§ Law in Context

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Property Law

Commentary and Materials

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Fragmentation of ownership

8.1. Introduction

One of the distinctive features of English property law is that it can accommodate a wide range of property interests subsisting in the same thing at the same time, each held by a different person. As we pointed out in Chapter 6, in our system property is not synonymous with ownership. The rights and obligations which Honoré described as the attributes of 'the full liberal concept of ownership' need not all be held by the same person at the same time. They may be shared between and distributed among any number of different people in a number of different ways.

However, this fragmentation of ownership is highly systematised. While an owner can by contract give any person a personal right to exercise any of his ownership-type rights and obligations in any way, for any purpose and for any length of time, there are only strictly limited ways in which ownership-type rights can be subdivided and redistributed so as to leave each right holder or group of holders with a distinct property interest, as opposed to merely personal rights against the grantor. This results in a formalised structure of interdependent property interests, which is what we will be examining in this chapter. In Chapter 9, we then look at the gateways to this structure by considering why it is regulated in the way that it is – i.e. why we limit the range of property interests recognised in our system in the way that we do – and when and how the structure can be modified so as to give proprietary status to novel rights, or to novel regroupings of established rights.

8.2. Present and future interests

The first distinction to be made is between present interests (i.e. a present right to have enjoyment of a thing now) and future interests (i.e. a present right to have enjoyment of it at some point in the future). In our system it is not only possible to limit the length of time for which a property interest will last, but also to create a property interest where the enjoyment of the thing is deferred, so that enjoyment will not commence until a future date. By combining the two, the enjoyment of a

thing can be divided up into time slices. Take the following example: you and I have an aunt, a composer, who dies leaving the copyright in her music to me for the first ten years after her death and thereafter to you for the remainder of the copyright period. When she dies we will both acquire property interests in her music: I will have a present right to have the royalties paid to me for the next ten years, and simultaneously you will hold a present right to have the royalties paid to you from a date ten years on.

In this example, both my right and your right are property interests, but, as you might expect, this is not true of all the ways in which one might divide enjoyment of a thing into time slices. We consider here the basic technical rules which determine how enjoyment of a thing can be split up in this way so as to give rise to separate, simultaneous property rights to successive enjoyment of a thing. These rules are not particularly difficult, but they are of ancient origin, mostly vestigial remains of long-abandoned social and legal constructs, and consequently their rationale can be obscure and the terminology unfriendly.

8.2.1. Interests in possession, in reversion and in remainder

The first point starts as essentially a matter of vocabulary. Present rights to present enjoyment are said to be 'in possession', whereas present rights to future enjoyment are either 'reversionary' (or 'in reversion') or 'in remainder'. There is no qualitative difference between a reversionary interest and a remainder interest: the distinction lies in the identity of the person who first acquires the interest. Specifically, reversionary interests involve enjoyment reverting back to the holder of the larger interest out of which the reversionary interest was carved, whereas remainder interests involve a movement of enjoyment forward to someone else. This distinction is significant because, while reversionary interests can, like remainder interests, be created deliberately, they will also arise by operation of law to fill any gap in a chain of time-sliced property interests. The general principle (not always to be applied too mechanistically, as we see later) is that, whenever rights to enjoyment of a thing are split up into time slices, the proprietary right to each slice must be vested in somebody, and unless it has been effectively allocated elsewhere by the grantor, it will automatically vest in the grantor. This is what Honoré describes as the 'residuarity' element in ownership.

An example will make this clearer. Going back to our composer aunt, assume that, while alive, she held a ninety-nine-year lease of her studio and also owned a piano. As owner of the piano, she would be entitled to its use and enjoyment for a period unlimited in time. Consider three possible situations:

1 When still alive, she gives both the piano and the lease of the studio to me for my lifetime, and then to you absolutely. As soon as the gift is made I acquire an interest in possession in both the piano and the lease (I will be entitled to the exclusive use of the piano and the studio during my lifetime – or, in the case of the studio, until the lease ends, if earlier), and you acquire an interest in remainder in them (i.e. you acquire a

present right that, when I die, you will become absolute owner of the piano and holder of the lease for the rest of its term).

