

## Conveyancer and Property Lawyer

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### Overreaching and the Trusts of Land and Appointment of Trustees Act 1996 - a reply to Mr Dixon

Graham Battersby

Graham Ferris

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**Cases:** City of London Building Society v Flegg [1988] A.C. 54 (HL)

Birmingham Midshires Mortgage Services Ltd v Sabherwal (Equitable Interest) (2000) 80 P. & C.R. 256 (CA (Civ Div))

**\*Conv. 221** In his valuable commentary on *Birmingham Midshires Mortgage Services Ltd v Sabherwal*<sup>1</sup> Mr Martin Dixon has sought to dispose of what he calls “the Ferris/Battersby effect”, *i.e.* the argument that the Trusts of Land and Appointment of Trustees Act 1996 (TOLATA) has, no doubt inadvertently, overruled *City of London Building Society v Flegg*<sup>2</sup> in relation to dispositions of registered land made in breach of trust. We are flattered, of course, to have an “effect” named after us, but to a large extent we would wish to disclaim paternity. In our original article<sup>3</sup> we sought to analyse the provisions of TOLATA and to elucidate its structure, building on the work that Mr Charles Harpum had done on the pre-1997 law.<sup>4</sup> Mr Harpum showed that overreaching depends on the valid exercise of a dispositive power; a disposition outside such a power (which Mr Harpum called *ultra vires*) would not overreach. In our article, we sought to apply that insight to the changed structure of trusts of land brought into being by Part 1 of TOLATA. Our concern has been to analyse the new law at a structural level, and therefore it is not any supposed “Ferris/Battersby effect” but the effect of TOLATA that is in issue.

Mr Dixon clearly starts out with a desire to defend the continuing integrity of *Flegg*, and in his note he advances the view that section 18 of the Land Registration Act 1925 has a role to play in granting powers to trustees of land.<sup>5</sup> The fact is, however, that the House of Lords in *Flegg* put forward two lines of reasoning concerning the nature of overreaching. One line of **\*Conv. 222** reasoning linked overreaching in the case of a trust for sale (the relevant case on the facts of *Flegg*) to the doctrine of conversion.<sup>6</sup> We agree with Robert Walker L.J. in the *Birmingham Midshires* case that the abolition of the doctrine of conversion has had no impact on the operation of overreaching.<sup>7</sup> The operative reasoning in *Flegg* must therefore be the other line, which relied on the effects of the powers granted to trustees for sale by the 1925 property legislation.<sup>8</sup> That line of reasoning took no account of section 18 of the Land Registration Act 1925. The crucial section was section 28 of the Law of Property Act 1925, and the reasoning of the House of Lords is applicable to both unregistered and registered land. When, therefore, Mr Dixon resorts to section 18 of the Land Registration Act 1925 to explain the operation of overreaching in registered land, he departs from any possible *ratio decidendi* of *Flegg*. On that view, the reasoning in *Flegg* is therefore flawed. Mr Harpum reached the conclusion that *Flegg* was decided *per incuriam* in failing to rely on section 18.<sup>9</sup> Yet section 18 was cited to the House in argument,<sup>10</sup> and was expressly referred to by Lord Templeman in his speech.<sup>11</sup> In upholding *Flegg*, therefore, Mr Dixon is forced to conclude that it was correctly decided but for the wrong reasons. We would argue, to the contrary, that *Flegg* was correct in refusing to give section 18 a crucial role in the operation of overreaching in registered conveyancing. Further, the reasoning may be seen as, *sub silentio*, supporting our argument that section 18 (and similar provisions in the Land Registration Act 1925, *e.g.* section 25) are concerned with the *ability* of any registered proprietor to enter into dispositions and create charges, not with the *authority* of **\*Conv. 223** registered proprietors who are trustees.<sup>12</sup> That argument is not met by anything that was said in either the *Birmingham Midshires* case or *State Bank of India v. Sood*.<sup>13</sup>

