem to me to present an insuperable obstacle to its adoption. It would mean that in every case in which a relevant insufficiency in the trust fund occurred the parties would have to go to court for directions, committing an already inadequate fund to the cost of what may (as here) be contentious and therefore expensive proceedings. Although in abstract theory a lien of this kind is, in the last resort, only a right to seek the court's intervention in the administration of the fund, its recognition as a proprietary interest is based upon a reasonable degree of certainty as to how the court will enforce it, in the same way in which a purchaser's proprietary interest in land is based upon the expectation of being able to obtain specific performance. To treat the question of priority as dependent purely upon discretion would be to risk downgrading the lien from a proprietary interest into a mere equity.

269. That said, I would not entirely rule out the possibility that exceptional circumstances might arise in which the strict application of a pari passu rule of priority might work such obvious inequity that an exceptional discretion to depart from it might be justified. As Lieutenant Bailiff Hazel Marshall QC put it at paragraph 216 of her first instance judgment in the Guernsey appeal, it would have to be something wholly exceptional which would otherwise "shock the conscience of the court". In this

context it needs to be borne in mind again that a complaint that a particular alleged trustee expense ought not to rank pari passu because it should not have been incurred at all requires no discretionary departure from the rule itself. It will fall to be addressed by disallowing the relevant item in the trustee's account.

270. No such exceptional circumstances are demonstrated by the present appeals. Mr Taube's main complaint was that litigation expenses incurred by trustees in succession to his client in an unsuccessful challenge to its conduct as trustee ought not to be allowed to compete with his client's claim. But those expenses were either incurred with court approval on a *Beddoe* application or at the successor trustee's risk as to recoverability if not. Resolution of that issue does not arise on this appeal. Nor does its resolution require a discretionary departure from a pari passu priority rule.

271. It is also instructive to see what if any priority applies as between multiple (including successive) occupants of other fiduciary offices. The immediate parallel is company directors. They are just treated as unsecured creditors in a liquidation, having no lien or other proprietary claim for their expenses and proper liabilities. They therefore share pari passu between themselves. Liquidators and administrators have a special priority as a class at the top of the insolvency waterfall, but no priority inter se. If there are two or more such officeholders working together or in succession, they share an inadequate fund pari passu: see Totty, Moss and Segal at D1-60 and *Re Salters Hall School Ltd* [1998] 1 BCLC 503. While it may be said that these consequences are all part of the statutory insolvency code in which, as between those with equal claims, *pari passu* reigns supreme, it needs to be borne in mind that the code emerged from the general law and in particular from the equitable maxim that equality is equity.

272. Solicitors also enjoy an equitable lien over recoveries made from litigation in which they are retained. It has recently been likened to a charge, in *Edmondson*. But where successively retained solicitors both contribute to the generation of the fruits of the litigation it is the second to be retained, not the first, who enjoys priority if the fruits are insufficient: see *In re Wadsworth* (1886) 34 Ch D. 155.This is the exact opposite of a first in time rule, yet their liens constitute proprietary equitable interests in the fund, like trustees' liens. This order of priority between solicitors no doubt has its own justification, but it demonstrates that there is no history of applying a first in time rule to equitable liens. The true priority (if any) depends upon the nature of the right, the nature of the office to which it is an incident, the presumed intention of the parties and the justice or otherwise of the consequences of the chosen rule.

273. It is therefore no answer to these comparisons just to say that there is a simple and sharp divide between those with proprietary claims, between whom first in time

prevails, and those of mere creditors without such claims, who generally share pari passu. The increasing use of a pari passu rule in the resolution of claims to share in a deficient fund (described above) proves the absence of such a divide, because such claims are by their nature in substance proprietary. Nor is it an answer to say that there is a clear divide between the claims of secured creditors under a charge and other proprietary claims. The trustee's lien is neither a straightforward charge of any recognisable kind, nor is it essentially a form of security. Nor are the trustees or the 'trust creditors' who stand behind them truly creditors in any ordinary sense. Although they have a claim to payment, there is no debtor who owes them any personal liability to pay.

274. I was originally in sympathy with the view expressed in the Joint Opinion that the debate about the priority of trustees' liens inter se is not brightly illuminated by the prospect that each trustee may have a group of 'trust creditors' standing behind him, whose only recourse at least in Jersey is against the fund by way of subrogation to the trustees' lien. This is because it is now settled that those creditors can be in no better position as against the fund than the trustee or trustees through whose lien they have to claim by subrogation, so that they are as vulnerable as the trustee is to the state of account between that trustee and the trust estate. As the facts have turned out, the Board has not in this case been called upon to adjudicate as between trustees and 'their' creditors, or between the trust creditors of one trustee and those of another, for the reasons given in the Joint Opinion.

275. But having read in draft the judgment of Lady Arden I do not consider that the prospect of there being such trust creditors standing behind the trustee with recourse (in Jersey) only against the fund is wholly irrelevant to the resolution of the priority issue as between the trustees themselves. Part of the purpose of the trustees' lien is to provide a mechanism by which trust creditors get paid: see per Allsop CJ in *Jones v Matrix* at para 48:

> "The right of the trustee to reach into the trust assets is not a personal right devoid of connection with the purposes and working of the trust; it inheres in, and arises out of, the trust relationship that exists for a purpose – to pay the creditors and thus to exonerate the trustee. It is without doubt a right of the trustee (and in that sense personal), but one that is constrained in its content by its purpose – the payment of trust creditors."