2 When still alive, she makes a gift of both piano and lease to me for my life, but states that, after my death, they are to revert to her. Again, that gives me an interest in possession in the piano and the lease, but this time it gives her an interest in reversion in them.

3 When still alive, she makes a gift of both piano and lease to me for my life, but this time says nothing about what is to happen to them after I die. In general, the result will be the same as in (2) above: I acquire an interest in possession and she acquires an interest in reversion. Her interest arises under a resulting trust because the law requires someone to hold the future interest, and the only possible contenders are the grantor who failed to dispose of it elsewhere, or the Crown as the repository of ownerless property (*bona vacantia*). In general, the law prefers to make the interest revert back to the grantor under a resulting trust, although it will go to the Crown as *bona vacantia* in some circumstances, as Lord Browne-Wilkinson explains in his judgment in *Westdeutsche Landesbank* v. *Islington London Borough Council* [1996] AC 669 (Extract 8.1 below).

There are a few other things to say about present rights to future enjoyment. The first is that your remainder interest (in example (1) above) and the aunt's reversionary interest (in (2) and (3) above) are property interests, not personal to you or her. Consequently, they can be sold or given away, and if you or she die before me still holding your respective interests, the interest will simply pass to whoever it is who becomes entitled to your property on your death (as to which see below). So, in example (1), it makes no difference if I am aged three when our aunt makes the gift and you are aged ninety (leaving aside complications about how minors hold property interests). We both still acquire property interests in the studio and the piano, even though you are unlikely to survive long enough to enjoy yours personally.

Secondly, when reversionary and remainder interests are sold or inherited, the terminology remains the same: a person who buys or inherits an interest in the piano or the copyright from you gets a remainder interest, and the person who buys or inherits the interest from the aunt gets a reversionary interest.

8.2.2. Absolute entitlements, contingent entitlements and mere expectancies

When rights to enjoyment are divided up into time slices, the ending of one person's right to present enjoyment and the beginning of the next one's are made to depend on the happening of a future event. Some future events are certain to happen – for example, the death of a human person, or the arrival of a specified date. Other future events may or may not happen, depending on various factors.

8.2.2.1. Absolute entitlements

If the commencement of the right to present enjoyment is dependent on the happening of a future event that is certain to happen, then the interest is said to

be absolute (here meaning unconditional: 'absolute' can also mean unlimited in time, as in example (1) above). The interest is absolute even if we do not know in advance *when* the future event is going to happen, provided it is certain that it *will* happen. Suppose when our aunt died she also left a sum of money (say £10,000) to me for life and then to you absolutely (here meaning unlimited in time). During my lifetime you have an absolute (i.e. unconditional) interest in the £10,000, because it is certain that enjoyment of the £10,000 will eventually pass to you (or the person who has bought or inherited the interest from you), even though no one knows when that might happen.

8.2.2.2. Contingent interests and expectancies

On the other hand, the commencement of enjoyment may be made dependent on the happening of a future event which is not certain to happen, but which may or may not happen. In that case, the interest is said to be contingent – future enjoyment is not certain, but contingent on that thing happening. Different kinds of contingency must be distinguished, because not all types of contingent interest are capable of being proprietary. Take the following examples:

1. You and I agree that I will sell you my land in six months' time for £100,000 if by then I have received planning permission to develop it in accordance with the application I made last month. Here, your right to have the land in six months' time for £100,000 is contingent (a) on you paying me £100,000 on the due date (an event within your control) and (b) on planning permission being granted by the planning authority (an event outside the control of either of us).
2. I give £10,000 to trustees to pay the income for the next twenty-one years to my niece for so long as she remains unmarried but if and when she marries to pay the income to you. Your right to receive any income from the £10,000 is contingent on my niece marrying within the next twenty-one years. Again, this is an event outside the control of either of us, but it is within the control of a prior-interest holder (my niece).
3. You and I agree that I will sell you my land in six months' time for £100,000 if by then you serve notice on me that you want to buy at that price. Your right to buy the land is an 'option to purchase'. It consists of a right to acquire the land in six months' time, contingent (a) on your serving notice and (b) on your paying the money on the due date. Both these events are within your control.
4. You and I agree that, if I decide to sell my land within the next six months, I will sell it to you for £100,000 if you serve notice on me that you want to buy it at that price. Your right here is a 'right of pre-emption'. It consists of a right to acquire the land, which, as in the previous example, is contingent on two factors within your control (your serving notice on me and paying the price when due) but it is also contingent on a factor wholly within my control: my decision to sell in the first place.
5. I make a will leaving you £10,000. As long as I am still alive, your right to get the £10,000 is contingent (a) on my actually having £10,000 when I die (more or less within my control, and certainly not within yours) and (b) on my not changing my will (wholly within my control).

