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A Normative Approach to the *Quistclose* Trust

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This is the first article to undertake a sustained analysis of normative justifications for the *Quistclose* trust. Whilst much of the existing writing on this topic has focused on the better classification of such trusts – for instance, whether they are express, resulting, constructive or *sui generis* – this article asks why the law should recognise a trust in addition to any underlying legal relationship. Four key justifications are addressed, based on respecting party intention, unconscionability, fairness, and the incentivisation of desirable transactions. It will be argued that: (i) there are difficulties with each of these justifications, although an intention-focused explanation is probably the most convincing; and (ii) the existing law and commentary lacks coherence and consistency, as seen in the mismatch between normative and doctrinal analysis, and the failure to properly address the ramifications of the *Quistclose* trust during insolvency.

INTRODUCTION

This article explores justifications for the *Quistclose* trust. Such trusts are named after the famous decision of the House of Lords in *Quistclose Investments Ltd* v *Rolls Razor Ltd*[1] (*Quistclose*) and have been held to arise where money is transferred on terms that it may only be used by the recipient for a specific purpose.[2] If the money is applied for the permitted purpose, the trust dissolves and – if the transfer was by way of loan, which is often the case – a relationship of debtor and creditor remains. If, however, performance of the purpose becomes impossible or is not carried out, the lender may enforce rights to the money under a trust, an option that is particularly attractive if the borrower becomes insolvent.[3] In *Quistclose*, Lord Wilberforce held that there were two trusts that

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1 *Quistclose Investments Ltd* v *Rolls Razor Ltd* [1970] AC 567.
2 Such purposes have extended from the payment of creditors to include the purchase of property or equipment: For example, *Twinsectra Ltd* v *Yardley* [2002] 2 AC 164 (*Twinsectra*); *Re EVTR Ltd* (1987) 3 BCC 389 (*Re EVTR*).
3 This assumes that prior to the money being applied for the designated purpose, there is a trust that: (i) takes the money outside the general assets of the borrower; and (ii) is not caught by

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arose sequentially: a 'primary' trust in favour of the shareholders, and when that trust failed due to Rolls entering voluntary liquidation, a 'secondary' trust in favour of the lender.[4] Whilst some cases have applied a two-trust characterisation, other explanations have also been presented, most notably that *Quistclose* scenarios involve a single express or resulting trust for the lender, subject to a power allowing the borrower to apply the funds for the designated purpose.

There is a sizeable body of literature considering the better characterisation of the *Quistclose* trust. Significantly, however, this characterisation exercise typically rests on unstated and untested assumptions that a trust should arise. But why ought the law to recognise a trust in addition to any underlying legal relationship? This article focuses on this prior question through a normative analysis that critiques the key values or goals that might be said to underpin the *Quistclose* trust. It does not suggest that existing classification efforts are irrelevant but rather that many court judgments and academic contributions either lack an explicit normative framework or deal too swiftly with contentious assertions regarding the basis and effect of the *Quistclose* trust.[5] Emphasis of these normative matters is important not just to explain the existence of a trust but to explore how, if at all, *Quistclose* trusts ought to be regulated.

As seen in the next part of this article, one explanation for the *Quistclose* trust is a 'methodological' approach that looks to its form, most notably by reference to intent.[6] For instance, Jamie Glister, discussing the possibility that *Quistclose* scenarios involve an express trust in favour of the lender, has observed that 'as long as the necessary intention to create a trust can be inferred from the parties' agreement, there is no reason to deny them the relationship that they objectively intended.'[7] As a normative matter, this statement would seem to rest on the proposition that the rules regarding the creation of trusts are the product of decisions about when trusts ought to arise. If the prerequisites for the creation of an express trust are met, it may therefore be unnecessary to invoke any *additional* normative justification for a *Quistclose* trust. This second

prohibitions on preferences or other unlawful attempts to contract out of insolvency rules. The relevance of insolvency law to the *Quistclose* trust will be considered throughout this article, and especially in the fourth section.

4 *Quistclose* n 1 above, 580, 582.

5 Pierre Schlag, writing in relation to American academic legal scholarship, has stated that the 'orientation of [such scholarship] is pervasively and overwhelmingly normative', although sometimes this normative agenda 'is a covert "should" – hidden beneath layers of legal positivism': P. Schlag, 'The Critique of Normativity (1991) 139 U Pennsylvania LR 801, 808. As Schlag notes, there is much in the argument that the distinction between descriptive and normative analysis is often illusory because 'many of the categories uncritically adopted in [descriptive work] are already normatively charged' (*ibid*, 813). To illustrate, some judicial and academic defences of the *Quistclose* trust place weight on following outcomes in the prior case law. This can be seen as normative, to the extent it values goals such as continuity and predictability. Difficulties arise in a number of ways, for example, because the relevant values are not stated explicitly, because only some values are considered, or through incoherence in the way the stated values translate to the legal reasoning.

6 C. E. F. Rickett, 'Different view on the scope of the *Quistclose* analysis: English and antipodean insights' (1991) 107 LQR 608, 646-647.

7 J. A. Glister, 'The nature of *Quistclose* trusts: classification and reconciliation' (2004) 63 CLJ 632, 645.

part describes how intention is used in the case law in relation to express and resulting trust models, and describes two key problems with a form-justifying-existence approach. One problem is empirical: in many cases, the conclusion that the transaction exhibited trust-consistent features was tenuous or counterfactual. A second issue is philosophical, and relates to the degree to which justifications for the express trust are often based on its characteristics and potential applications rather than the desirability of any particular application. It may be that the trust is, on balance, a desirable instrument, despite the costs associated with some uses, such as aggressive tax planning. However, we must take care in pressing any normative justification of the *Quistclose* trust that relies solely or mainly on the settlor having satisfied the prerequisites for trust formation.

It is therefore necessary to consider other rationales that might justify the *Quistclose* trust. Three possibilities are discussed in the third part of this article. The first focuses on the conscience of the recipient being bound such that she cannot accept the money from the lender *and* disregard the restrictions on use, consistent with the *Quistclose* trust preventing unconscionable conduct. It has also been suggested that fairness demands that the lender get back her money upon failure of the purpose, for instance because this will prevent the borrower or her other creditors from receiving a windfall. Still another possibility, albeit one not seen explicitly in the case law, is that the quasi-security provided by a *Quistclose* trust serves to incentivise desirable transactions, in particular lending to entities in financial difficulty. This article argues that that there are difficulties with each of these justifications, raising doubts as to whether any of them help bolster the case for *Quistclose* trusts.

In the fourth part, the article turns to consider the regulatory consequences of the foregoing analysis. It argues that whilst an intention-focused explanation is the most compelling normative justification for the *Quistclose* trust, we have not pressed such a characterisation to its logical conclusion. For instance, there is widespread acceptance that in insolvency situations, *Quistclose* trusts function like security interests.[8] If this is correct, one might ask whether they ought to be a target of regulation, for instance by being required to be registered. This section explores these points by reference to the Personal Property Securities Act 2009 in Australia, which despite adopting a functional definition of security interest expressly excludes *Quistclose* trusts from its ambit.[9] It also notes other possibilities for regulation of the *Quistclose* trust, in particular as an unlawful preference.

The ultimate conclusion is that we need a clear, consistent and principled approach to the recognition of *Quistclose* trusts. There are two main possibilities that are not mutually exclusive: first, they are intentional trusts that function like security interests; and secondly, they are imposed by courts as constructive trusts. However, these characterisations are based on different normative underpinnings, result in different doctrinal tests for creation, and will produce

8 For example, Mr Justice Priestley, 'The *Romalpa* Clause and the *Quistclose* Trust' in P. D. Finn (ed), *Equity and Commercial Relationships* (Sydney: Lawbook Co, 1987); M. Bridge, 'The *Quistclose* Trust in a World of Secured Transactions' (1992) 12 OJLS 333.

9 Personal Property Securities Act 2009 (Cth), s 8(1)(h).

different regulatory consequences – for instance, whilst it may be right to require registration of an express trust that captures some of the benefits of a traditional security interest, the same may not be the case for trust that is imposed as a matter of law. At present, the *Quistclose* trust operates as an unsatisfactory amalgam of an express and constructive trust: intention is emphasised but not always taken seriously by judges as a matter of evidence; concepts such as unconscionability and fairness are cited without clarity as to what they add; and the economics of insolvency is largely ignored.

QUISTCLOSE TRUSTS AND INTENTION

This part examines the possibility that intention justifies the *Quistclose* trust, focusing on express trust models but also discussing the relevance of intention to a sole resulting trust characterisation. The analysis commences in the first section by providing an overview of the stated doctrinal relevance of intention in the case law.[10] It is then argued that despite intention being said to play a central role, in a number of leading English cases, a trust has been found despite the evidence of intention being limited or pointing in the opposite direction. This suggests that in those cases, the *Quistclose* trust was actually imposed. The third section sets out a further problem: that even if we take seriously the need for convincing evidence of intention, it is questionable whether the usual rationales for the express trust as a legal institution provide a complete normative explanation for the *Quistclose* trust. That is, even if *Quistclose* trusts are intentional trusts, this is not the end of the matter in justifying their existence and operation.

Intention in the case law

Express Trust Models

Many characterisations of *Quistclose* scenarios involve at least one express trust, being a trust for human beneficiaries or for a purpose. Under both approaches, compliance with the three certainties requires an intention to create a trust, the main difference being the objects of the trust, with the purpose trust approach contentious due to its conflict with the beneficiary principle.[11] Although there were a number of decisions in the 1970s and 1980s that preferred this construction of the *Quistclose* trust,[12] it has been criticised by academics and

10 A more profound thought experiment – and one beyond the scope of this article – is whether a fundamental reconceptualisation of the logic behind classification is necessary: see B. McFarlane, 'The Centrality of Constructive and Resulting Trusts' in C. Mitchell (ed), *Constructive and Resulting Trusts* (Oxford: Hart, 2010).

11 For further discussion of the beneficiary principle, see J. S. Getzler, 'Morice v Bishop of Durham (1805)' in C. Mitchell and P. Mitchell (eds), *Landmark Cases in Equity* (Oxford: Hart, 2012).

12 Especially *Re Northern Developments Ltd* (unreported, 6 October 1978, Ch D, *per* Megarry VC); *Carreras Rothmans Ltd* v *Freeman Matthews Treasure Ltd* [1985] Ch 207 (*Carreras*). The decision in *Re EVTR* n 2 above is also consistent with the understanding that the initial trust was a private purpose trust.

judges,[13] and has fallen out of favour in the courts.[14] Given that much of the normative analysis in this section will be the same irrespective of whether the objects of a *Quistclose* trust are people or a purpose, this article will not discuss the desirability of expanding the range of valid private purpose trusts. Instead it will ask whether respecting party intention provides any assistance in justifying the *Quistclose* trust.

When we look to the case law, we see numerous statements that intention is central to the *Quistclose* trust. For example, in *Quistclose* itself, the reasoning of Lord Wilberforce was informed by what he understood to be the mutual intention of the parties to the loan transaction. The key facts were that Rolls had declared a final dividend of just under £210,000 but was in a precarious financial position and could not afford to pay its shareholders without external assistance. Quistclose agreed to lend the required sum to Rolls, and this sum was paid into a separate account set up by Rolls at Barclay's Bank. Not long after – and before the dividend was paid – Rolls entered voluntary liquidation. The Bank applied the money in the special account against other Rolls accounts that were in debit. Quistclose sought the return of its money from the Bank, however, in order to succeed it needed to demonstrate that it had a continuing interest in the money and was not a mere creditor of Rolls.[15] In finding in favour of Quistclose, Lord Wilberforce derived from the facts the proposition that the 'mutual intention' of Quistclose and Rolls, and the 'essence of the bargain', was that the loan moneys should not become part of the general assets of Rolls but should be used exclusively for payment of the shareholders.[16] He concluded that:

> when the money is advanced, the lender acquires an equitable right to see that it is applied for the primary designated purpose . . . if the primary purpose cannot be carried out, the question arises if a secondary purpose (ie repayment to the lender) has been agreed, expressly or by implication: if it has, the remedies of equity may be invoked to give effect to it, if it has not (and the money is intended to fall within the general fund of the debtor's assets) then there is the appropriate remedy for recovery of a loan.[17]

It will be necessary to return to the evidence used by Lord Wilberforce to locate this mutual intention. In terms of the doctrinal analysis, Lord Wilberforce identified two trusts – a primary trust 'in favour . . . of the creditors', and a

13 Especially *Re Australian Elizabethan Theatre Trust* (1991) 102 ALR 681, 692-693; *Twinsectra* n 2 above at [85]-[92] *per* Lord Millett; W. Swadling, 'Orthodoxy' in W. Swadling (ed), *The Quistclose Trust: Critical Essays* (Oxford: Hart, 2004) 9, 28-29.

14 In *Cooper* v *PRG Powerhouse Limited* [2008] EWHC 498 (Ch), Evans-Lombe J used the language of 'purpose trust' when describing the *Quistclose* trust: for example, heading to [10]-[11]; [14]-[16]; [18]. However, there is no suggestion that the judge considered himself to be departing from the approach of Lord Millett in *Twinsectra*; rather, it seems that Evans-Lombe J was (perhaps unfortunately) using the words '*Quistclose* trust' and 'purpose trust' interchangeably.