276. Viewed from the perspective of the trust creditors, it would seem even more inequitable and unbusinesslike for their priority to depend upon the respective dates

of appointment of the trustees with whom they happened to contract for the provision of services for the use and benefit of the trust. By contrast with those thinking of giving credit to a company, those thinking of extending credit to trusts do not generally have access to published trust accounts. It is bad enough (and the subject of considerable criticism in *Investec 1*) that trust creditors are exposed to the unknowable state of account between the trustee with whom they deal and the trust. But that is no reason why there should now be formulated a rule of priority which, if it is to be first in time, exposes trust creditors to the further uncertainty (from their perspective) of the different times of appointment of the trustees, as a basis for allocating priority as between them. Their natural expectation, as unsecured creditors, would be that all trust creditors should share pari passu the consequences of the inadequacy of the fund, just as they would share the consequences of having given credit to an insolvent company or a bankrupt individual. And, as Lady Arden says, the relative date of appointment of the particular trustee with whom the creditor dealt when giving credit would be a mere happenstance. I would add that it would be a date of which the creditor would (unlike fellow trustees) be likely to be wholly unaware.

277. For the above reasons I would conclude that considerations of justice, fairness, equity and common sense strongly militate in favour of the recognition between trustees of a pari passu general rule for enforcement between them of their liens over an inadequate trust fund. By contrast a first in time of appointment rule would in this context be unconnected with any considerations of justice or equity. It would also in my respectful view be inappropriate between fiduciaries loyally serving the interests of their beneficiaries in a continuing trust relationship, regardless whether they all serve together at the same time, because competition between them for unequal shares of the inadequate fund would be incompatible with their joint pursuit of a common cause. I do not mean that a pari passu rule will work perfect justice in every case. In many cases it will do no more than rough justice. But there is an inherent justice in equal division, or equal sharing in a common misfortune, which is captured in the equitable maxim equality is equity.

278. For completeness I would make the following additional points. First, my conclusion that pari passu is the appropriate general rule of priority as between trustees seeking to exercise their liens over a fund which is inadequate to satisfy them in full involves no taking away from them a previously enjoyed first in time priority, at the time when the fund becomes inadequate, or otherwise. In agreement on this point with Lady Arden, pari passu is the appropriate general rule of priority between them, from start to finish. Secondly, the existence of pari passu priority between trustees of a single fund in no way inhibits one or more of them from enforcing their lien in full, for as long as there is no doubt as to the sufficiency of the fund to satisfy them all in full. Each trustee retains their own lien for their own benefit, subject only to the claims of subrogation creditors as between whom and the trustee this appeal has not provided

an opportunity for an examination of priority. Thirdly, neither has this appeal provided an opportunity (still less submissions) as to the procedure by which pari passu priority may be enforced, when the fund becomes inadequate to satisfy all the liens in full. In many cases it may be achieved by consent, out of court, under the supervision of the current trustees. But it may in cases of doubt or dispute require the intervention of the court or even the administration of the fund by the court. Finally it is necessary also to leave open the question whether the general rule of pari passu priority might be displaced, in a particular case, by express provision to the contrary in the relevant trust instrument. These are all important questions, but they will have to be resolved upon another occasion.

LADY ARDEN:

My overall conclusion

279. For all the reasons given in this judgment, I consider that where the trust fund is insufficient, it is consistent with the principles of equity to hold that the first-in-time maxim does not apply to successive trustees' proprietary interests arising because of their right of indemnity in relation to an identical trust. I therefore disagree with Lord Richards and Sir Nicholas Patten on this Issue, called Issue (3) (and no other). These proprietary interests are equitable interests. Under the first- in-time maxim, as between equitable interests, where the equities are equal, the first-in-time prevails. Nonetheless, in my judgment it is inconsistent with equitable principle that the former trustee should have priority in that situation. Moreover, there is no logical purpose in establishing a priority date for expenses by reference to the appointment dates of trustees or at all. That date is mere happenstance. The first-in-time maxim will lead to the payment of creditors being unnecessarily delayed while the priority position is sorted out and disrupt trust administration and diminish the utility of the trust concept. The priority which trustees have for expenses is as against the beneficiaries, and not as against each other. Accordingly, former and current trustees in my judgment rank pari passu as regards the trust fund if it is insufficient to pay all the sums against which they are entitled to be indemnified.

Some general principles relating to the trustee's right of indemnity

280. I wish to start by paying tribute to the judgment of Lord Richards and Sir Nicholas Patten. Lord Stephens agrees with them. I pay tribute to Lord Briggs, with whom Lord Reed and Lady Rose and with whom I agree in part, below. I agree with much of what Lord Richards and Sir Nicholas have said, and their judgment will shorten my task in that regard. As explained, I agree with their conclusions save on the priority

to be accorded to a trustee's claims under his right of indemnity. In my judgment, where a trust fund is insufficient for the payment of all expenses due to trustees, equity does not give earlier trustees priority over later trustees for these expenses. I have decided to avoid the detailed citation of authority because, in my judgment, what is important is the principle. This is a case for a principles-based solution and not a rules-based one.

281. A trust is not, subject to the points which I make below in the Appendix about Jersey statute law, a separate legal entity and the trustee is personally liable for debts and other obligations incurred by him as trustee. Under Jersey statute law, as explained below, it appears that in disputes arising out of the non-payment of obligations incurred by the trustee, the claim is made against the trustee who incurred the liability in his capacity as trustee and not in his personal capacity. The court can order the current trustee to pay the expenses of his predecessors in office out of the trust fund, but, if there is no reasonable doubt about the propriety of these expenses, the current trustee generally has, by virtue of his office as trustee, authority to make payment of them without the need for the former trustee to obtain a court order. Trustees have by virtue of their office the right to be indemnified against liabilities that they properly incur while discharging their duties. There are various ways in which that right can be fulfilled but the ways with which this judgment is concerned are: (1) exoneration when the trustee requires the liability to be discharged out of the trust fund and not by himself; (2) reimbursement of the trustee where the trustee has for whatever reason himself paid the liability.

