Case Note

LA Micro Group (UK) Ltd v LA Micro Group Inc [2023] EWCA Civ 214—A (sub-)trust for thee but not for me

Seongwook Nam* and Alexander Yean†

Abstract

In *LA Micro Group (UK) Ltd v LA Micro Group Inc* [2023] EWCA Civ 214, the Court held that under an express trust with A as trustee and B as beneficiary, a constructive sub-trust could arise with B as sub-trustee and A as beneficiary under the sub-trust, resulting in B dropping out of the picture and the legal title and beneficiary interest merging in A. It is argued that the Court's reasoning is conceptually untenable given the inherent instability of a circular sub-trust structure; the better view is that the remedy given was a *sui generis* equitable order.

Introduction

Over a century ago, Professor Maitland had already observed that the trust "is an institute of great elasticity and generality".[1] This vaunted elasticity was on full display in the recent Court of Appeal decision in *LA Micro Group (UK) Ltd v LA Micro Group Inc*[2] ("*LA Micro*"), in which a just outcome was reached by way of the unique, simultaneous application of two types of trust—the sub-trust and the vendor–purchaser constructive trust (the "VPCT")—to a difficult and unusual set of facts involving the beneficiary under an express trust also being the trustee of a sub-trust, with the beneficiary of the sub-trust being the trustee of the "head" express trust.

However, the authors submit that the reasoning adopted by the Court of Appeal in grappling with the difficult circular relationship between the parties was not fully satisfactory, and has strained the elastic application of the trust to breaking point. It is suggested that the inherent tensions stemming from the circularity of the trust structure under consideration in *LA Micro* is such that the result in that case is better conceptualised as a *sui generis* equitable order, rather than flowing from a genuine (sub-)trust.

Case summary

The dispute in *LA Micro* concerned the beneficial entitlement to shares of LA Micro Group (UK) Ltd (the "Company"), in respect of which there were two issued shares: one in the name of Bell and the other in the name of Lyampert. Each of Bell's share and Lyampert's share was held on express trust as to 49% for Bell and 51% for

*Seongwook Nam, Exeter College, University of Oxford, Oxford
†Alexander Yean, Gray's Inn, London

1. F.W. Maitland, 'Uses and Trusts' in *Equity: A Course of Lectures* (2nd ed., CUP 1969), 23.
2. [2023] EWCA Civ 214.

https://doi.org/10.1093/tandt/ttad057
Advance Access Publication 9 July 2023

LA Micro Group Inc (which was partly owned by Lyampert) ("Inc").

In 2010, Lyampert and Bell entered into an oral agreement (the "2010 Agreement") whereby, in exchange for valuable consideration:

i. in the case of Bell's share, the 51% beneficial interest formerly held by Inc should be transferred to Bell so that he became the 100% legal and beneficial owner; and
ii. in the case of Lyampert's share, the 51% beneficial interest held by Inc and the 49% beneficial interest held by Bell should both be transferred to Lyampert.

However, the 2010 Agreement between Lyampert and Bell failed to satisfy the requirement laid down in s.53(1)(c) of the Law of Property Act 1925 that the disposition of an equitable interest had to be in writing. One of the issues on appeal, and the only one of wider academic interest, is the question of whether a VPCT had arisen in respect of the 51% beneficial interest in Bell's share in the Company that was legally held by Bell for Inc—this would allow the disposition to be governed by s.53(2) of the 1925 Act, circumventing the writing requirement. In other words, did Inc hold its beneficial interest in the Company for Bell under a sub-trust (in the form of a VPCT), notwithstanding that Bell was the trustee under the "head" express trust?