Mr Dixon suggests that we might read the relevant provisions as “providing a remedy inter se

between trustee and beneficiary while maintaining the largely unassailable position of a purchaser relying on overreaching and a properly registered disposition".<sup>14</sup> This suggestion would render most of section 16 of TOLATA otiose. There is nothing in TOLATA to suggest that a breach of section 6(5), (6) or (8) operates merely internally between trustee and beneficiary. If that were the effect, the protection afforded to purchasers of unregistered land in section 16(1) and (2) would be quite unnecessary. Similarly, in relation to section 8(2); if a breach of the duty to obtain consent operates merely internally, there is no need for any purchaser protection given by section 16(3)(b). Again, in relation to section 11(1); if a breach of the duty to consult operates merely internally, there is no need for any purchaser protection given by section 16(1). Mr Dixon needs to demonstrate how his proposition can be derived from the provisions of TOLATA. In fact, the whole thrust of section 16 is in the opposite direction, resting on the assumption that without its protective provisions a purchaser would be adversely affected by the various breaches which it covers; the bulk of that section cannot be ignored in order to explain away section 16(7).

In advancing the argument that the relevant provisions operate only internally, Mr Dixon proffers a concession towards those who might be concerned about the justice of overreaching in operation: "If we are concerned that beneficiaries could suffer a breach of trust and have no viable remedy (after all, the trustees usually are worthless defendants), one solution might be that a purchaser of a registered title (even though having relied on **\*Conv. 224** overreaching) could be liable if, but only if, that purchaser knowingly assisted in the breach of trust or knowingly received property in breach of trust."<sup>15</sup> That suggestion surely cannot be correct. If overreaching occurs under a trust of land then section 2 of the Law of Property Act 1925 operates. That section protects "a purchaser of a legal estate in land ... whether or not he has notice ..." "Purchaser", for this purpose, is defined as "a person who acquires an interest in or charge on property for money or money's worth", *i.e.* there is no requirement of good faith.<sup>16</sup> We must assume that provisions in the property legislation of 1925 "were drafted with the utmost care, and their wording, certainly where this is apparently clear, has to be accorded firm respect".<sup>17</sup> Accordingly, the absence of a requirement of good faith in the relevant definition of a purchaser is taken to indicate a legislative intention that good faith is not required.<sup>18</sup> As to the meaning of "notice", from the effect of which section 2 protects the purchaser, that must be read as comprising actual, imputed and constructive notice.<sup>19</sup> It follows from all of this that, where section 2 applies and overreaching operates, there is no room for any personal liability imposed upon a purchaser as a result of knowingly receiving trust property,<sup>20</sup> nor, we suspect, in the absence of clear fraud, for dishonest assistance in a breach of trust.<sup>21</sup> In this context, "it is not fraud to rely on legal rights conferred by Act of Parliament",<sup>22</sup> and the courts have refused to allow claimants to avoid the consequences of the 1925 legislation by means of alternative sources of personal or proprietary liability **\*Conv. 225** *ity*.<sup>23</sup> It is true that the effect on an equitable owner of the doctrine of overreaching can be harsh, even devastating, but Parliament has not thought fit to limit its effect.<sup>24</sup> In the face of that legislative policy Mr Dixon's suggestion cannot be sustained.

This leaves us with Mr Dixon's third line of argument. This argument accepts the possibility that there are breaches of trust which preclude overreaching. Prior to TOLATA such breaches were those known as *ultra vires* breaches of trust, which, in the context of the pre-1997 law, meant those transactions which were neither sales nor authorised by section 28 of the Law of Property Act 1925. Quite correctly Mr Dixon states<sup>25</sup> : "... there is no necessary correlation between a breach of trust and a disposition being *ultra vires* so as to destroy overreaching and registration ... all *ultra vires* dispositions are in breach of trust, but it does not follow that all dispositions in breach of trust are *ultra vires*." We accept that completely, in the sense that it is impossible to postulate any logical congruence of the terms "breach of trust" and "*ultra vires*". But that was never our position. We attempted to deduce from the terms and structure of TOLATA which, if any, breaches of trust would preclude a disposition from having an overreaching effect. Mr Dixon may think that our deductions are wrong, but if so he needs to explain how, and why, by reference to the precise provisions of TOLATA.