In all five examples, you have a contingent right to future enjoyment, but not all of the five give you property interests. In examples (1), (2) and (3), you have an immediate property interest, as we see in Chapter 12, and the same is mostly now true of example (4) (after earlier uncertainties) whereas in example (5) you definitely do not. The distinction that the law seeks to draw here is between contingent *rights* and 'rights' that are not, properly speaking, rights at all, but mere hopes or expectancies. The law is clear that contingent *rights* are capable of giving rise to property interests, however remote the contingency, whereas mere expectancies are not, however likely it is that the contingency will occur. So, to add a variation to an earlier example, suppose our aunt dies leaving £10,000 to me (then aged three) for my lifetime, and then to you (then aged ninety) absolutely (i.e. unlimited in time), but this time your interest is made contingent on you surviving me. As long as you and I are both alive, you have a property interest in the £10,000 (a contingent remainder interest), unlikely though it is that you or anyone else will ever get to enjoy it (consider what would happen if you sold the interest to someone during your lifetime). Compare this with what would happen if I, a ninety-year-old millionaire, make a will leaving everything to you, my only relative and friend. Until I actually die, you will have no property interest whatsoever in any of my assets, regardless of how likely it is that you will get all of it very soon.

What then is the critical distinction between a contingent right and no right at all, if it is not the likelihood of receiving benefit? The question arises in a broad range of different contexts, so it is not possible to provide a definitive answer. Nevertheless, a common thread appears to be dependency on the will of the benefit-conferrer. In *Pritchard* v. *Briggs* [1980] Ch 338, which we look at in Chapter 12, the Court of Appeal held that a right of pre-emption (example 4 above) was not a property interest because the holder's right is dependent on the volition of the seller. It was not made clear why this factor should be conclusive, nor whether the same applies to any other contingency which is in the seller's control in the sense that he can decide whether or not to bring it about. In the case of rights of pre-emption which relate to land, the effect of *Pritchard* v. *Briggs* has been reversed, at least in registered land, by section 115 of the Land Registration Act 2002, without, however, throwing any light on this particular issue.

In the context in which rights of pre-emption arise, a more promising test to apply in deciding whether a contingent right is proprietary or not might be to ask whether outsiders can easily tell whether or not the contingency has occurred. In *Pritchard* v. *Briggs*, the key issue was whether the interest was to have the quintessentially proprietary attribute of enforceability against third parties. As we saw in Chapter 5, there are good reasons for demanding that no interest should be enforceable against third parties unless third parties can easily ascertain the interest. For present purposes, this means being able to find out not only that the interest exists, but also whether or not any contingencies have been satisfied. A registration requirement (which now exists for rights of pre-emption in registered land by virtue of section 115 of the Land Registration Act 2002) will alert outsiders

that I hold a right of pre-emption over your land, but it cannot help them find out whether you have taken the decision that will trigger off my right to insist that you sell to me. This is something that is inherently difficult both for me and for outsiders to ascertain, except perhaps retrospectively (when you demonstrate by selling to someone else that you made a prior decision to sell). However, it is perfectly possible to have a right of pre-emption where the contingency is not the seller arriving at a state of mind about selling but the seller providing some external manifestation of that state of mind: 'if the seller decides to sell' is necessarily difficult to ascertain, but 'if the seller serves notice on the buyer that he has decided to sell' is not. Nevertheless, this distinction was not drawn either in the Court of Appeal decision in *Pritchard* v. *Briggs* or in section 115 of the 2002 Act: before the 2002 Act, both types of right of pre-emption were incapable of binding third parties, whereas now both are fully enforceable against third parties.