15 Under a normal loan agreement, the borrower receives absolute title to the money, and can apply it at her own discretion. The lender's right is a mere personal right to be repaid: see *Twinsectra* n 2 above at [68].

16 *Quistclose* n 1 above, 580.

17 *ibid*, 581-582.

secondary trust, if the primary one failed, of the lender[18] – although he did not discuss in detail the nature of these trusts, and there is ambiguity in his language.[19] One interpretation is that the primary trust was a garden-variety express trust for human objects (the shareholders),[20] whilst another is that the primary trust was for a purpose.[21] In *Re Australian Elizabethan Theatre Trust*, Gummow J observed that Lord Wilberforce's reasoning was 'indicative of an express trust with two limbs' rather than an express trust followed by a resulting trust, although this did not alter the outcome in the *Quistclose* case.[22] Gummow J also reiterated the importance of intention to the express trust, stating that:

> The question as to the existence of any express trust will always have to be answered by reference to intention. . . . Ordinarily, the relevant intention is that of the alleged settlor, but where the subject matter of the trust is contractual rights against the settlor, conferred by the settlor upon the alleged trustee, the objective (or 'purpose') of the transaction being to benefit third parties, it may be appropriate to look to the mutual intention of settlor and trustee . . . The relevant intention is to be inferred from the language employed by the parties in question and to that end the court may look also to the nature of the transaction and the relevant circumstances attending the relationship between them . . .[23]

Gummow J did not seek to fix *Quistclose* scenarios with a single characterisation, observing that 'the facts in such cases are susceptible of infinite variation and the trust is a supple instrument'.[24] Indeed, his Honour also noted that some arrangements that have trust-like characteristics may, on closer inspection, involve an assignment or the creation of some other equitable interest such as a charge.[25] That said, Gummow J's analysis was predicated on the view that any trust that arose was an orthodox express trust,[26] whether the transaction involved a single trust subject to a mandate, a single trust with two limbs, etc. His Honour did not consider the possibility that a sole *resulting* trust might arise, as proposed some ten year later by Lord Millett in *Twinsectra* and discussed in the next sub-section. However, *Twinsectra* does not seem to have had any significant impact on the Australian understanding of the *Quistclose* trust, with judges largely of the view that such trusts are express.[27] This article will return

18 *ibid*, 580.
19 For example, G. Dal Pont, *Equity and Trusts in Australia* (Sydney: Thomson, 6th ed, 2015) at [27.75].
20 For example, R. Chambers, 'Restrictions on the Use of Money' in Swadling (ed), n 13 above, 79; Graham Virgo, *Equity & Trusts* (Oxford: OUP, 2nd ed, 2016) 291.
21 For example, *Bellis* v *Challinor* [2015] EWCA Civ 59 at [54]; J. E. Penner, *The Law of Trusts* (Oxford: OUP, 9th ed, 2014) at [9.58].
22 *Re Australian Elizabethan Theatre Trust* n 13 above, 691.
23 *ibid*, 693 (citations omitted).
24 *ibid*.
25 *ibid*, 694.
26 *ibid*, 692, noting that 'the use of the expression "purpose" [by Lord Wilberforce in *Quistclose*] should not be read as heralding a new era for the non charitable purpose trust.'
27 For example, *Salvo* v *New Tel Limited* [2005] NSWCA 281 especially at [32]-[53] *per* Spigelman CJ, [83]-[96] *per* Young CJ; *Pearson* v *State of Western Australia* [2012] WASC 102 at [40], [42], [46]-[53]; *Legal Services Board* v *Gillespie-Jones* [2013] HCA 35 at [112]-[119]; *Sino Iron Pty Ltd*

below to the question of how the law should ascertain intention. Before turning to this question, it will consider how intention is relevant to Lord Millett's single resulting trust characterisation.

Resulting Trust Model

The leading authority that *Quistclose* trusts are resulting trusts in favour of the transferor is Lord Millett's speech in *Twinsectra*. That case centred on a loan for the acquisition of property.[28] Lord Millett was of the view that in a *Quistclose* scenario, the beneficial interest must remain with the lender throughout the entire transaction.[29] However, he departed from his earlier 1985 article by concluding that the *Quistclose* trust is best characterised as resulting as the lender did not intend to vest in the borrower the beneficial interest in the loaned money.[30] In adopting this approach, Lord Millett cited the work of Robert Chambers that resulting trusts arise where the transferor lacks any intention to benefit the recipient rather than responding to a positive intention that the beneficial interest be retained.[31] As Lord Millett noted, Chambers did not, in his 1997 monograph, apply this model to the *Quistclose* trust,[32] a fact Lord Millett found 'surprising'.[33]

There are doctrinal tensions in Lord Millett's reasoning. As stated by James Penner, Lord Millett's characterisation appears to be a 'hybrid' between an intentional and an imposed trust.[34] On the one hand, Lord Millett said that *Quistclose* trusts are resulting, a conclusion that subsequent English cases have repeated.[35] On the other, his reasoning suggests that it will be necessary for litigants to lead evidence of the transferor's actual intention in order for a trust

v *Palmer (No 3)* [2015] QSC 94 at [76]. It has been said by Campbell JA that where a trust is held to have arisen, this will be 'a matter arising from analysis of the facts of the particular case in accordance with well established principles for identifying when there is a trust, not because there is any separate legal institution known as a "*Quistclose* trust"': *Raulfs* v *Fishy Bite Pty Ltd* [2012] NSWCA 135 at [51].

28 The facts of *Twinsectra* are described around n 62 below.

29 This was said to explain two things: first, that the lender had the capacity to enforce the primary trust (which would not be possible if the lender was only the settlor of that trust); and secondly, how the insolvency of the borrower caused the primary trust to fail: *Twinsectra* n 2 above at [96]-[98].

30 *ibid* especially at [100], [102]; compare Sir P. Millett, 'The Quistclose Trust: Who Can Enforce It?' (1985) 101 LQR 269. Writing extra-judicially in 2011, Lord Millett stated that he first put forward his *Twinsectra* reasoning in this 1985 article: Lord Millett, 'The *Quistclose* trust – a reply' (2011) 17 T&T 7, 10. Whilst it is correct to say that Lord Millett retained the view that the beneficial interest remains with the lender, the LQR article appeared to proceed on the basis that the trust created by the lender is express.

31 *Twinsectra* n 2 above at [91]-[92].

32 R. Chambers, *Resulting Trusts* (Oxford: OUP, 1997) ch 3.

33 *Twinsectra* n 2 above at [92].

34 J. Penner, 'Lord Millett's Analysis' in Swadling (ed), n 13 above, 56.

35 Especially *Re Margaretta (in liq)* [2005] EWHC 582 (Ch) at [12], [24]; *Templeton Insurance Limited* v *Penningtons Solicitors LLP* [2006] EWHC 685 (Ch) at [18]; *Bieber* v *Teathers Ltd* [2012] EWCA Civ 1466 at [14] (Patten LJ reproducing with apparent approval the legal summary set out by the trial judge); *Bellis* v *Challinor* n 21 above at [55]-[56].

to be recognised. To explain, consider the following statement from *Bellis* v *Challinor*,[36] where Briggs LJ observed:

> where it is *not* demonstrated that money apparently advanced by way of loan is *not* to be at the free disposal of the transferee, the ordinary consequence is that the money becomes the property of the transferee, who is free to apply it as he chooses, leaving the lender at risk of his insolvency . . . This is the *true default position,* in which the transfer of the legal title carries with it the beneficial interest.

Thus in *Quistclose* fact patterns, there will typically be a transfer whose usual effect is to vest beneficial title in the recipient. In order to show that a trust has arisen, it will be necessary to oust the default position by demonstrating the presence of trust-consistent characteristics such as restrictions on use and segregation from other assets. Importantly, these are characteristics that embody positive decision-making by the parties. To speak of presumptions of resulting trust or advancement would seem to be inapt,[37] as it will be the intentions of the parties and not the mere fact of transfer that will permit the conclusion that a trust has arisen. On first inspection this may seem to be more consistent with an express rather than resulting trust.

One response is that this misunderstands the role of intention in the creation of resulting trusts, as the Chambers model clearly contemplates that actual intention is relevant but in a negative sense, ie, to show that the transferor did not intend to benefit the recipient.[38] However, even if this model is accepted (and there remains much debate in this regard[39]), there are problems with its application in *Twinsectra*. One relates to what, precisely, is the relevant intention. At a number of points Lord Millett appeared to suggest that the transferor must *intend to create a trust*,[40] and indeed that approach was utilised by the Court of Appeal in *Bellis* v *Challinor* on the authority of *Twinsectra*.[41] However, if resulting trusts are distinct from express trusts, then the relevant intention cannot be an *actual or inferred* intention to create a trust, or else the outcome ought logically to be an express trust.[42] Elsewhere in *Twinsectra* the intention was described by Lord Millett differently: whether 'the parties intended the money to be at the

36 *Bellis* v *Challinor ibid* at [65].
37 For example, Chambers, n 20 above, 83-84.
38 For example, Millett (2011), n 30 above, 10-13. Chambers uses *Hodgson* v *Marks* [1971] 1 Ch 892 to illustrate this general principle. In that case, Mrs Hodgson's attempt to create an express trust over land failed because it was not in writing, however her intention permitted a resulting trust to arise, as it showed that the transfer of legal title was not intended as a gift. Although the outcome was consistent with Mrs Hodgson's original intention, the Court of Appeal did not give direct effect to that intention.
39 Some prominent contributions include W. Swadling, 'Explaining Resulting Trusts' (2008) 124 LQR 72; J. Mee, 'Presumed Resulting Trusts, Intention and Declaration' (2014) 73 CLJ 86.
40 The key examples are Lord Millett's observation that 'a settlor must, of course, possess the necessary intention to create a trust', and his endorsement of the observation that *Quistclose* trusts function in a way similar to a retention of title clause: *Twinsectra* n 2 above at [71], [81]. As Penner observes, '[i]n the vast majority of cases, one would presume that reservation of title arrangements are intentionally entered into by the parties, not that they arise by operation of law': Penner, n 34 above, 55.
41 *Bellis* v *Challinor* n 21 above at [57].
42 Virgo, n 20 above, 255-258.

free disposal of the recipient'.[43] It was not enough that the loan was motivated or made in light of a particular purpose – it was necessary that the recipient's use be restricted.

Does this change in focus sit more comfortably with the conclusion that a resulting trust arises? There are strong arguments that at least in *Quistclose* scenarios, it does not. As explained by Penner:

> This distinction [between express and resulting trusts] is almost scholastic in its unreality. What, in a two party case where A transfers property to B, genuinely distinguishes A's intention that he retain the beneficial interest from A's intention only that B should not have it? If B is not to have it, then who else can A mean to have it except himself?[44]

This article is of the view that where *Quistclose* trusts are grounded in intention, they are better understood as express, as it will generally be the case that the evidence required to demonstrate an absence of an intention to benefit the recipient will simultaneously make the case for an intention by the settlor to retain the beneficial interest for herself.[45] As seen later in this article, the choice between an express and resulting trust characterisation may also be important for regulatory reasons. For the normative themes being developed for now, two key observations arise: first, as articulated in the case law, intention seems to be central to both the express and resulting trust explanations of the *Quistclose* trust; and secondly, under both of these models, judges have been too willing to locate an intention that permits the finding of a trust. This second point is elaborated upon in the next section.

Proving intention

If giving effect to intention is to form a key plank in any normative explanation for the *Quistclose* trust, then it is crucial that intention is taken seriously by judges when determining whether a trust has arisen. Dealing first with the express trust, the orthodox understanding is that the settlor does not need to intend to create a trust as such, so long as her intention is to create something that has the characteristics of a trust.[46] It is therefore not fatal if the word 'trust' is not used, and judges will look for other indicia that are consistent with a trust. For *Quistclose* trusts, these include restrictions on the use of the money (such that it may be applied *only* for the permitted purpose) and segregation of the money from other assets of the borrower.[47] However, when one looks to the case

43 *Twinsectra* n 2 above at [74].
44 Penner, n 34 above, 53, fn 37. For a similar point, see Dal Pont, n 19 above at [27.105].
45 In contrast Chambers has advocated a more nuanced approach in which the existence and characterisation of any given *Quistclose* trust will depend on the circumstances, including the intentions of the parties: see Chambers, n 20 above; R. Chambers, 'Is There a Presumption of Resulting Trust' in C. Mitchell (ed), *Constructive and Resulting Trusts* (Oxford: Hart, 2010).
46 For example, *Paul* v *Constance* [1977] 1 WLR 527; *Twinsectra* n 2 above at [71]; *The Charity Commission for England and Wales* v *Framjee* [2014] EWHC 2507 (Ch) at [28].
47 For example, Virgo, n 20 above, 289-290.

law – especially in England – there are instances where the evidence of intention has been limited or has tended *against* the finding of a trust.