Briefly, our position can be summarised as follows. A breach of trust that constitutes a breach of the terms of section 6(5), (6) or (8) is, in the absence of purchaser protection against that breach, a breach of trust that prevents overreaching from occurring.<sup>26</sup> The **\*Conv. 226** failure of TOLATA to extend its protective provisions to purchasers of registered land with respect to those provisions limits the effectiveness of overreaching in registered land after 1997. The situation is different with respect to a breach of trust that constitutes a breach of section 9 of TOLATA, or a breach of a provision made by the settlor that the consent of three people is required before a disposition is made.<sup>27</sup> A delegation purporting to be authorised by section 9(1), and a disposition made, contrary to the settlor's directions, with the consent of two people, are *prima facie* capable of precluding overreaching,<sup>28</sup> but a purchaser of registered land is able to shelter behind the same protective provisions as a purchaser

of unregistered land.<sup>29</sup> There is no inexorable logic determining when statute will shield a purchaser of registered land from the consequences of a breach of TOLATA, nor, as far as we can see, are there any general principles operating. We are faced simply with a list, derived from the very terms of TOLATA itself, of those breaches of trust which will preclude overreaching in the case of registered land, and those which will not.

Prior to 1997 the basic structure of the law was coherent: whenever trustees for sale effected a disposition of a legal estate that was permitted by their powers, section 2 of the Law of Property Act 1925 was activated, and the equitable interests would be overreached provided that any capital money that arose was paid to no fewer than two trustees. It was generally accepted that this applied to both unregistered and registered land, and that assumption was confirmed by *Flegg*. Before 1997 a purchaser taking under a disposition that was *ultra vires* could not take advantage of the provisions of section 2 of the Law of Property Act 1925; after 1997 a purchaser taking under a disposition made in breach of sections 6, 8 or 11 of TOLATA cannot take advantage of the provisions of section 2 of the 1925 Act. We have no wish to argue that TOLATA “dismantle[d] one of the cornerstones of the 1925 legislation”.<sup>30</sup> We simply argue that, if overreaching is a function of the powers of the trustees, then a structural change to the regime governing those powers will have an effect on the operation of overreaching. We have sought to deduce the nature of any such effect within the provisions of TOLATA, because it **\*Conv. 227** was Part 1 of that Act which made the change of regime governing trustees' powers.

There remains one final strand to Mr Dixon's defence of *Flegg*. He writes that “The implications of this [the Ferris/Battersby] analysis for institutional lenders ... need no emphasis”<sup>31</sup> and “... if TOLATA is held to have made this substantive change in the law of overreaching, and thereby to have undercut current mortgage lending practice ...”, the law will be promptly changed by statute.<sup>32</sup> In these circumstances, “it will take a very considerable leap of judicial imagination to conclude that TOLATA was ever intended to limit overreaching in registered land”.<sup>33</sup> We have never argued that the changes to the law introduced by TOLATA were intended to limit the operation of overreaching in registered land; on the contrary, we have always argued that the effect was probably inadvertent.<sup>34</sup> Nonetheless, we remain persuaded that this has been the baleful effect of the statute, largely owing to the impact of section 16(7). That subsection, in denying purchaser protection to purchasers of registered land, is a more sophisticated version of the fallacy which underlies section 3 of the Law of Property (Joint Tenants) Act 1964. It is the product of legislative error, and can be rectified only by amending legislation, not by strained judicial interpretation of the existing provisions.

### Graham Ferris

*Nottingham Trent University*

### Graham Battersby

*Sheffield University*

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1. (2000) 80 P. & C.R. 256. Dixon's note is at [2000] Conv. 267.

2. [1988] A.C. 54.

3. [1998] Conv. 168.

4. “Overreaching, Trustees' Powers and the Reform of the 1925 Legislation” [1990] C.L.J. 277.