282. When a trustee vacates office, he may request the new trustee to give him a direct contractual undertaking of indemnity, or where appropriate, he can take reasonable security to pay or provide for liabilities actual or contingent which are or might be payable by him as trustee after he vacates office. Article 43A of the Jersey law confers on the trustee an express right to require reasonable security for all liabilities incurred as trustee. When I refer to "security" below, I am, unless otherwise stated, referring to collateral given in addition to the primary obligations which arise as a matter of law, and so the term would include the direct contractual undertaking and the provision of security as explained in the first sentence. If these rights do not fully satisfy liabilities that he has, the former trustee can request the current trustee to procure payment out of the trust fund, and if the current trustee does not do so, the court may, in addition to making an order for payment out of the trust fund against the current trustee as already explained, order a sale, or appoint a receiver. A creditor of the former trustee (in his capacity as such trustee) can stand in the shoes of the former trustee and take these steps in place of him. The former trustee can also monitor what his successor is doing and can ask the court to restrain him from any activity that he uncovers, and which would jeopardise his indemnity right, for example, a distribution to beneficiaries to enable them to discharge their debts.

Common ground

283. I agree with Lord Richards and Sir Nicholas that the right of indemnity results in the creation of an equitable interest in the trust fund. That interest ranks ahead of beneficiaries. Whether a trustee can create a security over the trust fund for a liability which ranks ahead of the right of indemnity has not been covered in the submissions and depends at least on the terms of the trust instrument. If security can be, and is, validly given for the expenses of the retiring trustee, then in my judgment, the court's power to direct how outstanding expenses of various trustees are to be paid does not include power to vary the terms of that security.

The flexibility of equity allows the creation of an interest which has priority for some purposes but not others

284. On these appeals, I adopt the analysis that the trustee's proprietary interest is inherently capable of allowing priority among trustees on some basis other than the date of their appointment. The flexibility of equity allows for the creation of an interest which has priority over one group, the beneficiaries, but, if the trust fund is insufficient to meet all the trust-related liabilities, then, in my judgment, the holders of the equitable interests representing the trustee's right of indemnity will as between themselves rank pari passu. (In this judgment I leave out of account security granted to third parties by a trustee.)

285. As a matter of legal theory, equitable interests are created to reflect the principles that equity applies. Equity has created a system of interests in property which parallel those which exist under the common law because this is one of the ways in which equity follows the law. But equitable principles can apply flexibly because the function of equity is as a supplementary system of law, making exceptions and additions to the common law where the courts consider it appropriate to do so. This means that, to apply an equitable principle in the way intended by equity, it is important to look beyond the equitable interests themselves and to identify the reason for the right reflected in the equitable interest.

Reasons for the trustee's right of indemnity

286. There are several reasons for equity granting a trustee a right of indemnity. First, it would be unfair if he did not have such a right. Second, it would discourage persons from acting as trustees if the right was not an integral part of their office. Third, it promotes efficient trust administration. Fourth, and perhaps most importantly, it prevents the beneficiaries of the trust benefitting from the trust fund

built up by trustees without ensuring that those trustees are paid first (see *In re Johnson*, *Shearman v Robinson* (1880) 15 Ch D 548, 552 per Jessel MR, *In re Evans* (1887) 34 Ch D 597, 601 per Cotton LJ, *Hardoon v Belilios* [1901] AC 118,123 per Lord Lindley; and *Re Amerind Pty Ltd (in liq)*, *Carter Holt Harvey Woodproducts Australia Pty Ltd v The Commonwealth of Australia* [2019] HCA 20; 93 AJLR 807, para 133 per Gordon J agreeing, citing Allsop CJ in *Jones v Matrix Partners Pty Ltd; In re Killarnee Civil & Concrete Contractors Pty Ltd (In liquidation)* (2018) 260 FCR 310). The trust expenses doctrine is a sort of salvage principle: a "salvor" should be paid if he enables a ship to be saved or the trust to operate. All these reasons are relied on in the authorities.

287. It further follows that, when the authorities (several of which Lord Richards and Sir Nicholas cite) use the expression "first charge" in relation to the trustee's right of indemnity, the point they are making is that trustees, and those who claim through them, rank ahead of the beneficiaries. That is the nature of the priority conferred on them. As Professor F.W.Maitland states in *Equity*, *Also*, *the Forms of Action at Common Law: Two Courses of Lectures* (1909), p 96, "Costs, charges and expenses, those properly incurred, become *as against the cestui que trust* a first charge on the trust property." (emphasis added).

288. But to make what may seem an obvious point, the right of indemnity is not given to confer any priority on one trustee over another or on one trust-related creditor over any other. That is no part of the equitable principle. Priority is not part of the right or its purpose. Priority, as Lord Richards and Sir Nicholas demonstrate, only occurs if at all through the operation of an entirely separate and rather strict maxim of equity that is applied across the board to successive interests in equitable property (here, the trust fund). Lord Richards and Sir Nicholas have proceeded on the basis, in my view correctly, that the equities are equal for present purposes unless the former trustee has misconducted himself, and so that qualification to the maxim is not relevant on these appeals.

289. Why should the former trustee, I would ask, have any right of priority? The position of the former trustee will not in all circumstances justify this. It is one thing to say that he should have this right if a later trustee has, for example, acted without due care in raising a large loan secured on assets which subsequently fall in value. It is another if the insufficiency results from some action by the former trustee which was not disclosed to the trustee who succeeds him. In some cases, he will know or foresee the liabilities incurred by him as trustee which are outstanding when he vacates office. He will also have had the opportunity to ask for security for those liabilities (although I am in no way suggesting that such security will be appropriate in every case).