Three examples will be explored at this point,[48] the first of which is *Quistclose* itself.[49] Recall that Lord Wilberforce accepted that there was a mutual intention that the loan moneys not become part of Rolls' general assets, and that this finding was crucial to the conclusion that a trust arose. However, it is not obvious that this is the best interpretation of the facts. Quistclose was not some chequebook-wielding knight in shining armour; rather, it was another company of John Bloom, the man who was the 'moving spirit'[50] behind Rolls, having taken over the company a few years previously as a vehicle for his washing machine business. With sales falling and Rolls in a precarious financial position, Mr Bloom was negotiating with 'Mr X' for financial accommodation, and it was a precondition of the proposed loan that the recently-declared dividend be paid.[51] Quistclose itself had to borrow the money that was loaned to Rolls, and it appears that Mr Bloom was either the source of those funds or acted as intermediary in obtaining them. It also seems that Mr Bloom had 'such confidence that all would be well' that, having arranged the loan, he went on a trip to Bulgaria.[52] However, the financial position was sufficiently bad that the board of Rolls (*sans* Mr Bloom) accepted advice that the company be voluntarily wound up. At that point the Quistclose loan had only just been deposited in the separate bank account, and the dividend had not been paid to the shareholders.

These facts are not immediately suggestive of any intention by Quistclose to create a trust, and indeed might point in the direction of a hasty loan arrangement made by entities within the John Bloom family of companies to keep the Mr X finance in play.[53] The main evidence that is consistent with a trust comes from a resolution passed by the board of Quistclose and from correspondence between Rolls, Quistclose and the Bank. But even here the evidence is equivocal. The relevant documents were described in greatest detail in Harman LJ's opinion in the Court of Appeal. This account suggests that: (i) the board of Quistclose resolved to make a loan to Rolls 'for the purpose of that company paying the final dividend due on July 24 next';[54] (ii) the board intended that this payment be subject to the additional finance being secured,

48 Other cases in this article also involve a trust being recognised despite weak evidence of intent, most notably the (probably purpose) trust in *Re EVTR*: discussed at n 119 below.

49 For a brief overview of the facts, see n 15 above.

50 *Quistclose* n 1 above, 578.

51 These facts, including the pseudonym Mr X, are set out in the opinions of Harman and Russell LJJ in *Quistclose Investments Ltd* v *Rolls Razor Ltd (in liquidation)* [1968] 1 Ch 540, 549, 561-562 (*Quistclose (CA)*). The identity of Mr X has been revealed as Sir Isaac Wolfson: R. Stevens, 'Rolls Razor Ltd' in Swadling (ed), n 13 above, 5.

52 Stevens, *ibid*, 5.

53 See also, *Quistclose Investments Ltd* v *Rolls Razor Ltd (in liquidation)* [1967] 1 Ch 910, 915-916 (*Quistclose (Ch)*), where counsel for Rolls (ie, the liquidators) suggested that that if 'through inadvertence or mistake the company had declared a dividend which it could not pay it might well be good business to borrow money to pay the dividend from a man who was not going to ask for it back in a hurry.'

54 *Quistclose (CA)* n 51 above, 550 *per* Harman LJ.

and that if this condition was not met by July 24, the money would be repaid;[55] (iii) Rolls arranged for a separate bank account to be opened, into which the proceeds of the cheque were credited;[56] and (iv) Rolls and the bank agreed, as confirmed in a letter dated July 15, that 'the account will only be used to meet the dividend due on July 24, 1964'. In the House of Lords, Lord Wilberforce stated that the July 15 letter was 'before transmission to the bank . . . sent to [Quistclose] under open cover in order that the cheque might be (as it was) enclosed in it.'[57] This contradicts the facts as described elsewhere (namely that Rolls sent the cheque and covering letter to the Bank[58]), however, even if Quistclose did see or approve the letter, one must recall that the letter pertained to arrangements *between Rolls and the Bank* regarding the new account.

Thus it would seem open to conclude that Quistclose, motivated by a desire to help Rolls recover from its financial difficulties, made a loan that would enable the dividend to be paid, repayment being due on 24 July if further finance was not obtained by that date, or at some later point if it was.[59] However, by finding a mutual intention that the loan be used for this payment *and no other purpose*, Lord Wilberforce paved the way for the recognition of a trust. A similar conclusion was reached in the Court of Appeal. The attraction of this result was particularly evident in the reasons of Russell LJ, who in discussing whether the Bank had notice of the trust, observed that if the Bank believed that Quistclose had not restricted the use of the moneys this would 'surely be for [the Bank] to place Quistclose in the lunatic fringe of the business world.'[60] There may be good reasons why a rational third party lender would, in this scenario, seek to limit the use of the loan. However, Quistclose was not an independent entity, and furthermore we must take great care, when considering whether an *intentional* trust has arisen, not to be swayed by our own perceptions of what a rational actor would have done, especially for sophisticated repeat players like those in *Quistclose*.

Compared with *Quistclose*, *Twinsectra* provides an even stronger example of judges being too quick to find that a trust arose. It has been argued that Lord Millett's characterisation of the *Quistclose* trust as resulting facilitated this error,[61] and there may be truth to this. However, even in the Court of Appeal, where the analysis sat (at least in part) within an express trust framework, it was held

55 *ibid*. This appears not only from the resolution of the Quistclose board dated 15 July 1964, but from a letter of the same date signed by Mr Cass, director of Quistclose, and sent to Rolls (and copied to the Bank). In the letter, the language used was of the money being 'returnable to us' if the further finance was not forthcoming by 24 July.

56 Note also that the trial judge accepted that there was no condition that the money be paid into a separate account: *Quistclose (Ch)* n 53 above, 926.

57 *Quistclose* n 1 above, 580.

58 *ibid*, 579.

59 See the submissions of Rolls described in *Quistclose (Ch)* n 53 above, 914.

60 *Quistclose (CA)* n 51 above, 563 *per* Russell LJ. Whilst Harman LJ accepted that Mr Bloom arranged the loan through Quistclose and that Quistclose had borrowed the money, he stated at 549 that the source was 'immaterial'.

61 For example, Penner, n 34 above, 54-56; Dal Pont, n 19 above at [27.105].

that a trust arose.[62] As such, the difficulties in the analysis of intention seem to be common to the express and resulting trust models.

The pertinent facts were as follows. Mr Yardley, a property developer, required bridging finance of £1m for the purchase of land at Apperley Bridge and was negotiating for such a loan from Barclays. Worried about delays at the bank's end, Mr Yardley asked a financial advisor for assistance in locating an alternative lender. The advisor put Mr Yardley in touch with Twinsectra, who agreed to help. No security was required by Twinsectra save for a solicitor's personal undertaking that the loan would be repaid. When Mr Yardley's usual solicitor refused to give such an undertaking, Mr Yardley suggested it might instead be given by another lawyer, Mr Sims. In the meantime Barclays came through with the bridging finance, however, Mr Yardley decided to proceed with the Twinsectra loan, for reasons connected to existing business dealings with Mr Sims which resulted in the latter owing Mr Yardley a large sum of money.[63] The plan – which was not communicated to Twinsectra – was that Mr Sims would receive the £1m on his own account and apply it to the debt owed to Mr Yardley. Not long after, the loan was effected and the money applied to various purposes as per Mr Yardley's instructions. Twinsectra was never repaid, with Mr Sims going bankrupt not long afterwards. Twinsectra brought proceedings against Mr Yardley and other parties, pleading various causes of action, some of which were founded on a breach of trust by Mr Sims. To make these out, Twinsectra needed to demonstrate that its loan was subject to a *Quistclose* trust.

Both the Court of Appeal and House of Lords agreed that the loan was impressed with a trust, departing from the conclusion of Carworth J at trial that no such trust had arisen. Despite divergence in the reasoning, in the three key opinions – of Potter LJ, Lord Hoffmann and Lord Millett – intention was crucial to the conclusion that a trust had arisen. There was also consensus that intention was to be assessed objectively, meaning that the subjective viewpoint of the transferor (in terms of whether she appreciated that she was creating a trust) was irrelevant.[64] In *Twinsectra*, the key evidence used to demonstrate the requisite intention was the solicitor's undertaking drafted by Twinsectra and

62 *Twinsectra* v *Yardley* [2000] Lloyd's Rep PN 239 at [75] (*Twinsectra (CA)*). Potter LJ stated, first, that the primary trust in a *Quistclose* scenario is a purpose trust in which the beneficial interest is 'in suspense' until applied for the designated purpose. His alternative explanation, if this was wrong, adopted without citation the approach suggested by Chambers, n 32 above, ch 3: the borrower receives the money beneficially but subject to the equitable right of the lender to prevent its misapplication.

63 The scheme promoted by Mr Sims sought to secure payment of a US$49.2m debt owed by the Nigerian Ministry of Aviation and Transport under an engineering contract, that debt having been assigned to another entity. Mr Sims asked Mr Yardley to help contribute towards financial inducements to be paid to government officials to encourage payment of the debt. Particulars of this venture – which turned out to be a scam – are set out in the trial decision of Carnworth J: *Twinsectra Ltd v Yardley* [1996] Lexis Citation 2683 (20 December 1996) (*Twinsectra (QB)*).

64 *Twinsectra (CA)* n 62 above at [17], [92]-[93]; *Twinsectra* n 2 above at [71]. Similar statements appear in the Australian case law: intention to create a trust must be gleaned from 'outward manifestations' rather than subjective beliefs, ie, 'what is the meaning of what the parties have said?' and not 'what did the parties mean to say?': *Raulfs* v *Fishy Bite Pty Ltd* n 27 above at [48]. See also *Legal Services Board* v *Gillespie-Jones* n 27 above at [119] *per* Bell, Gageler and Keane JJ; *Coolbrew Pty Ltd* v *Westpac Banking Corporation* [2014] NSWSC 1108 at [52], affirmed in [2015]

given by Mr Sims, the undertaking including items regarding retention (that the loan moneys will be retained 'until such time as they are applied in the acquisition of property on behalf of our client') and exclusive use (the loan moneys will be used 'solely' for the acquisition of property 'and for no other purpose').

However, other elements of the transaction pointed against a trust. First, there was no requirement that Mr Sims keep the money separate from other funds received by him, and the loan was paid into his firm's client account. Secondly, the purpose of the loan was described in vague terms. The phrase 'acquisition of property' could refer to all manner of applications (land, a Picasso, thousands of widgets, etc), and indeed the trial judge – who held that the 'lack of clarity in the undertaking as to what was thought to be the intended use of the loan' was inconsistent with a trust – stated that Apperley Bridge was not considered by Twinsectra to be essential to the transaction, otherwise it would have been recorded in the undertaking.[65] Thirdly, there was evidence that representatives of Twinsectra were suspicious about irregularities with the transaction but did not ask further questions about the use of the funds.[66] Fourthly, the parties to the transaction were experienced commercial players and well-advised throughout – for instance, the business acumen of Mr Ackerman, the moving spirit behind Twinsectra, was reflected in Potter LJ's description of him as 'a man of substance who was able to lend money on a short-term basis'.[67] One might therefore expect the parties to have included unambiguous trust language if this was intended. Finally, and perhaps explaining the fourth point, the trial judge found that Mr Atherton subjectively understood the loan to be 'secured' solely by a solicitor's personal undertaking.[68] If this seems risk-tolerant for a loan of such magnitude, one must remember that Twinsectra also insisted upon an interest rate of 24 per cent. Thus, whilst the undertakings given by Mr Sims had some trust-consistent qualities, the facts were more consistent with the conclusion of the trial judge that no trust arose, at least not any trust explained by intention.

The final decision to be analysed at this stage is that of Evans-Lombe J in *Cooper* v *PRG Powerhouse Ltd*. Mr Cooper was Powerhouse's Managing Director. He purchased a car from Godfrey Davis on credit, with the instalments being paid by Powerhouse under Mr Cooper's remuneration package. Following Mr Cooper's resignation, an agreement was reached to discharge the credit agreement, pursuant to which Powerhouse would contribute £3,000 and Mr Cooper the balance of just over £34,000. Rather than paying this

NSWCA 135. The High Court of Australia has also preferred an objective test for ascertaining party intention in non-*Quistclose* scenarios: see *Byrnes* v *Kendle* [2011] HCA 26, especially the joint judgment of Heydon and Crennan JJ.

65 See *Twinsectra (QB)* n 63 above; findings also described in *Twinsectra (CA) ibid*, 248.

66 For instance, when Mr Serota, solicitor for Twinsectra, asked replacement solicitor Mr Sims why he was prepared to give a personal undertaking to repay the loan, the answer given was that 'his client was a very wealthy individual'. This lead Mr Serota to make a file note recording his concern that the transaction was 'unconventional': *Twinsectra (CA) ibid*, 244.

67 *ibid*, 243-244. Indeed, Mr Ackerman was so substantial that within a week of the initial approach, he had authorised the transfer of £1m to Mr Sims' bank account.