5. [2000] Conv. 267, n. 3, and 269. The possible role of section 25 of the Land Registration Act 1925, was not explored by Dixon; in principle that section should be treated in the same way as section 18. In *Flegg* Lord Oliver did not cite section 18 but did cite section 25: [1988] A.C. 54 at 86C. Lord Templeman, on the other hand, did not cite section 25 but did cite section 18(4): *ibid.* at 64D. See also nn. 10 and 11 and text thereto.

6. See [1988] A.C. 54 at 78A and 82-83, where Lord Oliver adopts a passage from the judgment of Cross L.J. in *Irani Finance Ltd v. Singh* [1971] Ch. 59.

7. (2000) 80 P. & C.R. 256 at 261-262. Dixon also agrees: [2000] Conv. 267 at 273. However, in the light of the statements cited in the previous footnote, the remarks of Lord Oliver in *Flegg* [1988] A.C. 54 at 90 G-H, cannot possibly be read as indicating that Lord Oliver considered that the doctrine of conversion was irrelevant to overreaching, as suggested by Dixon in n. 25.
8. See [1988] A.C. 54 at 78, 90E and 91G, on the role of section 28 of the Law of Property Act 1925, in overreaching.
9. [1990] C.L.J. 277 at 309.
10. [1988] A.C. 54 at 64D, citing section 18(4).
11. *ibid.* at 72F. Lord Templeman states: "By sections 2 and 18 of [the Land Registration Act 1925] proprietors of registered land may dispose of the land by transfer or by the creation of a legal estate including the grant of a legal charge by way of mortgage." Harpum, [1990] C.L.J. 277 at 309, says: "The Land Registration Act 1925, section 18(1), was neither cited to nor therefore discussed by the House." We do not imagine that Harpum was intending to draw a distinction between section 18(1) being cited and section 18(4) being cited. We therefore submit that, in the light of Lord Templeman's dictum, the argument that section 18 was not before the House is untenable. See also n. 5.
12. [1998] Conv. 168 at 180-183. That argument is supported by Roger Smith, *Property Law* (3rd ed.), p. 314 ("argument ... seems overwhelming"). Smith also states that the argument based on section 18 is inconsistent with *Hodgson v. Marks* [1971] Ch. 892 (to which might be added that, consequently, the approval of *Hodgson v. Marks* in *Williams & Glyn's Bank Ltd v. Boland* [1981] A.C. 487, would be *per incuriam*). We respectfully differ from that argument. The sale in *Hodgson v. Marks* was undoubtedly in breach of trust. Since it was a bare trust section 2 of the Law of Property Act 1925, could not have operated to protect the purchaser from notice of that breach (and in any event the capital moneys were paid to only one trustee). It is a necessary but not sufficient condition for an overreaching disposition that it be *intra vires*; the disposition must also be lawful, or proper, unless some statutory provision shields a purchaser from the consequences of trustee impropriety.
13. [1997] Ch. 276. We considered this case in [1998] Conv. 168 at 181-182. It seems possible that *Sood* should be considered *per incuriam* on this point (which was not argued).
14. [2000] Conv. 267 at 269.
15. [2000] Conv. 267 at 269-270. It is argued that there is an analogy with the use of "notice" in the line of cases starting with *Barclays Bank plc v. O'Brien* [1994] 1 A.C. 180, citing Thompson [2000] Conv. 43, but we submit that the analogy is not valid. It is now clear, following work by, *inter alios*, Dixon himself, that in *O'Brien* type cases there is only one transaction and no question of priority arises: see *Royal Bank of Scotland Plc v. Etridge (No. 2)* [1998] 4 All E.R. 705; *Barclays Bank plc v. Boulter* [1998] 1 W.L.R. 1, especially at 11, *per* Mummery L.J. There is no "purchaser" in any relevant statutory sense, and no statutory provisions, which might have the effect of conferring purchaser protection, are relevant.
16. Section 205 (xxi) of the Law of Property Act 1925.
17. *Midland Bank Trust Co. Ltd v. Green* [1981] A.C. 513 at 529A, *per* Lord Wilberforce.
18. *ibid.* at 528-531, *per* Lord Wilberforce.
19. *City of London Building Society v. Flegg* [1988] A.C. 54 at 83F, *per* Lord Oliver (to paraphrase, in the context of section 2 "notice" means all forms of notice, including "express notice"). See also section 205 (xvii) of the Law of Property Act 1925 ("Notice" includes constructive notice", and therefore, *a fortiori*, must include actual notice).
20. If despite bad faith and actual notice an equitable interest is overreached, the property is not trust property in the hands of the purchaser.
21. Following the decision in *Royal Brunei Airlines Sdn. Bhd. v. Tan* [1995] 2 A.C. 378, this seems a better expression than "knowing assistance". The fraud required in this context would appear to be actual fraud, as defined by the Court of Appeal in *Armitage v. Nurse* [1998] Ch. 241 at pp. 252-253, *per* Millett L.J. (*i.e.* as requiring dishonesty).
22. *Midland Bank Trust Co. Ltd v. Green* [1981] A.C. 513 at 531B, *per* Lord Wilberforce.
23. See *Lloyds Bank plc v. Carrick* [1996] 4 All E.R. 630 at 641-642: "Section 4(6) of the 1972 Act invalidates, as against the bank, any estate contract ... It cannot be unconscionable for the bank to rely on the non-registration of the contract. I do not see how it could be right to confer ... indirectly, and by means of a proprietary estoppel ... that which Parliament prevented her from obtaining directly ..." Similar reasoning suggests that whenever a purchaser overreaches an equitable interest there should be no remedy available against the purchaser, in the absence of fraud. *Peffer v. Rigg* [1971] 1 W.L.R. 285 (a very questionable decision) and *Lyus v. Prowsa Developments Ltd* [1982] 1 W.L.R. 1044, remain the exceptions.
24. On the contrary, section 6 of TOLATA, gives to trustees of land all the powers of an absolute owner (though the powers can of course be excluded or limited, and can be hedged about by the requirement to obtain consents, etc.). *cf.* Harpum's suggestions in [1990] C.L.J. 277 at 331-333, for limitations on the mortgage powers of trustees. It is a moot point (but we think unprofitable to pursue) whether on balance