290. Moreover, those liabilities will not necessarily be apparent to successor trustees, and it may be very difficult for them to find out about them or verify them by objective evidence. This issue of lack of visibility must surely strengthen the conclusion that the former trustee should not have any priority over later trustees for his expenses. If the full financial position was known, it may be that the later creditors would not have given credit even on a secured basis. Successive trustees may similarly take office in ignorance of a large liability which emerges from activities prior to their appointment. The net effect is that persons will in future be reluctant to do business with a trust and this may have a very damaging effect on the trust industry throughout the common law world.

291. Added to that there are likely to be difficulties in practice if the first-in-time maxim applies. Lord Briggs refers to difficulties of this kind. It may become necessary for trustees to make inquiries into the activities of past trustees whenever they undertake obligations on behalf of the trust.

292. When a liability on a former trustee emerges from the shadows and is due for payment, it may in practice be the current trustee who causes the trust fund to discharge it, and he will do so under his own powers. If that is so, it is difficult to see why the former trustee should be able to get an advantage by discharging it himself.

293. In addition, the trustee has a single lien for all his expenses. The right of indemnity does not arise afresh each time a trust-related liability arises, which would be the case with some other types of indemnity. This indulgence is for the protection of the trustee, and it continues (subject to any waiver or release) after the trustee vacates office. If the first-in-time maxim applies, it gives the former trustee priority over later trustees by reference to the date of his original appointment. That is beyond the purpose of the indulgence and so a limit to the law's indulgence in this regard is justified.

294. Trustees are, moreover, not strangers dealing with equitable property: they are connected by their common relationship to the trust. There is no general expectation that trustees will have this priority (see, for example, the work of the Trust Law Committee, referred to below).

295. On these appeals, Lord Richards and Sir Nicholas have expressed the view that there is nothing to indicate that the right of indemnity is for the benefit of creditors. They thus "do not consider that the authorities establishing the trustee's right of indemnity contain anything to suggest that the purpose of the right is conferred, even in part, to benefit trust creditors" (para 182). In my judgment, to say that the creditors

are not protected by the trustee's right of indemnity puts the matter too highly. For my part, I consider that the right of indemnity, especially when considered alongside the right of subrogation, should constitute a remedy for the general body of creditors when the trust fund is insufficient to pay them all. Where trustees may be personally liable, one should bear in mind that trustees may also have become insolvent, which will affect any trust creditor's ability to enforce any personal liability that they have.

Grant of security to retiring trustee is not an answer to the Board's pari passu conclusion

296. Lord Richards and Sir Nicholas recognise that there is no authority which requires us to hold that the first-in-time maxim applies. Their joint judgment takes the view that the pari passu principle will not provide an answer to the impracticality of the first-in-time maxim because a former trustee could always require security: see paras 190-200 above. Indeed, under Jersey law, he does not have an express right to retain assets but only a right to require reasonable security (art 34(2), now art 43A of the Trusts (Jersey) Law 1984). We have not heard full argument on this point, including the considerations relevant to determining what is reasonable security, and so all I can do is express some reservations about the propositions in these paragraphs. If these reservations are well-founded, the grant of security to the retiring trustee will not always be reasonable or appropriate. These reservations fall under two main heads.

297. Firstly, there is on the face of it no reason why a court of equity should allow a former trustee of a trust to require to be put in a better position than a current trustee of the same trust by taking security over the trust fund. As I have explained elsewhere in this judgment, the former trustee can require the trustee to desist from actions which would damage his ability to enforce his right of indemnity in the usual way. (He may in some circumstances think it right to require some contractual undertakings to this effect.) This gives him some protection against the spendthrift successor trustee. So, it may be, when the implications of the Board's decision are digested, that there is no real prospect in the usual case of the former trustee being granted security in the sense of an additional property right. I appreciate that there are cases where the courts of Jersey have directed generous amounts of security to retiring trustees, but those cases preceded the decision of the Board on these appeals. They may need further consideration.

298. Secondly, following the judgments in this case, former and current trustees rank pari passu as regards the trust fund if it is insufficient to pay all the sums against which they are entitled to be indemnified. In those circumstances, the pari passu principle may exclude the possibility of taking security in the sense of a property interest which ranks ahead of other trustees save in an exceptional case. I would draw an analogy

here between the position of trustees and the holders of debentures which are issued on the basis that they rank pari passu. The company cannot allow some of them to be paid out first or receive additional security since that would infringe the pari passu principle: see, for example, *Palmer's Company Precedents Part 3: Debentures*, 16TH ed, (1952) Chapter 13, pp 115 to 116 :

> "The words pari passu are adopted as a term well recognised in the administration of assets in courts of equity. Even when no pari passu clause or words actually expressive of equality are used, it is not difficult to imply them, e.g., where the debentures each say 'this debenture is one of a series of 1,000 like debentures, all ranking as a first charge on the undertaking of the company.' True, nothing is here said about pari passu security, but if *all* are to rank as a first charge, it is clearly implied that, as between them, there is to be no priority. …
>
> And the same principle applies where a debenture holder in an issue ranking pari passu obtains from the company a special security. He cannot hold it for his own individual benefit. He must be content to share and share alike in this, as in other respects, with the other holders of the pari passu issue… This is old law; see, as long ago as *Fairtitle v. Gilbert*, (1787) 2 T. R. 169, the case of a turnpike loan, where the Act provided that no preference should be given, it was held that one of the mortgagees who had obtained a special security could not avail himself of it. …The same principle applies where one of a number of debenture holders, ranking pari passu, brings an action for payment, obtains judgment and issues execution-the other debenture holders can intervene and restrain him from proceeding with the execution on the ground that they are interested in the premises. He holds the judgment, in fact, as trustee for all the debenture holders of the issue: ."(footnotes omitted)

299. Any problems in practice with working out the effect of the Board's conclusions in this case would in my judgment be worked out by the courts as, to borrow a phrase of Lord Mansfield, the law "works itself pure" (per Sir William Murray, Solicitor General, later Lord Mansfield in *Omychund v Barker* (1744) 1 Atk 21, 33). It has

effectively done so in relation to pari passu debentures, but of course it may develop differently in relation to trusts.