68 *ibid*, 255.

sum direct to Godfrey Davis, Mr Cooper made it to Powerhouse, asserting in a witness statement that this arrangement was 'purely for convenience.'[69] Powerhouse entered into administration before the on-payment had cleared. Citing extensively from Lord Millett's decision in *Twinsectra*, Evans-Lombe J held that Mr Cooper's payment was 'impressed with a purpose trust'[70] and that Mr Cooper could trace this sum into Powerhouse's current account. Significantly, this conclusion was reached in the absence of explicit trust language or an express direction that the money could *only* be used to pay Godfrey Davis, and despite the commingling of Mr Cooper's payment with other funds when it was paid into Powerhouse's payroll account. Evans-Lombe J stated that the guiding question – whether the arrangements were such that 'it was understood by the recipient that [the payment] was not at his free disposal'[71] – could be answered in the affirmative because:

> [i]f not express *there was clearly to be implied* into the arrangement that neither Mr Cooper nor [Powerhouse] regarded the amount of the payment as part of the assets of the company at its 'free disposal' and available, in particular, as working capital or for payment of its creditors.[72] (emphasis added)

At this point the reasoning of Evans-Lombe J was fairly brief, however, if one looks at the classic principles for implication of terms – for instance that the proposed term is necessary to give business efficacy to the contract, is so obvious it goes without saying, etc – one might ask whether the term recognised by Evans-Lombe J truly satisfied these limbs.[73] As Lord Bingham observed in *Philips Electronique* v *BSB*, the implication of terms is an 'extraordinary power' which is subject to 'strict constraints' because it involves 'the interpolation of terms to deal with matters for which, ex hypothesi, the parties themselves have made no provision'.[74] Furthermore, because implication of terms often occurs *after* the reaching of some 'crisis', it takes place with the benefit of hindsight, making it 'tempting, but wrong' for the court to 'fashion a term which will reflect the merits of the situation as they then appear'.[75] In the trusts context, these statements accord with the warning of Briggs J in *Pearson* v *Lehman Brothers* that 'the law should not unthinkingly impose a trust where

69 *Cooper* v *PRG Powerhouse* n 14 above at [3].
70 *ibid* at [24]. As stated at n 14 above, it does not seem that this reference to 'purpose trust' was intended to be significant doctrinally.
71 *ibid* at [15].
72 *ibid*.
73 See *BP Refinery (Westernport) Pty Ltd* v *Shire of Hastings* (1977) 16 ALJ 363. Recently, there has been a considerable amount of judicial activity in relation to contract construction, including the implication of terms. Some statements by Lord Hoffmann have been thought to countenance a significant shift in approach (for example, in *Attorney General of Belize* v *Belize Telecom Ltd* [2009] 1 WLR 1988), however, the existing approaches have been confirmed, as has the continued relevance of cases like *BP Refinery*: For example, *Marks and Spencer* v *BNP Paribas Securities Services Trust Co (Jersey) Ltd* [2016] AC 742 *per* Lord Neuberger. For further discussion, see J. S. Getzler, 'Interpretation, Evidence, and the Discovery of Contractual Intention' in S. Degeling, J. Edelman and J. Goudkamp (eds), *Contracts in Commercial Law* (Sydney: Thomson, 2016).
74 *Philips Electronique Grand Public SA* v *British Sky Broadcasting Ltd* [1995] EMLR 472, 481.
75 *ibid*, 482.

purely personal rights between A and B sufficiently achieve their commercial objective.'[76]

In *Cooper*, Evans-Lombe J's findings in relation to the terms of the arrangement were central to the recognition of a trust. Although the decision focused mostly on the events following Mr Cooper's resignation in order to ascertain the intentions of the parties, the low threshold to establish a trust hinted at the influence of other considerations, perhaps relating to the perceived harshness of the opposite result (ie, no trust) to Mr Cooper. Indeed, Evans-Lombe J cited with approval statements of Lord Millett in *Twinsectra* regarding the trust and confidence reposed in borrowers in *Quistclose* scenarios.[77] The helpfulness of unconscionability and fairness as normative explanations for the *Quistclose* trust will be addressed in the next part of the article. For now, it can be noted that *Cooper* involved bare levels of trust-consistent indications.

Is intention a sufficient explanation?

The section above explored an empirical objection to invoking intention as a normative explanation of the *Quistclose* trust: that judges do not take intention seriously. But to the extent this is a problem (and bearing in mind the key examples come from English judges[78]), it can be corrected through a shift in judicial attitude. This section therefore explores a philosophical concern: even if judges assess intention using a sufficiently exacting standard, does that provide a compelling justification for the *Quistclose* trust? This section will focus on the argument that *Quistclose* trusts are express, with the resulting trust account discussed in the third part of this article.

In answering this philosophical question, it is necessary to start by considering the rationales for the express trust. Reviewing the accounts in the leading texts, it can be seen that many authors focus on the characteristics and potential powers of the trust. Michael Bryan and Vicki Vann cut through the detail with characteristic efficiency, describing the express trust as 'a form of wealth management.'[79] Elsewhere, the express trust is lauded for its flexibility and its capacity to permit forms of asset-holding that are not possible through outright gifts and contractual arrangements.[80] The trust is therefore identified as having applications in estate planning and investment, and as allowing such things as the appointment of expert trustees, asset partitioning, and the joint-management of assets for large groups of people.[81] Simon Gardner seeks to place these powers within a broader framework by describing the express trust

76 *Pearson* v *Lehman Brothers Finance SA* [2010] EWHC 2914 (Ch) at [225]; also [261].
77 *Cooper* v *PRG Powerhouse* n 14 above at [18], quoting *Twinsectra* n 2 above at [76].
78 cf Dal Pont, n 19 above at [27.105] (stating that the express trust characterisation in Australia has resulted in judges focusing heavily on indicia of intention); *Ontario (Minister of Training, Colleges and Universities)* v *Two Feathers Forest Products LP* 2013 ONCA 598 (*Two Feathers*) (setting narrow parameters for the *Quistclose* trust, and noting fairly limited reception in Ontario).
79 M. Bryan and V. Vann, *Equity and Trusts in Australia* (Melbourne: CUP, 2012) at [13.1].
80 For example, Penner, n 21 above at [1.16], [2.2], [3.1]; G. Thomas and A. Hudson, *The Law of Trusts* (Oxford: OUP, 2nd ed, 2010) at [1.69].
81 For example, Dal Pont, n 19 above at [16.45]; Virgo, n 20 above, 50-2.

as a 'facilitative device', ie, 'a facility of which people may take advantage if they desire to achieve the results it entails'.[82] He states that this can be supported by a liberal understanding of property in which the personal autonomy of the owner is maximised by affording that individual 'the greatest possible freedom as to how he may intentionally give it away.'[83]

However, as Gardner notes, trusts can be used for desirable and undesirable purposes, meaning that a liberal conception grounded in autonomy does not offer a full account of the legal framework – other policy levers may need to be pulled to reflect other concerns.[84] For instance, a settlor may structure a trust in a way that minimises liability to pay tax, a common situation that requires us to form a view about when the law should, in effect, sanction such conduct through validating the creation of a trust. Similarly, *Quistclose* trusts effect a major change to the rights and remedies of the lender upon the bankruptcy of the borrower. This requires us to consider the interaction between laws governing trusts, security interests and insolvency, for instance if and when courts should recognise an interest that has the effect of taking a creditor outside the statutory framework for asset distribution during liquidation.

In this regard, it is significant that in many cases on the *Quistclose* trust, the judicial analysis has been directed almost exclusively towards doctrinal matters and the assessment of party intention, with questions of policy either overlooked or afforded the briefest of discussion.[85] For instance, Lord Hoffmann's judgment in *Twinsectra* provided no illumination of the desirability or implications of the *Quistclose* trust, instead focusing on the doctrinal ramifications of the 'very unusual' undertaking given by Mr Sims.[86] In *Re Australian Elizabethan Theatre Trust*, Gummow J wrote an involved analysis of the history and nature of the *Quistclose* trust, but spent little time on normative matters. He did not seem perturbed by the observation that the recognition of a trust may expose a gap in the law on unregistered charges, responding that insolvency law 'did not strike' at transactions such as the one in *Quistclose* because the money never became the beneficial property of the borrower.[87] However, this observation tells us nothing about whether judges should recognise what is, in effect, a security interest; it merely summarises the legal conclusion.

To be clear, if a transaction unambiguously satisfies the requirements for an express trust and there are no relevant statutory restrictions, it may be that the only conclusion that is reasonably open to a judge is that a trust arose. However, we should not pretend that such a conclusion is free of any normative dimension, or that judges enjoy no discretion when applying the relevant tests of party intention. Furthermore, whilst it may be difficult to support the extreme regulatory response of invalidating all *Quistclose* trusts, there are persuasive arguments in favour of a less intrusive form of regulation,

82 S. Gardner, *An Introduction to the Law of Trusts* (Oxford: Clarendon, 3rd ed, 2011) 31.
83 *ibid*, 32.
84 *ibid*, 32-53, dividing these concerns into four categories: paternalistic considerations; communitarian concerns; utilitarian considerations; and rights concerns.
85 See also Rickett, n 6 above, noting the volume of 'methodological' reasoning in *Quistclose* cases, especially amongst English judges.
86 *Twinsectra* n 2 above at [12]-[17].
87 *Re Australian Elizabethan Theatre Trust* n 13 above, 691-692.

for instance through a requirement of registration. As Gardner observes – and as will be expanded upon in the fourth part of the article – the provision of money subject to a *Quistclose* trust:

> . . . gives a false appearance of creditworthiness: the other creditors may have been led to perceive the debtor as a viable concern with adequate resources available to meet its liabilities, when in reality these resources are already bespoken under trust arrangements. [However, some] judicial decisions have begun and ended with facilitative logic, little or no visible attention being paid to the question whether the arguable injury to creditors warrants limiting the freedom to make trusts in this respect.[88]

To conclude, whilst there has been a focus on party intention in the case law, this provides *at best* an incomplete justification for the *Quistclose* trust. This article therefore turns in the next section to consider three other justifications that can be made for a trust, grounded in the prevention of unconscionable conduct, the promotion of fairness, and the incentivisation of desirable transactions.

OTHER JUSTIFICATIONS

Unconscionability

This article will first consider unconscionability as an alternative justification for the *Quistclose* trust. Lord Wilberforce did not use such language in *Quistclose*, although he did refer to the arrangements giving rise to a 'relationship of a *fiduciary character* or trust',[89] which may be consistent with such a justification. In contrast, other judges have made explicit use of conscience-related ideas.

An initial question is whether unconscionability is a stand alone justification or whether it merely restates or explains an intention-focused approach. To illustrate, consider *Carreras Rothmans* v *Freeman Matthews Treasure*, in which the defendant undertook advertising services for the plaintiff, a tobacco company. The parties had an arrangement whereby the defendant would book advertising slots for the plaintiff, and the plaintiff would transfer funds to pay for those placements prior to the debts falling due.[90] When the defendant was experiencing financial difficulties, the parties came to an arrangement whereby this money was paid into a separate bank account to be used only for the payment of advertising fees incurred for the plaintiff. The defendant went into voluntary liquidation with invoices having not been paid, and the plaintiff – in order not to prejudice its advertising campaign, and to maintain favourable prices negotiated by the defendant – paid these debts itself, taking an assignment of the rights of the third party creditors. It then sought orders for the repayment of the money in the separate bank account on the basis that this money was

88 Gardner, n 82 above, 39.
89 *Quistclose* n 1 above, 580 (emphasis added).
90 These debts were incurred by the defendant on its own behalf and not as agent of the plaintiff: Carreras n 12 above, 211.

held on trust. In holding in favour of the plaintiff,[91] Peter Gibson J observed that although the case departed from *Quistclose* by involving payment of an antecedent debt rather than making a loan, the underlying principle was that:

> equity fastens on the conscience of the person who receives from another property transferred for a specific purpose only and not therefore for the recipient's own purposes, so that such person will not be permitted to treat the property as his own or to use it for other than the stated purpose.[92]

Significantly, however, Peter Gibson J also described the separate bank account as akin to a 'conduit pipe' and stated that it was 'clearly intended that the moneys once paid would never become the property of the defendant.'[93] It might therefore be said that *Carreras* was an iteration of an intention-focused analysis in which conscience was invoked to help explain why it was wrong for the defendant to depart from the restrictions on the use of money, those restrictions having arisen at the instigation of the parties. This would also be consistent with the proposition that unconscionability operates as an explanatory principle across equity, including in relation to the creation of express trusts.[94] There are, however, a number of questions. An initial one is what, precisely, makes *Quistclose* scenarios different from other instances in which commercial parties are limited to remedies in contract. If the answer is that the parties intended to set up a trust, then one might ask what additional doctrinal or normative dimension is added by referring to conscience. In this regard, one danger is that unconscionability is used in many ways in equity – including to explain many constructive trusts – meaning that reference to conscience in the *Quistclose* context might help facilitate the imposition of trusts in circumstances where there is weak evidence of party intention.

This risk was foreshadowed in this article in the analysis of *Cooper* above,[95] and is also illustrated by Lord Millett's decision in *Twinsectra*, where a trust was held to arise despite two well-advised commercial players entering into a transaction whose loan documentation made no explicit mention of a trust and which was understood subjectively by the lender to involve no security beyond a solicitor's personal undertaking. In concluding that a resulting trust arose immediately on transfer, Lord Millett deployed conscience-based ideas to explain the invocation of equitable principles:

> Equity's intervention is more principled than this. It is unconscionable for a man to obtain money on terms as to its application and then disregard the terms on

91 Albeit on the basis of the assignment and not that the plaintiff was itself the beneficiary under the trust: *ibid*, 223.

92 *ibid*, 222.

93 *ibid*, 220; similarly 221, 222.

94 Especially Lord Browne-Wilkinson in *Westdeutsche Landesbank Girozentrale* v *Islington LBC* [1996] AC 669, 705, observing that equity 'operates on the conscience of the owner of the legal interest' with the effect that a person 'cannot be a trustee of property if and so long as he is ignorant of the facts alleged to affect his conscience' which in the case of express or implied trusts is that 'he is intended to hold the property for the benefit of others'.

95 n 69 to n 77 above.

