

Quistclose: analysing the key decisions closely

We can only understand the arguments about the nature of a *Quistclose* trust if we focus in detail on the precise formulations used by the courts. In that vein, let us bore down a little more deeply into the detail of the dicta of Lord Wilberforce in *Barclays Bank v Quistclose*. The main argument advanced by Barclays Bank was that there was only a loan contract between Quistclose and Rolls Razor, and under banking law there is a clear principle that loan contracts and contracts for bank accounts in themselves do not create a trust relationship.¹ Lord Wilberforce, however, was prepared to imply the existence of a trust on the facts in line with earlier cases like *Re Rogers* where the existence of the trust was predicated on the important fact that the loan contract contained a statement of a limited purpose for which the loan money could be used.² It is important to dwell a little on the precise words which Lord Wilberforce used. His lordship held³ that “[i]t is not difficult to establish precisely upon what terms the money was advanced ... to Rolls Razor Ltd. There is no doubt that the loan was made specifically in order to enable Rolls Razor Ltd. to pay the dividend ... and for no other purpose”. The parties’ contractual purpose was clear, therefore: the money was to be used only for a limited purpose.

Lord Wilberforce continued:⁴

There is surely no difficulty in recognising the co-existence in one transaction of legal and equitable rights and remedies: when the money is advanced, the lender acquires an equitable right to see that it is applied for the primary designated purpose:⁵ when the purpose has been carried out (i.e., the debt paid) the lender has his remedy against the borrower in debt: if the primary purpose cannot be carried out, the question arises if a secondary purpose (i.e., 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.

This passage means that there is no problem with having obligations at common law (i.e. to repay the loan) and obligations in equity (i.e. to hold the money on trust until it is used for the specified purpose). Thus, if the purpose is performed then the lender has rights against the borrower at common law under the terms of the contract (i.e. “has his remedy in debt”). The “secondary obligation” arises in equity either on the express terms of the contract or impliedly from the circumstances. The “remedies of equity” in this context are the “secondary trust” which requires that the loan money is held on trust if it is not used for the specified purpose. Interestingly, though, Lord Wilberforce expressed this in terms of being a general “equitable right” rather than explicitly a resulting trust: an idea to which we shall return below. A similar formulation has been used by Lord Millett in *Twinsectra v Yardley*,⁶ and

¹ See Alastair Hudson, *The Law of Finance* (Sweet & Maxwell, 2009), para 30-04. See *Foley v Hill* (1848) 2 HL Cas 28, 9 ER 1002, 1005, *per* Lord Cottenham LC.

² [1970] AC 567, 581.

³ [1970] AC 567, 581.

⁴ [1970] AC 567, 581-582.

⁵ *In re Rogers*, 8 Morr. 243, *per* both Lindley LJ and Kay LJ.

⁶ [2002] 2 AC 164, para [69].

approved by Evans-Lombe J in *Cooper v PRG Power Ltd*,⁷ to the effect that “when the money is advanced, the lender acquires a right, enforceable in equity, to see that it is applied for the stated purpose, or more accurately to prevent its application for any other purpose”: again, it is an equitable ability to prevent misuse of the money. As Lord Wilberforce continued:

I can appreciate no reason why the flexible interplay of law and equity cannot let in these practical arrangements, and other variations if desired: it would be to the discredit of both systems if they could not. In the present case the intention to create a secondary trust for the benefit of the lender, to arise if the primary trust, to pay the dividend, could not be carried out, is clear and I can find no reason why the law should not give effect to it.

Therefore, the *Quistclose* trust arises from the interplay of the ordinary principles of the contract of loan at common law and the equitable principles which prevent ownership of the loan money being passed to a third party if it is misused. The manner in which the *Quistclose* trust arises then is by means of a “secondary trust” coming into existence for the benefit of the lender if the “primary trust ... cannot be carried out”. Three points emerge. First, this trust was based on that inter-action of primary and secondary trusts being the intention of the parties, an idea which has been approved in subsequent cases.⁸ For example, in *Abou-Rahmah v Abacha*⁹ it was held that there could not be a *Quistclose* trust if the parties’ intentions were that money was paid “unconditionally” from one to the other. Secondly, this does not require that the borrower must have misused the money; instead, it only requires that the purpose “cannot be carried out” for whatever reason, whether because of the borrower’s insolvency or some other event. Thirdly, this form of trust must be a resulting trust because the equitable interest arises for the first time once the primary purpose cannot be carried out. Moreover, because the House of Lords was asked specifically in this appeal whether or not a resulting trust came into existence, we must assume that they are therefore upholding the existence of a resulting trust on this appeal even though the expression “resulting trust” is not used by Lord Wilberforce.

It is this last conceptualisation of the *Quistclose* trust which we should pursue into the model advanced by Lord Millett in *Twinsectra v Yardley*. Lord Millett upheld the theory of the *Quistclose* trust being a resulting trust, but explains its nature differently from Lord Wilberforce in the *Quistclose* case. We shall focus on two passages in particular from his lordship’s speech. First, paragraph 81 of the judgment, which was considered in outline above, which reads as follows:

On this analysis, the *Quistclose* trust is a simple commercial arrangement akin ... to a retention of title clause (though with a different object) which enables the borrower to have recourse to the lender's money for a particular purpose without entrenching on the lender's property rights more than necessary to enable the purpose to be achieved. The money remains the property of the lender unless and until it is applied in accordance with his directions, and insofar as it is not so applied it must be returned to him. I am disposed, perhaps pre-disposed, to think that this is the only analysis which is consistent both with orthodox trust law and with commercial reality. ...