8.2.2.3. Alternative contingencies

If a person has a contingent interest – i.e. an interest where the commencement of enjoyment is contingent on the happening of an event which may never happen – then it must follow that someone else will simultaneously hold the mirror-image contingent interest – an interest where enjoyment is dependent on that event not happening. For the reason given in section 8.2.1 above, if no one is specified as the holder of this mirror-image contingent interest, it will belong to the grantor. So, in the example given at the end of section 8.2.2.2 above (our aunt dies leaving £10,000 to me, then aged three, for life, with remainder to you, then aged ninety, provided you survive me), the aunt's estate will include a reversionary right to the £10,000 on my death, contingent on you not surviving me.

8.2.3. When interests vest

To state the obvious, only a person who exists and is identifiable can hold a present *right* to future enjoyment of a thing. Suppose my aunt dies leaving £10,000 to me for my life, and then to my husband for life, and then to my eldest child absolutely ('absolutely' here meaning unlimited in time). If when she dies I am unmarried and have no children, it would be a nonsense to say that, at that point my husband and eldest child have property interests in the £10,000. Their interests can only vest in them when they come into existence. So, when my aunt dies, I acquire a life interest in possession in the £10,000. If and when I marry thereafter, my husband will acquire a contingent remainder interest in the £10,000 (contingent because he may not still be my husband when I die), and, if and when I first have a child, that child will also acquire a contingent remainder interest (consider why contingent, and consider also why, given the circumstances, a contingent reversionary interest in the £10,000 will form part of my aunt's estate when she dies).

Our legal system has never been very happy about allowing people to create these inchoate interests which will not vest in a person until some time in the future. We consider why this is so in section 8.2.8 below.

8.2.4. Alienation, management and control

When there are successive property interests in a thing, only the person with the absolute (i.e. unlimited in time) interest is entitled to the *capital* in the thing: the holder of an interest which is limited in time is entitled only to income/enjoyment type benefits. What these income/enjoyment type benefits are of course varies depending on the nature of the thing in question, whether it is a symphony, a piano, a sum of money or a piece of land. Whatever the nature of the thing, however, this immediately leads us into problems about alienation, management and control. Take alienation first. Each interest holder can of course deal independently with her own property interest in the thing (for example, sell or mortgage it or give it away), but none of them individually has the capacity to make an effective disposition of any greater interest in the thing (because of the *nemo dat* rule: see Chapter 10). If they do all want the whole thing sold (i.e. so that the buyer acquires absolute ownership) they are all going to have to act in concert – they must all get together, all agree the terms of the transaction, and all co-operate in the mechanics of carrying it out. This will be difficult enough when all interests in the thing are vested in people who exist (think of the holdout problems, and what you do if some of them are minors). When some interests are not yet vested, it will be impossible.

But alienation is not the only problem. What is to happen about management and control of the thing in which all these interests subsist? There would be advantages in giving practical charge of the thing to the person with the interest in possession, who has the present right of enjoyment, but there would be disadvantages too – it can put her in a very difficult position with serious conflicts of interest. Who is to ensure that she does indeed take only the income-type benefit and not consume any capital? And who is to ensure that the thing will continue to provide long-term income benefits for future interest holders, and that its capital value is preserved?

One way out of these difficulties is to use a trust. We look at this more closely below, but in essence it involves taking management and control out of the hands of the successive interest holders and giving them, together with absolute title to the thing, to a trustee (in practice, usually two trustees, for reasons considered below). The trustee then has the capacity to deal with the property as absolute owner, and also the power to manage and control it, but in all these matters he will be required to act in the interests of the successive interest holders, balancing their respective interests where they conflict. The use of a trust is in fact mandatory whenever an interest in land is divided into successive time slices (as for example when my aunt's lease of her studio was given to me for my lifetime in the example above) and it is also usual where there are successive interests in money or in other things which are either fungible (consider why) or non-commercial (consider why), or where there are inchoate future interests, or interest holders who are minors (again,

consider why). So, in the studio and piano examples above, when my aunt made the gift she would have had to transfer the lease to a trustee to hold on trust for me for my lifetime then for you or her, and for convenience she probably would have done the same thing with the piano, although it would not have been essential.