> which he received it. Such conduct goes beyond a mere breach of contract ... The duty is fiduciary in character because a person who makes money available on terms that it is to be used for a particular purpose only and not for any other purpose thereby places his trust and confidence in the recipient to ensure that it is properly applied. This is a classic situation in which a fiduciary relationship arises, and since it arises in respect of a specific fund it gives rise to a trust.[96]

Lord Millett did not provide any further account of the 'trust and confidence' reposed in *Quistclose* scenarios and why it is different from other promises that are protected only through the law of contract. Earlier in his judgment he said that the loan of money for a stated purpose will not necessarily generate a trust, as this is a common practice by lenders and will not, of itself, displace the default position that the money is received by the borrower absolutely.[97] 'The question in every case', he continued, 'is whether the parties intended the money to be at the free disposal of the recipient'.[98] Writing extra-judicially in 2011, Lord Millett repeated the view – which he described as 'elementary' and 'of long standing' – that a recipient who uses loaned property 'for some other purpose than the one for which it was entrusted to him ... betrays the confidence reposed in him. That is what makes such conduct unconscionable.'[99] Again, however, Lord Millett did not address the normative question of what differentiates the abuse of confidence in *Quistclose* scenarios from other instances where the lender's only legal recourse is through contract. As noted above, if the answer relates to intention, it is questionable what unconscionability adds to the analysis. Similar observations have been made by Lord Mustill in *Re Goldcorp*, in relation to arguments that investors retained a proprietary interest in moneys used to purchase gold by virtue of the (now insolvent) seller of the gold being a fiduciary.[100] Having rejected the contention that there was a trust over the purchase moneys on the basis that there was nothing in the sales contract to constrain the seller's use of those moneys, Lord Mustill stated:

> The same insuperable obstacle stands in the way of the alternative submission that the company was a fiduciary. If one asks the inevitable first question – What was the content of the fiduciary's duty? – the claimants are forced to assert that the duty was to expend the moneys in the purchase and maintenance of the reserved stock. Yet this is precisely the obligation which, as just stated, cannot be extracted from anything express or implied in the contract of sale and the collateral promises. In truth, the argument that the company was a fiduciary ... is no more than another label for the argument in favour of an express trust and must fail for the same reason.

96 *Twinsectra* n 2 above at [76].
97 *ibid* at [73].
98 *ibid* at [74].
99 Millett (1985), n 30 above, 14.
100 *In Re Goldcorp Exchange Ltd (in receivership)* [1995] 1 AC 74. Briefly, under the relevant sales contracts, the seller retained possession of the gold and stored it for the investors. The investors, in turn, received certificates of title that purported to confirm their ownership. The Privy Council held that the investors could not assert a proprietary interest in the gold in the seller's possession as it was held as an unascertained bulk. Alternative arguments were therefore made, including that the investors had a continuing interest in the purchase moneys.

In a recent article, Timon Hughes-Davies explores an alternative justification for the imposition of fiduciary duties in *Quistclose* fact patterns.[101] He argues that with the exception of *Twinsectra*, which was (on his model) wrongly decided, cases recognising *Quistclose* trusts have involved: (i) a lender with a particular interest in the performance of the agreed purpose of the loan, over-and-above the usual interest of a commercial lender in being repaid; and (ii) a 'soft' or 'forgivable' loan, for instance involving no interest rate and/or strict repayment schedule.

Hughes-Davies appears to have been inspired by the observation in Lord Millett's 1985 article that in *Northern Developments* the lenders, a consortium of banks, had a 'separate and distinct' interest in seeing that the purpose of the loan was carried out.[102] The loan was intended to provide Kelly, an ailing company, with a working fund from which it could pay new and existing creditors. The overarching motivation of the banks was to keep Kelly trading, there being a concern that Kelly's insolvency could trigger the collapse of the group of companies – all customers of the banks – of which Kelly formed a part. Hughes-Davies suggests that Lord Millett thought this separate interest 'was relevant to determining whether the relationship between lender and borrower was fiduciary or merely contractual.'[103] This may misconstrue the focus of Lord Millett's analysis: determining whether the borrower had a duty or mere power to apply the funds for the prescribed purpose. In Lord Millett's view, the banks in *Northern Developments* had a separate and distinct interest in the creditors being paid, meaning that the borrowers had a *duty* to use the money to pay the debts of Kelly.[104] In contrast, Quistclose did not have a similar interest in the shareholders being paid, so that Rolls had a *power* to apply the money for the specific purpose but was not obliged to do so – although it could not use the money for other purposes.[105]

Hughes-Davies uses the idea of a 'separate and distinct interest' differently: to justify the imposition of fiduciary obligations. As noted above, he argues that in many of the cases in which a *Quistclose* trust has been recognised, the lender had an interest in the 'end result of the transaction' which 'went beyond the normal interest of a commercial lender'.[106] Furthermore, the benefit to the lender comes not from the repayment terms but from the performance of the purpose. Hughes-Davies gives the examples of the lender cementing the happiness of his sister in *Toovey* v *Milne*;[107] John Bloom, moving spirit behind Rolls and Quistclose, keeping the Rolls business afloat in *Quistclose*; the banks in *Northern Developments* seeking 'to protect the loans

101 T. Hughes-Davies, 'Redefining the Quistclose trust' [2015] Conv 26.
102 *ibid*, 28, citing Millett (1985), n 30 above, 278-279 (discussing *Northern Developments* n 12 above).
103 *ibid*.
104 In fact, Lord Millett was of the view that given the existence of the arrangements was communicated to Kelly's creditors, the simple argument (not relied upon by the judge) was that there was an equity in the creditors' favour which prevented the banks from revoking the arrangement: Millett (1985), n 30 above, 278.
105 *ibid*, 284-285.
106 Hughes-Davies, n 101 above, 29.
107 *ibid*. In *Toovey* v *Milne* (1819) 2 B & Ald 683, 106 ER 514, the loan was made to the lender's brother-in-law to enable the latter to pay his creditors and secure release from prison.

they had already made to other companies in the group';[108] the tobacco company in *Carreras* ensuring its advertising campaign was not derailed by financial difficulties at its advertising agency;[109] Mr Barber in *Re EVTR* having an interest in the prosperity of EVTR and in securing future work at that company;[110] and Mr Cooper paying off his company car in *Cooper* v *PRG Powerhouse*.[111] Hughes-Davies states that the imposition of fiduciary obligations is justified by the lender's reliance on the recipient for the achievement of the over-arching purpose:

> If the true nature of the agreement is that B [the borrower] will help A [the lender] to achieve the intended end result, then it can be said that A is trusting B or, perhaps more significantly, relying on B to carry out the agreement: it is this element of trust or reliance that imposes fiduciary duties on B which go beyond the obligation to repay and which gives rise to the Quistclose trust.[112]

One difficulty with this analysis is that we fall back on the issues already discussed: what makes the trust and reliance in *Quistclose* fact patterns different from other contractual arrangements in which equity does not intervene? When the facts of these cases are examined holistically, many have involved rational lenders undertaking a cost-benefit analysis about how to best protect, or further, their commercial interests, in circumstances in which it is not obvious that equity should strengthen their position. For instance, the banks in *Northern Developments* were clearly motivated by a concern that contagion could bring down a group of companies. However, to go a step further to say that they were 'trusting' or 'relying' on the borrowers to pay the creditors of Kelly, *such that those borrowers owe the banks fiduciary duties*, seems at odds with the business of banking, where risk of default is par for the course. Similarly, to take the facts of *Quistclose*, one may question whether fiduciary concepts *really* come to mind when John Bloom Company No 1 makes a loan to help save John Bloom Company No 2.

Even in the antecedent debt cases – *Carreras* and *Cooper* – one might ask why the payors did not simply pay the creditors directly. In *Carreras*, one possibility is that the plaintiff was concerned about loss of the favourable advertising rates negotiated by the defendant, which it estimated would increase its advertising costs by 24 per cent.[113] In *Cooper*, the stated explanation was that it was more 'convenient'[114] for Mr Cooper to pay his component of the balloon payment through Powerhouse rather than direct to Godfrey Davis, although it is difficult to fathom a compelling logistical reason for this statement. Correspondence quoted elsewhere in the judgment referred to Mr Cooper being given the opportunity to purchase the car 'at a reduced price',[115] raising the possibility

108 *ibid*.
109 *ibid*, 28-29.
110 *ibid*, 30. The facts of *Re EVTR* are set out around n 119 below.
111 *ibid*, 30-31.
112 *ibid*, 42.
113 *Carreras* n 12 above, 213.
114 *Cooper* v *PRG Powerhouse* n 14 above at [3].
115 *ibid* at [4], quoting from a letter from Mr Onslow of Powerhouse to Mr Cooper.

that the company could negotiate a better deal, whilst another explanation is that this structure was desirable to reduce the tax payable on Mr Cooper's severance package.

A second difficulty is that some of the 'separate and distinct interests' are banal or generic, such as making a family member happy or keeping ill-defined job prospects alive. Even if we were to accept that such interests are deserving of legal recognition, there is the question of whether the Hughes-Davies approach can be translated into operationalised rules of law. In cases where there is a pre-existing relationship between lender and borrower, it will always be possible to point to *some* special interest, even if that interest is simply the continuation of the relationship. We therefore run the risk of encouraging litigants to retrofit self-serving assertions of their 'separate and distinct' interests in order to justify a trust. In response Hughes-Davies may emphasise other elements of his thesis, such as the borrower-friendly loan arrangements. However, the 'soft loan' thesis cuts both ways: whilst Hughes-Davies may suggest it is trust-consistent, an alternative gloss is that the pre-existing relationship encourages the lender to take the risk of the borrower's insolvency in terms that may not, on their face, seem commercial.

To conclude, there are a number of difficulties in using unconscionability to explain the *Quistclose* trust, difficulties that reflect broader issues with the concept of unconscionability and its capacity to obscure rather than clarify the policy or doctrinal matters being considered.[116] In the *Quistclose* context, we need to take care that unconscionabilty is not being used as placeholder for other (often unarticulated) ideas, and consider the repercussions of moving away from an approach grounded in intention to create a trust. Some of these repercussions will be considered in the next two sections, in relation to fairness and incentivisation.

Fairness

A second justification for the *Quistclose* trust is that fairness demands that the lender get back her money upon failure of the purpose, even if the borrower is insolvent. In addition to concerns about altruistic lenders being left without an effective remedy against insolvent borrowers, a further manifestation of the fairness explanation is that it would be wrong for *other creditors* of the borrower to receive a windfall by virtue of the lender's payment. Given that concerns about unfair gains may evoke unjust enrichment reasoning, this section will also consider an explanation of the *Quistclose* trust grounded in failure of basis.[117]

116 For some recent critiques of the ways conscience is used in equity, see R. Havelock, 'Conscience and Unconscionability in Modern Equity' (2015) 9 J Equity 1; G. Virgo, 'Whose Conscience? Unconscionability in the Common Law of Obligations' in A. Robertson and M. Tilbury (eds), *Divergences in Private Law* (Oxford: Hart, 2016).

117 This explanation might align with the proposition that resulting trusts arise to reverse unjust enrichment: for a summary of such arguments, see R. Chambers, 'Resulting Trusts' in A. Burrows and A. Rodger, *Mapping the Law: Essays in Memory of Peter Birks* (Oxford: OUP, 2006). Although Lord Millett cited Chambers' work on resulting trusts (see *Twinsectra* n 2 above at [92]), he did not discuss arguments in relation to unjust enrichment.

Compared with unconscionability, explicit reference to fairness concepts is not as common in the case law, although one prominent example appears in remarks of Bingham LJ in *Re EVTR*.[118] Mr Barber, a lighting director, had won almost a quarter of a million pounds on premium bonds. He had previously done some work for EVTR, a provider of specialist television services, and was on friendly terms with its personnel. EVTR was in financial difficulty, and the plan was for the company to trade its way out of its difficulties. This required new equipment, which was to be purchased with Mr Barber's financial assistance. The facts at this point become convoluted, although the important points were that: (i) Mr Barber paid £60,000 to EVTR's solicitors; (ii) he later provided a written authorisation to the solicitors permitting the release of the money for the 'sole purpose of buying new equipment'; (iii) EVTR used this money as part of a transaction to buy the required equipment; and (iv) this transaction fell over when receivers were appointed to the company. The seller repaid the money paid by EVTR (less interest and costs), and also took back some equipment supplied to EVTR on a temporary basis pending delivery of the final order. The question asked by the receivers was whether this sum (just under £49,000) formed part of the general assets of EVTR. At trial it was held that by this point the money belonged to the company; in the Court of Appeal, it was held that the sum was held on trust for Mr Barber.

Doctrinally, this case is interesting because of the seeming reappearance of a trust *after* the money had been paid to the seller. The trial judge had held that any trust that had arisen initially came to an end upon such payment, the money having been applied for the prescribed purpose and there having been no agreement as to what would happen if the deal later collapsed. To hold otherwise would constitute a 'substantial extension of the *Quistclose* principle.'[119] On appeal, Dillon LJ described this as blowing the final whistle at half-time: 'in any realistic sense of the words that purpose [ie, buying new equipment] has failed in that the company has never acquired any new equipment.'[120] The repaid money was 'subject to the same trusts as the original £60,000' by virtue of the long-standing principle that:

> if a person who is a trustee receives money or property because of, or in respect of, trust property, he will hold what he receives as a constructive trustee on the trusts of the original trust property.[121]

In the absence of any possibility that the money could be spent on equipment, it was held on resulting trust for Mr Barber.[122] Dillon LJ did not seek to place this reasoning in any explicit normative framework, instead invoking general principle to justify his approach. However, in a short concurring decision,

118 Another example – although perhaps not a strict example of a *Quistclose* case – is *In re Kayford* [1975] 1 WLR 279, discussed below at n 155 and surrounding text.
119 *Re EVTR Ltd* (1987) 3 BCC 382, 388 (*Re EVTR (Ch)*).
120 *Re EVTR* n 2 above, 393 (Dillon LJ).
121 *ibid*, citing *Keech* v *Sanford* (1726) Sel Cas T King 61, 25 ER 223; *Chelsea Estates Investment Trust Co Ltd* v *Marche* [1955] Ch 328.
122 *ibid*.