The Court of Appeal held that the answer was yes. The reasoning of Nugee LJ, who gave the leading judgment, is worth setting out at length:

> 111. The question is whether it makes a difference that the intended disponee [under the sub-trust] is himself the registered legal owner of the shares.
>
> 112. But I do not myself think there is the difficulty [Counsel] suggested. A holds on trust for B. B therefore holds a beneficial interest in the shares. B contracts to dispose of that interest to A. On the principles already discussed that means that B holds his interest on [a vendor-purchaser] constructive trust for A. . . In the normal case where the intended disponee is not the trustee the effect is that the beneficial interest passes from B to the intended disponee, at any rate once his side of the contract has been performed so that he is entitled to call for it to be completed. In the case where the intended disponee is the trustee, I do not see why the effect is not exactly the same, namely that B holds his beneficial interest for A. The alternative would mean that the beneficial interest remained with B, despite the fact that he has agreed that it should pass to A, and that that agreement is specifically enforceable.
>
> 113. [Counsel] said that that cannot be the case as it would mean that A would hold on trust for B who would in turn hold on trust for A and that is not possible. But I think this is to confuse the question whether B holds his interest for A with the consequences of his doing so. It is easier to see this if one considers the case where A still has to pay money or perform some other obligation under the contract. In such a case the effect of the contract would be, as I have explained above, that B would become a qualified trustee, or trustee sub modo, for A and not a bare trustee. There is no reason why such a constructive trusteeship cannot subsist as there is no objection to A holding on trust for B who in turn holds on a qualified trust for A, as in such a case B has his own interest and does not drop out. Now suppose that in such a case A pays the purchase price and becomes entitled to call for completion. B now does become a bare trustee, so the property is held by A on trust for B who in turn holds on trust for A. The effect it seems to me is that B would drop out, and A would be left holding both the legal and beneficial interest. As already referred to, A cannot hold on trust for himself, so the practical effect is that A would simply hold the whole legal and beneficial interest.
>
> 114. If this is right, and I am satisfied it is, then it cannot make any difference that A does not have to pay any money under the contract or perform any other obligation before being able to call on B to complete. From the date of the contract therefore *A holds on trust for B who in turn holds on trust for A*, with the consequence already identified that *B drops out* and *A*

holds the whole legal and beneficial interest. (emphasis added by authors)

Males LJ agreed with Nugee LJ, and said:

123. I also agree. The effect of Lord Justice Nugee's analysis at [111] to [114] above is that the *constructive trust* in favour of Mr Bell ("A" in Lord Justice Nugee's example) *came into existence and ceased to exist at the same moment.* As soon as Inc's (B's) beneficial interest in the share held by Mr Bell was held on a constructive trust for Mr Bell, Inc dropped out and the beneficial interest ceased to exist separately from the legal interest which Mr Bell already held. That may be an unusual situation, but does not detract from the analysis. (emphasis added by authors)

Arnold LJ also agreed with Nugee LJ and added nothing to this point.

Analysis

The authors submit that the Court of Appeal's analysis is conceptually unsatisfactory. It is accepted that, as a matter of justice vis-à-vis the 2010 Agreement, Bell ("A") ought ultimately to be entitled to the beneficial interest which A had been holding on express trust for Inc ("B"). However, it is difficult to reconcile the Court of Appeal's reasoning that B automatically "drops out" of the picture (or that the sub-trust "came into existence and ceased to exist at the same moment") with the modern view of sub-trusts.

The starting point is to consider the position in the case of a standard 3-party trust/sub-trust structure, where A, the legal titleholder, holds the beneficial interest for B, who in turn holds the beneficial interest for C. In such a case, the modern view is that B does not "drop out" of the picture; rather, B remains as the trustee for C while A remains as the trustee for B,[3] notwithstanding the existence of several dated authorities to the contrary.[4] This is because C has no direct legal relationship with A and hence no enforceable rights against A[5]; C's only enforceable rights are against B. In this sense, "the nature of the interest under a sub-trust may be regarded in one respect as analogous to that of a subtenant under a lease of land. The sub-tenant has a proprietary right vis-à-vis his immediate landlord but no relationship exists between the subtenant and the head-landlord."[6] Importantly, this analysis is unaffected by whether B has substantial duties to perform or is merely a bare trustee (of the sub-trust), since this has no bearing on whether C has directly enforceable rights as against A.

Indeed, some commentators have gone even further, suggesting that not only does B not "drop out", but B must necessarily retain for himself an equitable interest of some sort, since B's declaration of (sub-)trust in favour of C "cannot, by definition, constitute a disposition of the entirety of the interest hitherto present in the declarant, for if the declaration is to be effective as a declaration, the declarant must retain some proprietary right which can form the subject-matter for the sub-trust created by him".[7] While this theory is not universally accepted (and a fuller analysis thereon would be beyond the scope of this note),[8] it appears generally accepted that B cannot be considered to have "dropped out" even if he purports to hold the entirety of his beneficial interest for C.