⁷ [2008] BCC 588, para [13].

⁸ [Re Niagara Mechanical Services International Ltd \(in admin.\) \[2001\] B.C.C. 393; Shalson v Russo \[2003\] EWHC 1637 \(Ch\); \[2005\] Ch. 281](#); *Cooper v PRG Power* [2008] BCC 588.

⁹ [2005] EWHC 2662 (QB), [2006] 1 Lloyd's Rep 484.

The second sentence is very problematic: "The money remains the property of the lender unless and until it is applied in accordance with his directions, and insofar as it is not so applied it must be returned to him." There is a clear contradiction in terms here: if the money *remains* the property of the lender then how can it possibly be *returned* to him? If I retain property then I cannot possibly ask you to return it to me later because I have kept it. Imagine that you ask to borrow my umbrella because it is raining and I refuse to lend it to you,¹⁰ if I were then to come to you the next day and demand that you return my umbrella you would say "well, you kept your umbrella so how can you possibly have it returned to you?" It is the same problem with Lord Millett's formulation here: if the lender retains the money, it cannot logically be returned to him. What we might take Lord Millett to mean is that *ownership* of the money in equity remains with the lender even if *possession* of the money is passed to the borrower, such that the borrower has to return *possession* of the money to the lender. Similarly, Lord Millett's reference to "the property" is unclear because we cannot know if it means retention of absolute title (which would negate the possibility of there being a trust) or whether it is supposed to mean only retention of an equitable interest under a trust.

The following paragraph from Lord Millett's speech also presents problems; it is paragraph 100:

As Sherlock Holmes reminded Dr Watson, when you have eliminated the impossible, whatever remains, however improbable, must be the truth. I would reject all the alternative analyses, which I find unconvincing for the reasons I have endeavoured to explain, and hold the Quistclose trust to be an entirely orthodox example of the kind of default trust known as a resulting trust. The lender pays the money to the borrower by way of loan, but he does not part with the entire beneficial interest in the money, and in so far as he does not it is held on a resulting trust for the lender from the outset. Contrary to the opinion of the Court of Appeal, it is the borrower who has a very limited use of the money, being obliged to apply it for the stated purpose or return it. He has no beneficial interest in the money, which remains throughout in the lender subject only to the borrower's power or duty to apply the money in accordance with the lender's instructions. When the purpose fails, the money is returnable to the lender, not under some new trust in his favour which only comes into being on the failure of the purpose, but because the resulting trust in his favour is no longer subject to any power on the part of the borrower to make use of the money. Whether the borrower is obliged to apply the money for the stated purpose or merely at liberty to do so, and whether the lender can countermand the borrower's mandate while it is still capable of being carried out, must depend on the circumstances of the particular case.

Again, as with paragraph 81, there is a problem in that we are told that the money "remains throughout in the lender" and yet that "the money is returnable to the lender". Furthermore, the *Quistclose* trust is held explicitly to be a resulting trust, even though ownership of the money is said to *remain* with the lender. Therefore, this is not a resulting trust as Prof Birks has explained it because a resulting trust ordinarily requires that equitable ownership of the property has passed away and

¹⁰ I can be capricious like that, especially with umbrellas because you never get them back.

that it then “jumps back”¹¹ to the lender. That cannot happen if the lender *retains* equitable ownership of the loan money throughout the loan contract. Alternatively, we must reject Prof Birks’s analysis of a resulting trust and instead accept that Lord Millett has established that resulting trusts are merely a “default trust” in which a court of equity simply recognises that when there is a question as to the ownership of property then we should recognise that the last owner of that property is still its owner. This is the analysis which is advanced in Chapter 11 of this book of resulting trusts in general: an automatic resulting trust operates in circumstances in which it is unclear who is the owner of property to declare that the property is held on trust for the last person who was undoubtedly the owner of that property.

We are told that the borrower has merely a power to use the money for the described purpose (just like the powers discussed in Chapter 3). The money is said “to be returnable to the lender” (oddly even though the lender has nevertheless retained equitable ownership of it) because the power disappears (apparently) once it is not performed. In the final sentence, Lord Millett acknowledges that the precise nature of the parties’ obligations will depend upon the precise terms of the contract between them. Therefore, we have a very stylised form of resulting trust in the speech of Lord Millett. This model is necessary for Lord Millett’s analysis and yet Lord Millett delivered a dissenting speech in the House of Lords, and as such it is difficult to know what the force of this model is in English trusts law. What is important to note is that subsequent cases have supported it, and thus have lent it some gravitas. It is nevertheless suggested that the better analysis would be to infer the existence of an express trust (just as in *Re Kayford*¹²) from the circumstance.

¹¹ See section 11.1 of this book.

¹² [1975] 1 WLR 279.