Bingham LJ pointed to the unfairness of Mr Barber being limited to a personal remedy:

> It would, I think, *strike most people as very hard* if Mr Barber were in this situation to be confined to a claim as an unsecured creditor of the company. While it is literally true that the fund which he provided was applied to the stipulated purpose, the object of the payment was not achieved and that was why the balance was repaid to the receivers. My doubt has been whether the law as it stands enables effect to be given to what I can see as the *common fairness* of the situation. . . . I am *happy to be persuaded* that the sums repaid are to be treated as held on the same trusts as the original £60,000 and, in present circumstances, on a resulting trust for Mr Barber.[123] (emphasis supplied)

It is easy to understand the concern for Mr Barber and his quasi-lottery winnings: on one view of the facts, he had generously helped his friends at EVTR, and it would be unfair for this money to swell the general assets of the company to the benefit of other creditors who were never intended to be the direct recipients of this largesse. This position may be particularly compelling if the creditor that receives the lion's share of the money is a bank or similar lender holding extensive security rights. However, we must be cautious before adopting fairness as a justification for the *Quistclose* trust.

The first issue relates to our assessment of fairness vis-à-vis the lender, including the relevance of their personal characteristics. Ought *all* lenders in potential *Quistclose* scenarios to enjoy the same favourable position? Should we treat one-off private lenders in the same way as specialist institutional lenders? By what yardstick is unfairness to be measured? In *Re EVTR*, for example, Mr Barber acted with the advice of his accountants and kept himself informed of developments at EVTR, for instance by attending board meetings. At first it was planned that Mr Barber would buy the equipment and lease it to EVTR, however, logistical issues caused these plans to change such that Mr Barber would provide a loan to allow the company to purchase the equipment itself. The trial judge held that Mr Barber 'undoubtedly concurred in this new plan'[124] and contemplated that it would make him a 'loan creditor of the company', but did not give any conscious thought to what would happen if the purchase later failed.[125] Furthermore, any normative analysis of Mr Barber's position must take account of a capital restructuring agreement signed by Mr Barber, under which he agreed to purchase £40,000 worth of shares in a holding company that was to take over EVTR. Mr Barber was not just a lender – he was also an investor in EVTR's business. In short, the language of fairness may feel increasingly strained the more we learn about the events and transactions.

Secondly, as soon as we consider what is fair for lenders like Mr Barber, we must also discuss the position of other creditors and the economics of

123 *ibid*, 394 *per* Bingham LJ.
124 *Re EVTR (Ch)* n 119 above, 387.
125 *ibid*, 388.

insolvency.[126] In countries like the UK and Australia there exist statutory insolvency regimes that govern the distribution of assets between various classes of creditor. The details of these schemes vary but can be said to embody decisions about the relative merits of different claims in an attempt to create rules that are generally applicable in terms of their normative basis. In the UK, for example, the relevant rules suggest that employees ought to have their claims preferred to general creditors, and that holders of floating charges should be prevented from hoovering up the assets ahead of all other creditors.[127] If fairness is our guiding principle, one might ask whether it is fair in *Quistclose* situations that cash-rich lenders *always* beat out everyone else, bearing in mind that not all *Quistclose* scenarios involve a corporate rescue and that the creditors may include employees.[128] In truth, the law in this space seems to be the opposite of a fairness-based assessment, relying instead on glib denials of the relevance of insolvency principles because the money never formed part of the general assets of the borrower.

Thirdly, it is questionable whether, in this context, fairness can and should translate into operationalised rules of law to be applied by judges. In addition to embodying policy decisions about the priority of competing claims to an insolvent's assets, a statutory insolvency framework is desirable for other reasons, including to provide a series of *ex ante* rules that help reduce litigation by and against liquidators.[129] One possible repercussion of the *Quistclose* trust – especially if it is grounded in indicators other than clear party intention – is to further disadvantage the borrower's creditors, because the costs of the liquidator seeking judicial directions about a loan or defending a claim will come out of the company's assets, thereby reducing the funds available for distribution. As stated above in relation to unconscionability, if we maintain the view that *Quistclose* trusts are intentional, there is also a capacity for fairness to water down the need for clear evidence of intent. For instance, although the trial judge and Dillon LJ in *Re EVTR* both applied *Quistclose* in finding an initial (probably purpose) trust,[130] it must be questioned whether there were sufficient trust-consistent features for this trust to be intentional rather than imposed.

126 See *Two Feathers* n 78 above at [23]; and in a different context *Moriarty* v *Various Customers of BA Peters Plc* [2008] EWCA Civ 1604 at [19], [21] (Lord Neuberger resisting an argument that would, in effect, create a new class of preferred creditor).

127 Insolvency Act 1986, s 175; for an overview, see E. McKendrick, *Goode on Commercial Law* (London: Penguin, 4th ed, 2010) ch 31.

128 For example, in *Two Feathers* n 78 above, the relevant sum took the form of a grant advanced by Ontario's Minister of Training Colleges and University to Two Feathers Forest Products, a First Nations limited partnership. The funding agreement contained a number of requirements, including that the money could only be used in accordance with the project as set out in the agreement. At trial it was held that unspent money was subject to a *Quistclose* trust in favour of the Ministry, a conclusion overturned by the Ontario Court of Appeal.

129 This connects to the literature on the respective merits of standards and rules as a way of drafting law: For example, I. Ehrlich and R. A. Posner, 'An Economic Analysis of Legal Rulemaking' (1974) 3 J Legal Studies 257; L. Kaplow, 'Rules versus Standards: An Economic Analysis' (1992) 42 Duke LJ 557.

130 *Re EVTR (Ch)* n 119 above, 388; *Re EVTR* n 2 above, 392.

A final question is whether normative concerns about unfair windfalls might provide support for the resulting trust analysis of Lord Millett in *Twinsectra*. As hinted at in the beginning of this section, *Quistclose* trusts have been seen as a response to unjust enrichment brought about by failure of basis.[131] However, even if failure of basis explains the *Quistclose* trust – and there are questions about whether it is consistent with the *immediate* appearance of a resulting trust, if the basis of the transaction is still intact – it has been emphasised that this unjust factor is an instance of qualified intention and not the manifestation of public policy concerns or palm-tree justice. Indeed there have been concerns about replacing unjust enrichment analysis with concepts like unconscionable conduct, as seen in Peter Birks' criticism of the judgment of Gummow J in *Roxborough* v *Rothmans of Pall Mall*.[132] This critique reflected Birks' view that the word 'unjust' in unjust enrichment is 'only weakly normative', for the most part 'merely [gathering] up the law's reasons . . . why an enrichment should be given up to a person at whose expense it was received.'[133] That is, it is only unconscionable to retain an enrichment because there is *some other reason* why it ought to be given back. 'It is the obligation to make restitution which renders retention unconscientious', Birks said, 'Unconscientiousness *ex post* clearly has no explanatory weight.'[134]

It is not the view of this article that standards such as fairness or unconscionability ought never to serve as legal tests; on the contrary, there are many contexts in which justice is best achieved by a fact-responsive, open-textured doctrine applied *ex post* by a judge.[135] However, in the *Quistclose* context, the issue is that these concepts either add little to an intention-focused approach or have not been properly developed in the case law. Indeed, if fairness or unconscionability is our driving concern, doctrinal considerations and intellectual honesty may demand that we view the *Quistclose* trust as imposed, and probably as a constructive trust.

Incentivisation

A third justification for the *Quistclose* trust revolves around the proposition that the recognition of a trust encourages desirable transactions, most notably lending to entities that are in financial difficulty. This justification is possible because of the doctrinal understanding that the borrower does not receive absolute title to the loan money, with the result that this money never becomes part of its general assets.[136] This gives the *Quistclose* trust characteristics similar to functional security interests such as retention of title clauses and hire-purchase

131 For example, Bryan and Vann, n 79 above at [22.27]-[22.30].
132 P. Birks, 'Failure of Consideration and Its Place on the Map' (2002) 2 OUCLJ 1, criticising *Roxborough* v *Rothmans of Pall Mall Australia Ltd* [2001] HCA 68.
133 P. Birks, *Unjust Enrichment* (Oxford: Clarendon, 2nd ed, 2005) 274.
134 *ibid*, 6.
135 For example, E. Hudson, 'Implementing Fair Use in Copyright Law: Lessons from Australia' (2013) 25 IPJ 201 (supporting introduction of an open-ended fair use defence in copyright law).
136 For example, *Re Australian Elizabethan Theatre Trust* n 13 above, 692; Stevens, n 51 above, 154-155.

contracts, insofar as it protects the lender against the insolvency of the borrower. Despite enjoying this quality, it is frequently asserted that *Quistclose* trusts are not security interests as there is no *independent* obligation that they secure.[137] It will be necessary return to this argument in the fourth part of this article, as it is relevant to the regulation of such devices. It is clear, however, that any protection against insolvency is not full-blown: once the money has been applied for the permitted purpose, the only relationship that remains (if the original transaction was a loan) is one of debtor-creditor.

At least in the leading English and Australian cases, there has been no explicit reference to incentivisation to justify the recognition of a trust; the highest proposition that can be drawn from the case law is that judges have noted the synergy between *Quistclose* trusts and functional security interests.[138] In *Australian Elizabethan Theatre Trust*, for example, Gummow J cited the suggestion of Professor Finn that such a trust is 'in substance . . . a security device operating for the benefit of the lender',[139] and observed that there may be 'force' in the submission that the *Quistclose* trust exposes a hiatus in the law in relation to the registration of charges.[140] Similarly, in *Twinsectra,* Lord Millett referred to the work of Michael Bridge and Mr Justice Priestley (writing extra-judicially),[141] stating that '[o]n this analysis, the *Quistclose* trust is a simple commercial arrangement akin . . . to a retention of title clause (though with a different object)'.[142] It is therefore not surprising that one proponent of the incentivisation thesis, Michael Smolyansky, describes the *Quistclose* trust as motivated by 'unarticulated policy concerns', namely, the desire to protect lenders – not as a goal in its own right, but rather as a means of promoting lending to entities in financial difficulty.[143]

The incentivisation justification requires a number of empirical and normative claims to be made out, above all that *Quistclose* trusts motivate lending and – assuming that they do – that lenders under *Quistclose* arrangements are deserving targets of equitable intervention. Here reference should be made to Smolyansky's analysis of the policy framework. For Smolyansky, the benefit of

137 For example, Stevens, *ibid*; A. Duggan and D. Brown, *Australian Personal Property Securities Law* (Chatswood: LexisNexis Butterworths, 2012) at [3.12].

138 In *Two Feathers* n 78 above, Feldman JA of the Ontario Court of Appeal observed at [15] that the '*Quistclose* trust concept was originally drawn by Lord Wilberforce in narrowly defined parameters', namely the loan of money in emergent circumstances to allow the payment of certain creditors 'in order to keep the debtor in business.' One criticism made by Feldman JA of *Twinsectra* was that it effected a significant expansion of this concept. In holding that no trust had arisen in relation to the facts before the court (summarised at n 128 above), one relevant matter was that those facts did not have the characteristics of *Quistclose* or, for that matter, *Twinsectra*: at [36].

139 *Re Australian Elizabethan Theatre Trust* n 13 above, 691, citing Priestley, n 8 above, 237, footnote 58.

140 *ibid*, 691-692.

141 *Twinsectra* n 2 above at [80], citing Priestley, n 8 above; Bridge, n 8 above.

142 *ibid* at [81], although Lord Millett also stated at [72]: 'Arrangements of this kind are not intended to provide security for repayment of the loan, but to prevent the money from being applied otherwise than in accordance with the lender's wishes.'