300. It is not appropriate for me to answer the reservations that I have expressed but they show that the grant of security to a retiring trustee does not undermine the conclusion that, if the trust fund is insufficient, it must be applied in discharge of unpaid trust-related liabilities pari passu. The law has yet to be worked out and that cannot be done in these appeals.

301. Trust-related liabilities should normally be paid when in the ordinary course of the administration of the trust they become due and payable. If the trust fund is insufficient to pay all expenses, the current trustee can apply to the court for directions as to how he should act. In the case of a trading trust, the court may direct the trustee to cease to trade and direct accounts and inquiries. Rateable abatement will follow as a matter of course unless the court thinks fit to order some preferential payments (see *Dowse v Gorton* [1891] AC 190, 203-204 per Lord Macnaghten). Any application for preferential payment would have to be made on evidence to the court below. It is likely to be necessary for the date for determining the amounts due to creditors to be established for the purposes of determining the amount by which they must abate.

Interpreting rights of indemnity according to their purpose is legitimate

302. Lest it be said that the limitation of officeholders' indemnity by reference to the purpose of the indemnity is without precedent, I would point to the decision of the Court of Appeal of England and Wales in *In re Atlantic Computer Systems Plc* [1992] Ch 505. This concerned the priority to be given in a company administration to the expenses of an administrator appointed by the court under the Insolvency Act 1986, where the administrator had adopted arrangements made before administration but had not incurred any new obligation. The court held that, when the court was asked to give directions for the payment of these expenses (which are not provided for by statute), it had to consider the legislative purpose of company administrations. This purpose might be jeopardised if all such expenses had to be paid as expenses of the administration. Nicholls LJ, giving the judgment of the Court of Appeal of England and Wales, held:

> "Parliament must have intended that when exercising its discretion the court should have due regard to the property rights of those concerned. But Parliament must also have intended that the court should have regard to all the other circumstances, such as the consequences which the grant or

> refusal of leave would have, the financial position of the company, the period for which the administration order is expected to remain in force, the end result sought to be achieved, and the prospects of that result being achieved." (p 528)

303. This is an example of the level of priority given to expenses being moulded to meet the purpose for which the right to recoup expenses was given and balanced against the rights of those entitled to be paid. The analogue to the intention of Parliament in this context is the intention of the settlor as discernible from the trust instrument. As explained, it is to be inferred from the trust instrument that the settlor intended the trust to be a continuing institution whose operation was not disrupted merely by a change in trustee. The expenses doctrine in relation to liquidations, administrations and receiverships is the subject of helpful and detailed analysis in G Moss QC and N Segal, *Insolvency Proceedings: Contract and Financing - The Expenses Doctrine In Liquidation Administrations And Receivership* [1997] 1 CFILR 1.

The work of the Trust Law Committee provides some support about trustees' expectation where the trust fund is insufficient

304. The conclusion to which I have come receives some support from the valuable work of the Trust Law Committee ("the TLC"). In 1997, the TLC issued first a comprehensive consultation document and then, in 1999, a (briefer) report on *Rights of Creditors Against Trustees and Trust Funds* (Society of Trust and Estate Practitioners (STEP) and Tolley Publishing Co Ltd). The project was chaired by Professor David Hayton (former CCJJ). The foreword to the consultation paper was written by Lord Browne-Wilkinson, who was also involved in taking Law Commission bills about trust law through Parliament. I was the Chair of the Law Commission of England and Wales from 1 January 1996 to the end of January 1999. The TLC did not even consider the possibility that trust-related liabilities could rank in priority according to the date of appointment of the trustee who incurred them. In its report, the TLC states that no commentator took issue with its exposition of the law.

305. By way of background, the TLC was established in 1994 under the chairmanship of Sir John Vinelott on his retirement as a Justice of the Chancery Division of the High Court of England and Wales, with backing from leading professionals and academics. It was formed to prepare a programme of reform for trust law. The Lord Chancellor authorised the Law Commission of England and Wales to work with the TLC. The TLC's publications are, therefore, authoritative.

306. The TLC considered that, subject to netting, trust-related liabilities of a single trustee would be paid pari passu (consultation paper, paragraph 2.62). As explained, it did not contemplate the ranking of creditors according to the date of appointment of the relevant trustee.

307. The TLC described "lack of visibility", as I call it in para 290 above, as "most unjust" (report, paragraph 3.6).

308. On my approach, the former trustee never has priority over a later trustee and so the law as I would enunciate it does not involve the deprivation of any property right for the purposes of article 1 of the First Protocol to the European Convention on Human Rights, which I therefore do not consider.

Judgment of Lord Briggs

309. I have read the judgment of Lord Briggs with admiration. Lord Briggs agrees with Lord Richards and Sir Nicholas that each trustee has a separate lien for his expenses and that, unless the first-in-time maxim can be disapplied, the separate liens would rank in the order in which the trustees are appointed. He then points out the practical difficulties of that course and holds that in consequence equity would disapply the first-in-time maxim and hold that trust-related liabilities should be paid or discharged pari passu by whichever trustee they were incurred.