TOLATA has made the position of beneficiaries better, or worse, or has left their position much the same.

- [25.](#) [2000] Conv. 267 at 269.
- [26.](#) We would also argue that a breach of section 11(1), a disposition of a type not authorised by a settlor who has under section 8(1) excluded or limited the trustees' powers of disposition, and a disposition made contrary to section 8(2) without any requisite consent, are breaches that preclude overreaching; otherwise, the protective provisions in section 16(1), (2) and (3) would be unnecessary. In some circumstances such breaches will also fall within section 6(5) (beneficiaries' rights disregarded) and section 6(6) (rule of law or equity contravened).
- [27.](#) Further examples can be given, e.g. a sale conducted under depreciatory conditions (see section 13 of the Trustee Act 1925), and a sale by a mortgagee after the power of sale has arisen but before it is properly exercisable (see section 104 of the Law of Property Act 1925).
- [28.](#) Either because they constitute a breach of section 9 of TOLATA, or because they operate independently to prevent overreaching.
- [29.](#) TOLATA, ss 9(2), 10(1).
- [30.](#) See [2000] Conv. 267 at 269.
- [31.](#) *ibid.* at 268. It is perhaps worth noting that institutional lenders habitually seek consent to mortgages from occupiers even when lending to two or more legal owners.
- [32.](#) *ibid.* at 268.
- [33.](#) *ibid.* at 273. We have always argued that a distinction between registered and unregistered land would, in this context, be unacceptable.
- [34.](#) Equally, it is probably correct to say that section 2 of the Law of Property (Miscellaneous Provisions) Act 1989, was not "intended" to undermine the validity of mortgages by deposit of title deeds or land certificates, but that result followed from the changes brought about by the Act: see *United Bank of Kuwait plc v. Sahib* [1997] Ch. 107.