143 M. Smolyansky, 'Reining in the *Quistclose* Trust: a Response to *Twinsectra v Yardley*' (2010) 16 T&T 558, 558.

the *Quistclose* trust (properly conceived) is that it provides a financial 'lifeline' in order to 'rescue a person from bankruptcy or a firm from insolvency':[144]

> There is obvious societal and economic benefit in forestalling bankruptcy where it is feasible to do so, and *thus in encouraging such lending practices.* Yet if potential lenders in these circumstances are not protected then *such loans are unlikely to be made.* For this reason, both the distressed firm's creditors and society as a whole are materially better off if such lenders are accorded, what is in effect, a legally imposed assurance that their money will not disappear into the general pool of funds available to the unsecured creditors in the event of insolvency.[145] (emphasis added)

In Smolyansky's opinion, the misstep in *Quistclose* was for Lord Wilberforce to suggest that the court was responding to the intention of the parties rather than the 'sound' policy concern of protecting the lender. Smolyansky argues that such an approach paved the way for a number of errors in *Twinsectra*, notably the articulation of a loose test of intention,[146] the satisfaction of that test despite weak evidence of intent on the facts,[147] and the permeation of *Quistclose* reasoning into a case that had nothing to do with staving off insolvency.[148] He argues that the recognition of a trust in *Quistclose* was both 'inherently fair and manifestly justified by sound, though unarticulated, policy concerns', and that the only doctrinal characterisation that fits with this rationale is for the *Quistclose* trust to be constructive.[149]

There are, however, inconsistencies in Smolyansky's analysis. For any incentive effect to operate, parties must be *subjectively* aware that a trust will or is likely to arise, as it is only with this knowledge that they will be encouraged to adjust their behaviour. As Jessica Litman has noted in another, very different, context:

> [i]t is difficult to speak of the incentives supplied by a legal regime without relying on the convention that those whom the law seeks to prod are aware of the goodies that it offers as a bribe.[150]

But if there is a subjective desire to take the benefit of a trust, then this would suggest an actual intention to create a trust, and furthermore make it likely that the lender – who is probably sophisticated and will have had access to legal advice in order even to know about *Quistclose* reasoning – will ensure that the loan documentation specifies that a trust arises. This sits uneasily with Smolyansky's view that in *Quistclose* fact patterns, there is no actual intention to retain a beneficial interest.[151]

144 *ibid*, 566.
145 *ibid*.
146 *ibid*, 561.
147 *ibid*, esp 561-562.
148 *ibid*, 566-567.
149 *ibid*, 567.
150 J. Litman, 'Copyright as Myth' (1991) 53 *University of Pittsburg Law Review* 235, 241 (noting the economic justification of copyright law as providing an incentive for creation, but also that many authors are not aware of the existence or details of the law).
151 Smolyansky, n 143 above, 567.

At this point the justification being pressed by Smolyansky seems to morph from incentivisation to one grounded in fairness. He explains:

> In the context of a [Quistclose-type] loan, there is no difficulty in concluding that it would truly be unconscionable for the unsecured creditors, who stood to gain significantly if the purpose of the loan was fulfilled and insolvency was thus avoided, to then claim that, because insolvency was not in fact avoided, that the unexpended loan money should now belong to them. *There is a fundamental inequity in this situation*. For no additional consideration the unsecured creditors would have been rescued if the loan was successful. The retention by them of any unexpended loan money would therefore represent *a windfall profit at the expense of the lender.* A constructive trust is an appropriate mechanism by which to prevent this from occurring.[152] (emphasis supplied)

As noted earlier, if *Quistclose* trusts are a response to unfairness or unconscionability, then it may be appropriate to classify them as constructive. However, an analysis that focuses on the windfall to unsecured creditors rests on an entirely different normative basis to one grounded in the provision of an *ex ante* assurance to lenders. The Smolyansky analysis therefore ends up in essentially the same place as the fairness justification above, and does little to advance the two propositions that an incentives-based justification must demonstrate: that lenders like Mr Bloom (through Rolls Razor) and Mr Atherton (through Twinsectra) are the sort of people who should be the objects of special equitable rights; and that they would be more inclined to lend money in a world that recognises the *Quistclose* trust, rather than a world that merely recognises a whole host of other forms of security interest. Indeed, if we look to the facts of the leading cases, it is questionable whether the lenders were at all concerned about securing their loans. In *Twinsectra*, for example, a far more compelling explanation is that the proximal cause of Mr Atherton's agreement to lend was the 24 per cent interest rate, whilst in *Quistclose*, it appears the loan was necessary to keep the 'Mr X' finance in play.

This is not to say that we can categorically rule out an incentive-based rationale for the *Quistclose* trust. The key difficulties, however, are twofold: first, locating empirical evidence that a rational 'man of substance' behaves as the theory suggests; and secondly, explaining why such lenders are desirable targets of equitable intervention. Anyone seeking to defend *Quistclose* trusts by reference to an incentivisation analysis needs to address both of these issues.

PRACTICAL RAMIFICATIONS

Synthesis of analysis

The foregoing analysis suggests a number of issues in the characterisation of the *Quistclose* trust. One is the lack of a clear basis for the recognition of a trust.

152 *ibid*, arguing by analogy to *Chase Manhattan Bank NA* v *Israel-British Bank (London) Ltd* [1981] Ch 105 (mistaken payment).

This is particularly so in England, where the current approach represents an unsatisfactory halfway house between an express and constructive trust. On the one hand, judges have placed considerable emphasis on locating the intentions of the parties. As discussed in the second part, above, the view of this article is that such intention is best understood positively (ie, as an intention to retain the beneficial interest), meaning that the trust is better characterised as express. On the other hand, judges have often set a low threshold for the evidence required to find a trust, and have used the language of unconscionability and fairness to explain equitable intervention, which is more consistent with such trusts being imposed. A second issue with the *Quistclose* trust is locating a compelling normative explanation for its existence. As seen in the third part of this article, there are difficulties with justifications based on unconscionability, fairness and incentivisation. Perhaps the strongest explanation is that covered in the second part: that *Quistclose* trusts give effect to party intention. However, as noted there, that does not mean that *any* application of the *Quistclose* trust is normatively justified.

This leads to the matters addressed in this final part, which focuses on the practical ramifications of our explanation of the *Quistclose* trust. It may be said that it does not matter how we classify the *Quistclose* trust, so long as there are consistently applied rules regarding its creation. However, express, resulting and constructive trusts arise and are regulated differently, as seen, for example, by the rules on formalities.[153] It is the contention of this article that if it is accepted that intention constitutes an important plank in the doctrinal and normative explanation of the *Quistclose* trust, it is not obvious that we have pressed an intention-focused analysis to its logical conclusion.

Regulation of the *Quistclose* trust

This section will focus on the operation of *Quistclose* trusts in insolvency contexts. Two possibilities will be considered: that *Quistclose* trusts constitute preferences; and that they should be regulated as functional security interests.

Unlawful Preference

Whether a *Quistclose* trust constitutes an unlawful preference will depend on the terms of the trust and the content of the particular legislative insolvency scheme; for instance, the current approach in England is that the alleged preference must have occurred at the 'relevant time' and must have been given by a company 'influenced ... by a desire' to put that creditor, surety or guarantor 'into a position which, in the event of the company going into insolvent liquidation, will be better than the position he would have been in if that thing had not

153 For example, Law of Property Act 1925, s 53 (setting out signed writing requirements for declarations of trust, disposition of subsisting equitable interests, etc, but noting in subsection (2) that this section 'does not affect the creation or operation of resulting, implied or constructive trusts').

been done.'[154] Although arguably not a true *Quistclose* case, the proposition that there was a fraudulent preference was rejected by Megarry J in *In re Kayford* on the basis that the facts did not involve the preferring of creditors but 'preventing those who pay money from becoming creditors, by making them beneficiaries under a trust.'[155] In that case, a company carried on a mail-order business where customers either paid a deposit for their goods or paid the purchase price in advance. There were issues with the company's suppliers, so the managing director arranged for customer payments to be paid into a separate bank account pending delivery of their orders. The aim was that if the company failed, this money would be returned to the customers. The company went into voluntary liquidation, and the question was whether the money in this account formed part of its general assets. Megarry J held that a trust had been created. Given the lack of customer knowledge of these arrangements, the best explanation is that this trust was declared unilaterally by the company.[156]

As noted by Robert Stevens, there are compelling arguments that the declaration of trust did not prevent the customers from becoming creditors, and that 'it is difficult to escape the conclusion that the declaration . . . was a preference according to the wording of the legislation'.[157] However, Megarry J seemed concerned to protect the customers, citing fairness concepts not dissimilar to those in the later judgment of Bingham LJ in *Re EVTR*:

> Different considerations may perhaps arise in relation to trade creditors; but here I am concerned only with members of the public, some of whom *can ill afford to exchange their money for a claim to a dividend in the liquidation,* and all of whom are likely to be anxious to avoid this. In cases concerning the public, it seems to me that where money in advance is being paid to a company in return for the future supply of goods and services, it is *an entirely proper and honourable thing* for a company to do what this company did, upon skilled advice, namely, to start to pay the money into a trust account as soon as there begin to be doubts as to the company's ability to fulfil its obligations to deliver the goods or provide the services.[158] (emphasis added)

As discussed earlier, whilst one might be very sympathetic to attempts to protect ordinary customers, the whole point of a statutory insolvency scheme is to determine the fairest distribution of limited assets between a range of different claimants.[159] A similar point was made by Pincus J in *Re Miles*, who in seeking to limit the *Quistclose* trust to the facts in *Quistclose*, observed:

154 Insolvency Act 1986, s 239. Preference recapture has a long and convoluted history, being developed 'over five centuries or more, from a bewildering array of sources': J. S. Getzler, 'Assignment of Future Property and Preferences' in J. Glister and P. Ridge (eds), *Fault Lines in Equity* (Oxford: Hart, 2012) 83. It remains necessary to pay close attention to the specific text in determining whether a payment is a fraudulent preference.

155 *In re Kayford* n 118 above, 281.

156 For example, Rickett, n 6 above, 609.

157 Stevens, n 51 above, 158; see also Priestley, n 8 above, 233-235.

158 *In re Kayford* n 118 above, 282.

159 This brings to mind the famous statement of Lord Hatherley LC in *Freeman* v *Pope* (1870) LR 5 Ch App 538, 540 that the 'principle on which the statute of 13 Eliz 1, cl 5 [the Fraudulent Conveyances Act 1571] proceeds is . . . that persons must be just before they are generous, and that debts must be paid before gifts can be made.'

> Experience suggests that bankruptcy or the liquidation of an insolvent company often awkwardly interrupts the progress of an intended transaction or set of transactions. If goods are delivered under a contract of sale and the property has passed, but bankruptcy supervenes just before an intended payment is made for them, the vendor cannot get them back. He must submit to their being sold to satisfy the general body of creditors – or perhaps even more galling, to satisfy a secured creditor or one having statutory priority. The common sense claim of such an unpaid vendor to recover 'his' goods rather than prove for the price may be no less appealing than Quistclose's claim to repayment of the money it advanced and the same may be said of any number of types of transactions interrupted by bankruptcy. This illustrates the unwisdom of extending the Quistclose principle to cover more situations in which money or property comes to the bankrupt, in contemplation of a transaction which bankruptcy forestalls.[160]

On the question of whether the 'usual' *Quistclose* trust is a preference, Stevens concludes that there are viable arguments that some payments under *Quistclose* trusts will be preferences. Stevens is particularly scathing of the outcome in *Carreras*, arguing that this was a clear example of one class of creditors (the advertising agency) being preferred over the others, and that '[t]he most that can be said in favour of *Carreras* . . . is that it is a testament to the advocacy skills of leading counsel for the lender.'[161] In contrast, Stevens argues that where the *lender* is paid, she is not preferred as the borrower never received the money beneficially: 'trust money being paid over to a beneficiary is not preferential.'[162] However, this sits uneasily with the policy behind the prohibition on preferences and would seem to rest on the problematic idea, critiqued next, of a demarcation between the lender as a beneficiary and as a creditor.

Security Interest

To illustrate these ideas further, let us turn to the possibility that *Quistclose* trusts ought to be regulated as functional security interests, such that registration may be required to perfect them. This argument will be made with particular reference to the Personal Property Securities Act 2009 (PPSA), which has harmonised and centralised the regulation of security interests in Australia by setting up a comprehensive register of interests over personal property. The reason for focusing on this statute relates to its explicit treatment of the *Quistclose* trust.

Like equivalent legislation in other jurisdictions, the PPSA adopts a functional definition of security interest, capturing transactions which *in substance* secure payment or performance of an obligation.[163] Because the form of the transaction and identity of who has title are both irrelevant, the range of

160 *Re Miles; ex parte National Australia Bank Ltd* v *Official Receiver in Bankruptcy* (1988) 85 ALR 216, 221.

161 Stevens, n 51 above, 163, inserting a cheeky footnote to 'PJ Millett QC'. Mr Justice Priestley has also suggested that this fact pattern would constitute a preference under Australian law: Priestley, n 8 above, 235 (writing in 1987).