310. I agree with Lord Briggs that in the event of insufficiency of the trust fund the court will not give priority to the outstanding claims under the trustees' right of indemnity according to the date on which the trustees were appointed. Lord Briggs regards "the common misfortune" doctrine as supporting his conclusion in favour of a pari passu distribution. However, like Lord Richards and Sir Nicolas Patten, I do not consider that much assistance is given by the "common misfortune" doctrine. The doctrine results in the distribution of assets pari passu but for different reasons. Lord Briggs cites four cases: *Barlow Clowes International Ltd v Vaughan* [1992] 4 All ER 22, *In re British Red Cross Balkan Fund* [1914] 2 Ch 419, *In re Hobourn Aero Components Ltd's Air Raid Distress Fund* [1946] Ch 86 and affirmed at [1946] Ch 194 and *In re Salters Hall School Ltd* [1998] 1 BCLC 401; [1988] BCC 503. The first three concern disapplication of the rule in *Clayton*'s Case 35 ER 781, (1816) 1 Mer 572; [1814-23] All ER Rep 1; which, as Astbury J pointed out in the *British Red Cross Balkan Fund* case at page 421, summarising what had been held by Lord Halsbury LC in *The Mecca* [1897] AC 286, 290, is a "mere rule of evidence and not an invariable rule of law". Moreover, the majority of the Court of Appeal of England and Wales in *Barlow Clowes International Ltd v Vaughan* held that the rule in *Clayton's* case did not apply not

because of the inconvenience which its application would cause, but because on the facts the relevant fund was a collective investment scheme whose participators intended that their contributions should be pooled. There was no question of any person having a claim to priority in respect of the fund. The fourth case is *In re Salters Hall School*. This does not assist on the point under consideration because it concerns a company in liquidation and there has since 1844 been statutory authority for the court to determine the order of priority of liquidation expenses (see generally G Moss QC and N Segal, above).

311. Moreover, courts of equity follow the law and have sought to uphold creditors' rights which have already accrued: see, for example, *In re Trix Ltd* [1970] 1 WLR 1421 and *In re Calgary and Edmonton Land Co Ltd* [1975] 1 WLR 355, where the courts declined to order respectively a compromise of provable debts in a liquidation and a stay of a liquidation (under which creditors had statutory rights to the distribution of the assets) without the consent of the creditors or their consent being obtained by a statutory scheme of arrangement.

312. The importance of respect for property rights also emerges from the passage cited above from the judgment of Nicholls LJ. If in the present case the trust-related liabilities in successive trusteeships give rise to proprietary interests which rank for priority in the order of appointment of the trustee who incurred them, then if the court were to order assets to be distributed pari passu, equity would potentially be altering property rights.

313. For my own part, I do not analyse this as a case of taking away of a right of priority. My view is that there was never any priority in the first place save as respects beneficiaries (see paras 286 to 288 above). Thus, the first-in-time maxim has no application in circumstances such as arise on the present appeals where the contest does not involve beneficiaries. Accordingly, there is no maxim to be disapplied and no right of priority to be taken away.

Analogy with trusts for the payment of a deceased's debts

314. The situation is in some respects similar to that described by Maitland where the deceased had devised property on trust for the payment of his debts. According to Maitland, courts of equity could order a proportional distribution of equitable assets to creditors without regard to the legal rank of their debt: see Maitland, *Equity*, *Also*, *the Forms of Action at Common Law: Two Courses of Lectures* (supra) p 199:

> "Here equity could neglect the old rules- it could say, and did say, that an equal or proportional distribution among all the creditors was the fairest mode of distribution. It had come by certain property which could be called equitable assets as opposed to legal assets; it could say that these equitable assets should be distributed without regard to the legal rank of debts, it could even forbid the executor to give himself an advantage by retaining his own debt out of these equitable assets."

315. Equity regards *pari passu* distribution that "as the fairest mode of distribution". Indeed, in *Equity* Maitland gives other instances of equity adopting it.

The Appendix is not part of my essential reasoning, but it shows that new article 32 as now in force provides some support for my conclusion

316. I could conclude here. While it is not an essential part of my reasoning, I consider that the recent reforms in the Jersey trust law support my conclusion. This is a lengthy point, so I have included it in the Appendix to this judgment.

Conclusion

317. I would allow these appeals. If the trust fund becomes insufficient, trust-related liabilities should not rank according to the date of appointment of the trustee who incurred them.

Appendix

318. Jersey statute law takes precedence over the law of England and Wales in relation to Jersey trusts. Under Jersey statute law, the trustee can now be regarded as a representative for the trust. I will explain this below. In my judgment, this is another factor supporting my conclusion that trust-related liabilities do not rank in priority to the date of appointment of the trustee which incurred them.

319. I start by setting out the Trusts (Jersey) Law 1984, as substituted by article 11 of the Trusts (Amendment No 4) (Jersey) Law 2006 ("the TJL") and then a lengthy passage from the Board's earlier judgment in *Investec Trust (Guernsey) Ltd v Glenalla Properties Ltd* (*"Investec 1")*, which analyses it. This analysis represents a key part of its reasoning in *Investec 1* since the Board went on to hold (by a majority) that the limitation of liability in article 32 of the TJL was to be characterised for the purposes of private international law as a matter of status regarding a trust (see paras 88-91). I set the analysis out in full in para 321 below as it has not previously been set out in these judgments. Indeed, it might be said that the Board would have to qualify its earlier decision in *Investec 1* if it did not now proceed from the basis of the status of the trust having regard to article 32. In my judgment, its special characteristics confirm the conclusion to which I have come.

320. Article 32 of the TJL provides:

> "32. Trustee's liability to third parties
>
> (1) Where a trustee is a party to any transaction or matter affecting the trust -
>
> (a) if the other party knows that the trustee is acting as trustee, any claim by the other party shall be against the trustee as trustee and shall extend only to the trust property;
>
> (b) if the other party does not know that the trustee is acting as trustee, any claim by the other party may be made against the trustee personally (though, without prejudice to his or her personal liability, the trustee shall have a right of recourse to the trust property by way of indemnity).
>
> (2) Paragraph (1) shall not affect any liability the trustee may have for breach of trust."