The modern position that B does not "drop out" is not only coherent as a matter of principle, but also as a matter of practice, in that the creation and/or the key details (such as the duties of B as sub-trustee) of the sub-trust as between B and C may lie beyond A's knowledge, such that it is necessary to retain B as the conduit between A and C to ensure clarity as to the parties' respective rights and obligations vis-à-vis each other.[9]

3. *Nelson v Greening and Sykes (Builders) Ltd* [2007] EWCA Civ 1358, §§56–57 (Lawrence Collins LJ); *Sheffield v Sheffield* [2013] EWHC 3927 (Ch) §§80–86 (HHJ Pelling QC sitting as a High Court Judge); Snell's Equity (34th ed.), §21-006; Lewin on Trusts (20th ed.), §1-046.
4. See e.g. *Grainge v Wilberforce* (1889) 5 T.L.R. 436; *Re Lashmar* [1891] 1 Ch. 258.
5. *Hayim v Citibank NA* [1987] A.C. 730.
6. Patrick McLoughlin, 'Rights of beneficiaries under trusts and sub-trusts' (1988) Conv. 60, 63.
7. Brian Green, 'Grey, Oughtred and Vandervell—A Contextual Reappraisal' (1984) 47(4) M.L.R. 385, 396.
8. Patrick McLoughlin, *op. cit.*, 62.
9. Leigh Sagar, 'Sham about the sub-trust – some random thoughts about the decision in *Sheffield v Sheffield*' (2014) 20(8) Trusts & Trustees 826, 831.

This factor becomes especially relevant in the event of a breach of trust by A. For instance, if A, in breach of trust, transfers the trust property to an unrelated party X, the remedy available to C is to require B, as the "mezzanine" trustee, to hold A accountable for the breach of trust to B, rather than C directly holding A to account.[10] This is sensible since it is conceivable that, for instance, C might not even know A's identity (given that it is not required for the establishment of the sub-trust between B and C).

However, the above analysis applicable to the A→B→C structure does not translate to the A→B→A structure under consideration in *LA Micro*. Assuming the same fact pattern where A (*qua* trustee of the "head" trust) transfers the trust property to X in breach of trust, absurdity results in that A (*qua* beneficiary of the sub-trust) can sue B (*qua* trustee of the sub-trust) in respect of A's own wrongdoing. In other words, on this analysis, B is accountable to A for A's own breach of trust. This plainly cannot be correct.

The Court of Appeal in *LA Micro* circumvented this difficulty by holding that "B would drop out, and A would be left holding both the legal and beneficial interest",[11] such that the B→A sub-trust "came into existence and ceased to exist at the same moment",[12] with the ultimate effect that the legal title and beneficial interest are merged in A. This avoids the difficulty of B being accountable to A for A's own breach of trust, since at no point is B simultaneously both the beneficiary under the "head" trust and accountable to A under the sub-trust.

However, the Court of Appeal's approach is contrary to the modern orthodox framework for sub-trusts discussed above, viz. that B (the beneficiary of the "head" trust/trustee of the sub-trust) does not simply "drop out". None of the speeches in the Court of Appeal adequately explain why B can simply be assumed to have "dropped out". It is an insufficient justification that B is a bare trustee rather than a trustee *sub modo*, since, as argued earlier in respect of the standard A→B→C case, C nevertheless does not have directly enforceable rights against A. *Mutatis mutandis*, the mere fact that B has no obligations *qua* (sub-)trustee does not mean that A (*qua* trustee of the "head" trust) holds the beneficial interest in the trust property directly for A (*qua* beneficiary of the sub-trust) such that the legal title and beneficial interest are merged.