162 Stevens, n 51 above, 163; see also 159.

163 PPSA 2009 (Cth), s 12(1).

transactions caught by the PPSA is extensive, including not only traditional security interests such as the charge, mortgage and pledge but also conditional sale agreements, hire purchase agreements, leases of goods, etc.[164] The PPSA therefore, in the words of Anthony Duggan and David Brown, operates 'to take the "quasi" out of "quasi-security"' in relation to these transactions.[165] They state:

> The PPSA equates conditional sale agreements with other forms of security interest because they are functionally equivalent: in all cases, the objective is to give A an interest in B's asset that would allow A to access the asset if B (or a third party) defaulted on an obligation owing to A.[166]

Duggan and Brown observe that a trust that in substance secures payment or performance of an obligation will be caught by the PPSA,[167] but that trusts do not usually have this characteristic:

> [A] security interest depends on a debtor-creditor relationship and, in the usual case, the trust lacks this element. Trusts are most commonly used either for asset management purposes or for the supervised transfer of wealth, rather than access to credit. . . . To state the difference another way, the beneficiary does not hold equitable title to the trust assets to secure an obligation independently owed by the trustee. On the contrary, the beneficiary's interest is a manifestation of the trustee's obligations . . .[168]

We might ask whether this reasoning applies to *Quistclose* trusts, which are commonly overlaid on a debtor-creditor relationship. If such trusts are set up intentionally in order, *inter alia*, to give the lender access to an asset in the event of the borrower's insolvency, then what makes them qualitatively different from a retention of title clause? A number of possibilities have been raised in the literature. One reiterates the point above: there must be an obligation independent of the trust, such that an individual with *only* the interest of a beneficiary does not have a security interest.[169] For instance, Stevens argues that in *Quistclose* scenarios, the trust and debt are sequential, ie, at transfer the borrower does not have any repayment obligation – this arises only when the money is applied for the prescribed purpose.[170] Stevens therefore compares a sum which a lender asserts 'is mine to the extent that I remain unpaid'

164 *ibid*, s 12(2) (illustrative examples of transactions that may comprise security interests).
165 Duggan and Brown, n 137 above at [1.30].
166 *ibid* at [3.5].
167 *ibid* at [3.11], noting that it is not fatal that the trust is not in the illustrative list of functional security interests in PPSA, s 12(2). See also Law Reform Commission, *Personal Property Securities: Report No 64 Interim* (ALRC, 1993) at [5.18]-[5.20]; *North Shore City Council* v *Stiassny* [2008] NZCA 522 (observing in obiter that if a trust had arisen, it would have constituted a security interest under the New Zealand PPSA, as the trust was not coterminous with the primary obligation owed to the Council).
168 *ibid* at [3.12].
169 See also, *North Shore City Council* v *Stiassny* n 167 above at [29].
170 For example, Stevens, n 51 above, 165-166; see also *Quistclose* n 1 above, 581 (in relation to the co-existence of legal and equitable rights in the same transaction) and J. Glister, 'The Role of Trusts in the *PPSA*' (2011) 34 UNSWLJ 628, 641-642.

(a security interest) with one that is 'mine to the extent that you have not used it for the designated purpose' (not a security interest).[171] Duggan and Brown make a similar point when they say that, for *Quistclose* trusts, 'the purpose of the trust is not to secure [the borrower's] payment obligation but . . . to ensure fulfilment of the agreed purpose.'[172] A second reason given by Duggan and Brown is that the PPSA is premised on the assumption that the grantor of the security interest will, once the secured obligation is performed, become the unencumbered owner of the collateral. They say that in *Quistclose* scenarios, the performance of the purpose typically results in the loan money being paid to a third party, meaning that the borrower is in effect a conduit of the money.[173] Finally, in the UK, the Law Commission has said that even if a functional analysis correctly views the lender in a *Quistclose* scenario as a secured creditor, such an interest arises by operation of law.[174]

The third reason will be discussed later in this section. Turning to the first two reasons, the issue with these arguments is that as a matter of regulation they miss the point. The underlying rationale of the PPSA is to 'largely ignore' the legal form of a transaction and instead focus 'on the transaction's *commercial substance* to determine whether it should be treated as a security interest.'[175] This includes ensuring that 'ownership of an asset is no longer sufficient to protect a party, as an ownership interest in property can become subordinate to the interest of a third party, or even lost entirely, in some circumstances.'[176] In the case of *Quistclose* trusts, the usual fact pattern involves a loan or the payment of an antecedent debt. A number of the arguments above rely on a distinction between the lender as the beneficiary of a trust and as creditor under a loan contract. However, as a matter of commercial substance, the lender expects to be repaid, irrespective of whether the legal mechanism is via a debt or trust. Indeed, *Quistclose* trusts would seem to be motivated by insolvency concerns to a far greater degree than some title retention arrangements that fall within the PPSA, such as hire-purchase contracts and leases.[177] It may also be asked whether it is correct to say there is no obligation independent of the trust when a lender makes the loan subject to the immediate accrual of interest, as illustrated by the 24 per cent rate imposed in *Twinsectra*. Furthermore, whilst a *Quistclose* trust will dissolve if the loan is applied for the prescribed purpose, until then its characteristics dovetail with those of functional security interests, in terms of matters such as priority in insolvency and giving the lender a 'self-help' procedure (dissolving the borrower's power to apply the money for the designated purpose) on the happening of certain events.

171 Stevens, n 51 above, 166.
172 Duggan and Brown, n 137 above at [3.69].
173 *ibid*.
174 The Law Commission, *Registration of Security Interests: Company Charges and Property Other Than Land: A Consultation Paper* (London: TSO, 2002) at [7.53]-[7.54].
175 B. Whittaker, *Review of the Personal Property Securities Act 2009: Final Report* (Attorney-General's Department, 2015) 11 (emphasis added).
176 *ibid*.
177 For an example of a PPSA statute biting in ways probably unanticipated by the parties, see, for example, *New Zealand Bloodstock* v *Waller* [2005] NZCA 254 (lease-to-purchase agreement of horse).

We must also bear in mind that the use of registration as a means to perfect security interests is relevant not only to the legal question of priority but also supports the commercial imperative of transparency: the ability of fresh money suppliers and other third parties to find out about the financial position of a company (including whether assets apparently belonging to that company are encumbered by a security interest held by someone else), and for existing creditors to make determinations about the timing of liquidation decisions.[178] The upshot of equitable intervention in *Quistclose* was to support Rolls in its attempt to maintain the illusion that everything was okay. This points in the opposite direction to the information function of a register, and prompts us to ask why equity should sanction attempts to hide financial truths from investors, employees and other creditors.

Finally, in thinking about regulation it is necessary to consider how a well-advised repeat player might respond to a system in which many transactions are caught as functional security interests under PPS legislation but *Quistclose* trusts are not. If judges are willing to infer *Quistclose* trusts in the absence of unambiguous language, and are willing to dispense with the need for trust-consistent segregation and so forth, then lenders (and their litigation lawyers) may welcome the opportunity to retrofit a trust framework on unsecured loans that have gone bad.[179] We might also see *ex ante* attempts to bolster trust arguments, for instance by ensuring that loan documentation uses the word 'trust' and specifies the exclusive purpose of the loan. McKendrick argues that in practice, the *Quistclose* trust is most likely to comprise a 'residual device'[180] used by non-bank financiers, especially for transactions which due to urgency or otherwise do not utilise traditional forms of security. There is undoubtedly truth in the proposition that many lenders will view the *Quistclose* trust as too limited to replace traditional security such as the charge. However, especially for loans that are unsecured, the *Quistclose* trust may be a clear improvement on the status quo by giving further comfort to the lender that they will be repaid.[181] As noted in the third part, above, it is open to question whether this will encourage additional lending to take place; it would seem, though, that if *Quistclose* trusts are outside the PPSA, lenders have nothing to lose in advancing such arguments.

Thus, whilst it may be possible to draw legal distinctions between *Quistclose* trusts and title retention arrangements, the question is whether such distinctions are relevant to the policies underpinning PPS legislation. In Australia, *Quistclose* arrangements are the subject of an express exclusion from the PPSA,[182]

178 Law Reform Commission, n 167 above at [5.19]; see also Gardner, n 82 above, 39.
179 See also E. McKendrick, 'Commerce' in Swadling (ed), n 13 above, 150.
180 *ibid*, 152.
181 One might point, here, to McKendrick's observation that *Quistclose* arguments seem to have been more successful for lenders who had access to professional advice, such as the scheme for paying advertising fees in *Carreras*, and the structure of Mr Barber's investment in *Re EVTR*: *ibid*, 149. This suggests that such advisors may seek to protect the availability of *Quistclose* reasoning.
182 PPSA 2009 (Cth), s 8(1)(h) (excluding from the Act 'a trust over some or all of an amount provided by way of financial accommodation, if the person to whom the financial accommodation is provided is required to use the amount in accordance with a condition under which the financial accommodation is provided').

a matter not elaborated upon in the Explanatory Memorandum accompanying the legislation.[183] In contrast, no similar carve-out is found in equivalent legislation elsewhere, and in those jurisdictions there remain live questions about whether such trusts are security interests and (if so) require registration or fall within other exemptions, for instance for interests created by law.[184] In England, this regulatory question does not currently arise as there is no comprehensive PPS register, and to the extent charges are required to be registered, it has been accepted that the term 'charge' should bear its ordinary meaning and not extend to *Quistclose* arrangements.[185] In a report considering reform to English securities law, the Law Commission has said that even if the *Quistclose* trust involves a functional security interest, such an interest arises by operation of law and therefore ought not to require registration.[186] If *Quistclose* trusts are constructive trusts imposed by judges in response to unconscionable conduct or to address fairness concerns, then their exclusion from PPS statutes may make sense.[187] However, *Quistclose* trusts have not been explained in this way by the judiciary, even if some of the normative reasoning suggests that they are applying considerations more apt for such a characterisation. In Australia, for example, the prevailing understanding is that *Quistclose* trusts are orthodox express trusts. If the Australian government, in enacting the express exclusion in the PPSA, was influenced by the view that *Quistclose* trusts are imposed, then this is at odds with the views in the case law and does not take an intention-focused analysis to its logical conclusion. In the UK, *Quistclose* trusts are now understood as resulting, which at first blush may seem consistent with the exclusion of any registration requirement. However, not only is there long-standing debate about the doctrinal basis for the resulting trust and the role of

183 Personal Property Securities Bill 2009, Replacement Explanatory Memorandum (replacing version presented on 24 June 2009).

184 In *Two Feathers* n 78 above, Feldman LJ stated at [23] that if an argument is made for expansion of the *Quistclose* trust in Ontario, 'the court will have to consider a number of commercial consequences, one of the most significant of which is the potential effect on the creditors of the borrower (or grantee) of the subject funds. For example, as in this case, where funds are advanced to a business with no registration under the *Personal Property Security Act*, R.S.O. 1990, c. P-10, creditors will have no notice, and in many cases no knowledge, that they are dealing with a debtor whose money is subject to a trust and not available to the general creditors.' Such a statement might suggest that in other circumstances registration would be required.

185 *Carreras* n 12 above, 227.

186 The Law Commission, n 174 above. These statements were made in 2002 in the context of a lengthy consultation in relation to the reform of English securities law. The Law Commission's original recommendations were for introduction of an expanded registration regime that covered functional security interests. In a consultative report of 2004, the Law Commission noted that consultees who addressed the question of *Quistclose* trusts agreed with its provisional proposal that such trusts be 'outside the requirement to register', but concluded that with debate about the nature of the special purpose trust, this should be left to the courts rather than be the target of specific regulation: The Law Commission, *Company Security Interests: A consultative report* (London: TSO, 2004) at [3.61]. In its final report of 2005, the Law Commission retreated from some of its more ambitious suggestions for reform in relation to functional security interests, and there was no discussion of *Quistclose* arrangements: The Law Commission, *Company Security Interests* (Cm 6654, 2005).

187 Although unconscionability is often said to provide a common thread across different instances in which a constructive trust arises, this is not to say that intention is not relevant: see, for example, Chambers, n 32 above, 221-224. See also Glister, n 170 above, 635-640 (discussing the general law exclusion in the Australian PPSA, s 8(1)(c), to constructive trusts).

intention, but in *Quistclose* scenarios, the stated importance of party intention – even if not always taken seriously by judges – sits very uncomfortably with the proposition that such trusts are imposed rather than consensual.

In short, characterisation is not a strictly academic exercise – not only should it reflect the normative underpinnings of a legal principle, but it should help guide us in other regulatory matters.

CONCLUSION

There is an extensive academic literature considering the best doctrinal characterisation of the *Quistclose* trust. This literature has subjected each possibility to a high level of scrutiny for its coherence with principle and its ability to explain the outcomes in the case law. So far, all theories have been found wanting in some respect. This article has sought to build on this literature by paying far greater attention to the normative question of why we are better off in a world with *Quistclose* trusts. This is relevant in part because of characterisation; for instance, if *Quistclose* trusts are best seen as responding to unconscionable conduct, then we may be happy to place far less weight on party intention and to classify such trusts as constructive. It has been argued in the third part above that normative claims grounded in unconscionability, fairness and incentivisation all have weaknesses, and that the strongest normative argument is that *Quistclose* trusts are justified by reference to party intention. This article has therefore taken the view that *Quistclose* trusts are generally express, with the result that judges should pay proper regard to party intention when determining whether a trust has arisen, including taking seriously the need for trust-consistent characteristics like restrictions on use and segregation.

However, that is not the end of the matter, as we also need to consider how characterisation impacts on regulatory matters. The most obvious question for *Quistclose* trusts is how they are treated in insolvency situations. As seen in the discussion of security interests in the fourth part of this article, one issue is the potential mismatch if judges understand *Quistclose* trusts to be intentional (even if this analysis is watered down in the application) and PPS statutes understand them as imposed. If we prefer the former characterisation, we need to consider what this means for insolvency legislation and PPS statutes. There may be doctrinal reasons why a *Quistclose* trust, even if intentional, is not a security interest, although given PPS statutes prioritise substance over form, such arguments may feel unconvincing in isolation. We therefore need to be clear about why we have *Quistclose* trusts and what status they should enjoy upon insolvency. For instance, we may decide that on balance a wholesale exclusion from PPS legislation is warranted, perhaps because of pragmatic concerns in relation to legal certainty, practical difficulties in registering a short-term interest, or reducing clutter on the register. Importantly, however, we need to ensure consistency in the characterisation, normative explanation and regulation of *Quistclose* trusts. At the moment it is not clear that we have a unified and coherent understanding of these devices.