321. Lord Hodge, writing for the majority of the Board, analysed certain aspects of article 32 in *Investec 1*, paras 61 to 63. He held:

"61. The Board considers that the effect of article 32(1) is to abrogate the rule of English law that the law looks no further than the legal entity which has assumed the liability. It deals with the status of the trustee against whom the claim is made, introducing a legal distinction between his two capacities, personal and fiduciary. It provides that he may be treated as incurring liabilities not personally but 'as trustee', and therefore without recourse to his personal estate. The reasons are as follows:

(i) The object of the provision is to limit the exposure of the trustee in respect of liabilities incurred by him as such. Since the law already allowed him to do so contractually, it is reasonable to suppose that the draftsman intended something more than that. This is consistent with the fact that subsection (1) is not limited to contractual or even transactional liabilities. The opening words of the subsection ('Where a trustee is party to any transaction or matter affecting the trust') indicates that it is confined to liabilities arising from some pre-existing relationship to which the trustee can be said to be a 'party', and which has arisen in a manner affecting the trust. But that would extend to certain claims for unjust enrichment (for example claims arising from the frustration of a contract or a total failure of consideration), or tort (for example, claims for negligent misrepresentation).

(ii) Subsection (1) might be read literally as conferring a kind of claim in rem against the assets themselves. But the phrase 'shall be against the trustee as trustee and shall extend only to the trust property' must be read as a whole. The limitation of the trustee's liability is achieved by treating him as having two legally distinct capacities and two legally distinct estates. Only his capacity as trustee is relevant and only the trust estate is engaged. The words limiting the 'claim' to the trust property do not serve to introduce a monetary cap on the trustee's liability, as all parties now appear to accept. It would be unworkable in practice, in particular where there were

multiple third party claims against the trustees of a single trust. Nor are they concerned merely with controlling the execution of judgments. They serve to describe the character of the claim. It is a claim against the trustee in that capacity only. The limitation to trust assets follows on from that.

(iii) That view of the matter is reinforced by the contrast between subsection (1)(a), which deals with a claim against the trustee as such, and subsection (1)(b), which deals with a claim against the trustee personally. Before article 32 was enacted the trustee could incur liabilities in only one capacity, namely his personal one. The effect of the article is to create two.

(iv) It is fair to say that it is unusual for a statutory provision about the status of a person against whom a claim is made to depend on the knowledge of the claimant. But there is no conceptual difficulty about this. Irrespective of the knowledge of the claimant, the trustee has two capacities. The knowledge of the claimant does not determine his status. It only determines in which of his two distinct pre-existing capacities he is to be taken to have acted. The concept is familiar in other common law jurisdictions, and notably the United States, which the draftsman of article 32 is likely to have had in mind. In these jurisdictions, the unsatisfactory features of the English rule have led to the enactment of broadly similar statutory provisions to limit the liability of a trustee incurred in that capacity. The *American Law Institute*, *Restatement of the Law*, *Trusts*, 3rd (2012), vol 4, Chapter 21, pp 94-95 observes of the principle underlying these enactments that it

> ‘recognizes modern reality rather than traditional concepts. Technically, the trust is still not generally recognized as a legal “entity”, but … in practice trustees act on behalf of their trusts and are sued as trust representatives. Indeed, in this Chapter and elsewhere in this

> country, the trust is *treated* as an entity to such an extent that it is no longer inappropriate to refer to claims against or liabilities of a "trust" (as in the title and content of this Chapter) and to the liability or debt of a beneficiary to a "trust" (as in Chapter 20), or to refer to and treat trusts, in law and in practice, as if they were entities in numerous other contexts.'

62. This is, however, the only relevant respect in which the pre-existing law is altered by article 32. There is nothing in that article which modifies the rule that a creditor can access the trust assets only by way of the trustee's right of indemnity and subject to the limits on that right imposed by the trust deed or the general law. On the contrary, the continued subsistence of the rule is acknowledged by section 54(4) of the TJL. This provides:

> 'Where a trustee becomes insolvent or upon distraint, execution or any similar process of law being made, taken or used against any of the trustee's property, the trustee's creditors shall have no right or claim against the trust property except to the extent that the trustee himself or herself has a claim against the trust or has a beneficial interest in the trust.'

That subsection might have been expressly limited in its effect to a situation where article 32(1)(b), rather than (1)(a) applied, since in an article 32(1)(a) situation the solvency or otherwise of the trustee would be irrelevant, and there could be no distraint or execution upon his personal assets for his liability as trustee. But it was not. It assumes that the creditor's right to go against the trust fund continues to depend upon subrogation. In this regard the Jersey legislature has not gone as far as the legal initiatives in the United States in the personification of a trust by creating a direct right of action against the trust in return for relieving the trustee of personal liability. Instead it has relieved the trustee of personal liability by providing that a person when acting as a trustee acts in a separate capacity.

> 63. The creation of a new direct means of recourse by creditors against the trust fund, without the protection to the beneficiaries formerly accorded by the inherited English law, as described above, would be a radical departure which should not lightly be inferred or implied in the absence of clear words. The Jersey legislature plainly intended by article 32 to improve the position of trustees by insulating their personal assets from liabilities to third parties expressly incurred as trustees, and must have appreciated that this would have to be at the expense either of creditors or beneficiaries, or both. On the reasonably safe assumption that the legislature intended thereby to promote rather than damage the trusts industry in Jersey, and that its future prosperity would depend upon foreign settlors continuing to choose Jersey as the place for the establishment of their trusts, it seems very unlikely that a deliberate choice would have been made to improve the position of trustees at their beneficiaries' expense. By contrast with beneficiaries, creditors other than tax authorities are usually voluntary, and can choose upon what terms as to security and personal guarantees they are prepared to lend or give credit to trustees. Against that background the Board finds it impossible to discern from the terms of article 32 any intended change in the only method (of subrogation to the trustee's indemnity) whereby the pre-existing law enabled creditors to have recourse to the assets of the trust for the enforcement of liabilities incurred by the trustees."