A more plausible explanation for B "dropping out", at least at first glance, might lie in the *effect* of the A→B→A trust structure, viz. that A is both the legal owner and the ultimate beneficiary, such that in effect, the legal title and beneficial interest are merged; as a result, the entire trust structure collapses. The flaw in this explanation is that while it is certainly correct to say that A cannot hold on trust for himself, it is not in fact the case that A is holding on trust for himself; rather, B subsists as an intermediary. It would be circular to ignore B's existence to say that A is holding on trust for himself so as to justify having B "drop out". To borrow the words of Nugee LJ, "this is to confuse the question whether B holds his interest for A with the consequences of his doing so".[13]

As such, it is apparent that the A→B→A structure presents an inherent conceptual challenge. The Court in *LA Micro* was between Scylla and Charybdis: if B does not "drop out", absurdity may result in that B can theoretically be liable to A for A's wrongdoing; on the other hand, it is contrary to the modern orthodox understanding of sub-trusts for B to automatically "drop out". Ultimately, the Court's approach may have been spurred more by the pursuit of fairness than of conceptual clarity, as was hinted at by Nugee LJ in stating that he was "not sorry to reach" what he considered to be "a just result".[14]

This conceptual difficulty admits of no easy solution. The authors suggest that it appears to be the case that the A→B→A trust structure is fundamentally unstable. Putting aside the VPCT for the moment, consider the

10. *Sheffield v Sheffield*; Lewin on Trusts (20th ed.), §1-046.
11. *LA Micro*, §113 (Nugee LJ).
12. *LA Micro*, §123 (Males LJ).
13. *LA Micro*, §113 (Nugee LJ).
14. *LA Micro*, §120. (Nugee LJ).

simpler case where A holds property on express trust for B, and B then purports to declare himself the sub-trustee of an express sub-trust in favour of A. Since this would lead to the aforementioned absurdity, it is suggested that the law should not give effect to B's declaration of trust; the putative B→A sub-trust should not come into existence. Rather, B's declaration should be treated as a simple surrender of his beneficial interest back to A.

What, then, if the putative B→A sub-trust is not an express trust, but a VPCT? One possibility is to altogether reconceptualise the VPCT as a mere court order to specifically perform rather than a true trust, as has been argued by Professor Swadling.[15] Underlying this re-conception is the observation that, unlike in an express trust, the "trustee's" duty to transfer the "trust" property under a VPCT is the basis and not the product of the "trust"; as such, to say that a VPCT has emerged out of a specifically enforceable duty to transfer property is to reason backwards. Applying this analysis to *LA Micro*, B's duty to transfer the property to A can simply be reconceptualised as a court order to do so. No sub-trust between B→A ever arises, and all the difficulties inherent to the A→B→A trust structure discussed above can thus be avoided; this reasoning is preferable to the strained reasoning of the Court of Appeal that the B→A sub-trust "came into existence and ceased to exist at the same moment".[16]

However, such a radical re-conceptualisation of the VCPT is at odds with the long line of authority in support of VPCTs being true trusts, with the vendor/trustee being subject to specific duties.[17] As such, in the final analysis, the best view is that the "sub-trust" in *LA Micro* should not be understood as a VPCT, or indeed a trust at all; rather, the Court's declaration that the beneficial interest has merged with A's legal title can simply be seen as a *sui generis* equitable order. Pursuant to this order, no sub-trust between B→A ever arises, the conceptual problems thereto are avoided, and a just outcome is nevertheless reached. Accepting this view is to embrace equity at its most flexible, without the need to abuse the elasticity of the trust past breaking point.

Conclusion

The Court of Appeal in *LA Micro* was put in the unenviable position of having to achieve a just outcome while wrangling with unusual and difficult facts that were not susceptible of being fit neatly within a stable trust framework. With respect, it is suggested that the Court's conclusion as regards the A→B→A sub-trust is unsustainable for the reasons stated. The better view is to see *LA Micro* not as a sub-trust or VPCT case, but as a case involving a *sui generis* equitable order.

Seongwook Nam *is a student at Exeter College, University of Oxford.*
Alexander Yean *is a pupil barrister at 20 Essex.*

15. William Swadling, 'The Fiction of the Constructive Trust' (2011) 64(1) C.L.P. 399.
16. *LA Micro*, §123 (Males LJ).
17. See generally Snell's Equity (34th ed.), §24-003.