322. Under section 32(1)(a) the trustee must be a party to any transaction or matter affecting the trust and the other party must know that the trustee is acting as trustee. There is no statutory definition of "to be a party" and provisionally it seems to me that it must carry a wide meaning, such as "to participate". Under the law of England and Wales, subrogation to the trustee's right of indemnity has been held to apply to trust-related tortious liability.

323. This clear statement in legislation is an operative provision. The creditor can rely on article 32(1) without having to invoke any other common law.

324. Therefore, the immediate effect of the Board's analysis of article 32 is that many, if not most, trust-related creditors will now have no personal remedy against the trustee. (Even if they did, they might have no prospect of recovery if the trustee

was a shell company as appears to be the case in several cases to which we were referred.) They can no longer sue the trustee in his personal capacity or bring winding up proceedings against it (if it is a corporate trustee) or prove in its winding up or claim to be a secured creditor of the trustee. He is then not a principal but a representative of the trust which is treated as if it were vicariously responsible. The rule of English and Welsh law that trustees are personally liable for liabilities incurred to third parties with a right of indemnity against the trust fund has been replaced in Jersey law by article 32. The creditor's right of subrogation has now in Jersey law become his primary, and not a fall-back, remedy.

325. The "modern reality" referred to in para 61(iv) of the Board's judgment has not reached the UK statute book. In this jurisdiction, limitations on a trustee's liability to the trust assets are regularly imposed by contract and the TLC recommended that there should be reform (TLC report, paragraphs 3.14 and 10.4).

326. The "modern reality" has, however, reached the statute book in many states in the USA. In para 61, the Board refers to the American Law Institute's *Restatement of the Law of Trusts*, 3rd ("*Restatement*, *Trusts*, *3rd*") (2012), vol 4, Chapter 21). The passage which Lord Hodge cites is from the introduction to that Chapter 21. This Chapter contains two sections, 105 and 106, which depart markedly from the second edition of the Restatement (1959). Article 32, as Lord Hodge explains, is in similar terms to sections 105 and 106 of the *Restatement*, *Trusts*, *3rd*. Article 32 and sections 105 and 106 have all moved away from the traditional approach of trust law under the common law. That imposed personal liability on the trustee with a right of indemnification (where the trustee has acted properly). Both article 32 and section 105 now confine the creditor's remedy to the trustee in his capacity as a trustee of the trust where it was known or disclosed that he acted in that capacity. (In the case of section 105 at least, a trustee may also be sued personally if it is alleged in the alternative that he is personally liable, that is, where the equivalent of art 32(1)(b) applies). The trustee's capacity is now as an agent and fiduciary for the trust, as distinct from his personal capacity, and it follows that the trust is being *treated* as a separate legal entity. If this is so for the purposes of third-party creditor's claim, this must also be so in relation to the trustee's right of indemnity and generally his proprietary interest.

327. Where article 32(1)(a) applies, the creditor does not have the choice of also suing the trustee personally. The provision for representative responsibility is the procedural aspect of article 32(1)(a), but, as is often the case, the article involves substantive law as well.

328. The remedy under article 32 is not completely the same as that under the law of England and Wales. Under that law, the creditor exercising his right of subrogation in respect of a trust-related liability takes subject to the state of account between the trustee and the beneficiaries (ie netting). (The Board has not been asked to review the law on this point and some trustees may by contract take a wider right or even a direct right against the trust fund if the trustee has power to agree to such a right (see TLC Report, 1999, paragraph 10.7)). Under the law of England and Wales, reduction in the amount recoverable by a creditor in respect of any trust-related liability is not restricted to liability for any breach of trust. It would, for example, include unpaid remuneration. Under article 32(2) the permitted set-off is only of liability for breach of trust.

329. Importantly, article 32(1)(a) has substantive aspects. I have already referred to the principal one. In Jersey law, the personal liability of the trustee is now limited. The limitation on the liability to a trust-related creditor under article 32(1)(a) is the amount of the trust assets. The trust is treated as an entity as per the introduction to the *Restatement*, *Trusts*, *3rd*. The trustee is treated as the fiduciary agent only of the trust. This is a fundamental change in the nature of the trust but the significance for present purposes is that it confirms the conclusion that the role of the proprietary interest of the trustee in respect of trustee-related liabilities is relevantly to protect the position of trust-related creditors generally.

330. To amplify the separate entity point, I agree as regards England and Welsh law with Lord Richards and Sir Nicholas Patten that "A trust is not an institution, still less a legal person, separate from the trustee" (para 58 above). However, in relation to the enforcement of trust-related liabilities owed to third parties, in my judgment, where article 32(1)(a) applies, it appears that a Jersey trust is *treated* as a separate legal entity and can now, for instance, where that is so, properly be described as insolvent. That is the effect of the "modern reality" reflected in article 32(1)(a).

331. The creditor's remedy under article 32 co-exists with the trustee's right of indemnity, and it is a derivative of it. The statutory remedy appears to be an alternative to subrogation under the general law. The creditor may not wish to invoke it unless the trustee is insolvent but there is nothing in article 32 to stop him from exercising it as soon as the liability to him is incurred and becomes due for payment.

332. If the trustee is treated as a representative of a trust, and not as a principal, then it is even less likely that the correct conclusion is that the priority of trust-related liabilities should depend on the date of his appointment.

333. My conclusions on these appeals appear in paras 279 and 317 of my judgment, above.