An alternative way of dividing ownership of land and goods is to use leasehold durations. The owner grants the lessee possession of the land or the object for either a fixed period (say ninety-nine years, as in the studio example) or a periodic duration (as for example when a landlord grants you a monthly tenancy of a flat, which either you or the landlord can terminate at any time by giving the other one month's notice to quit). When land-holding is divided up into leasehold durations no trust is necessary.

8.2.5. Interests of contingent duration

So far we have been considering only those contingent interests where the happening of the contingency triggers off the commencement of enjoyment. However, contingencies may mark the end of an interest as well as its beginning. An interest of contingent duration (a right to something until the happening of an event which may never happen, or subject to forfeiture if it happens) can be carved out of a fixed duration interest as well as out of an interest of indefinite duration.

In either case, the principle of residuarity applies, in just the same way as when an interest of a fixed duration is carved out of a longer interest or one of indefinite duration. So, whenever an interest of a contingent duration arises, an alternate interest automatically vests in someone else – if you give me your car until I marry, you automatically (unless you specify another destination for it) acquire a reversionary right to have the car back if and when I do marry. For every interest of contingent duration, there exists in the wings another interest where the commencement of enjoyment depends on the happening of the contingency which will end the contingent duration interest. It may of course happen that there comes a point when it is certain that the contingency can never occur (I die unmarried, for example). If and when that happens, the alternate interest lapses, and the contingent duration interest (my right to the car until I marry) loses its limitation – in this case there will be nothing to now stop it continuing indefinitely, so that I will die owning the car absolutely.

There are two ways in which an interest can have a contingent length like this, and although superficially they look similar they are significantly different in effect. The first is where the duration of the interest is from the outset measured by reference to the happening of the future contingent event: the example just given comes within this category. This is a determinable interest. The second is where the interest is made *terminable* on the happening of the contingency (you give me your car, but reserve the right to take it back if I marry). This is an interest subject to a condition subsequent.

8.2.5.1. Determinable interests

The distinguishing feature of a determinable interest is that, on the happening of the future contingency, the determinable interest itself automatically expires, and the alternate reversionary/remainder interest waiting in the wings (here called a 'possibility of reverter') is automatically converted into an absolute, unconditional entitlement. This automatic transmission of title from one person to another is potentially dangerous: there is nothing to alert outsiders to the change in entitlement, and even the parties themselves may be unaware that it has happened. For this reason, such interests are nearly always now created under a trust, so that the title is vested in a trustee, who is required to hold the property on trust first for the determinable interest holder until the contingency occurs, and then on trust for the reversioner. Outsiders therefore deal only with the trustee and are not concerned with whether the beneficial interest has shifted from the determinable interest holder to the reversioner, and the duty of ensuring that the benefit goes to the reversioner once the contingency has occurred is placed on the trustee. This use of a trust is compulsory if the determinable interest is in freehold (as opposed to leasehold) land: the Law of Property Act 1925, Schedule 1, Part I, converted all legal determinable fee simple and determinable life interests into equitable interests under a trust.

8.2.5.2. Interests subject to a condition subsequent

An interest subject to a condition subsequent is quite different. It is essentially an interest of a specified duration (it could be perpetual, or limited to a life time, or to a period of years) which will become terminable prematurely if and when a future event occurs. The conceptual difference from a determinable interest is that, whereas in the latter the contingency measures the duration of the interest, in the former it defeats or forfeits an interest prematurely. However, the practical difference is that, in the case of an interest subject to a condition subsequent, none of this happens automatically. Instead of automatically terminating the interest, the contingency merely gives the alternate interest holder the right to elect to forfeit the interest. The terminology is that the creation of an interest subject to a condition subsequent automatically confers on someone else a right of entry (alternatively called a right to forfeit), and the happening of the contingency makes that right of entry or forfeiture exercisable. Unless and until it is exercised, the original interest continues.

This leads to two important further differences from determinable interests. First, because the shift in title requires a positive, provable act on the part of the holder of the right of entry or forfeiture, there is no great difficulty in ascertaining whether it has occurred or not. Consequently, there is no particular reason to hide these interests behind a trust, and in practice a trust would not normally be used here, even if the interest is in freehold land. The provisions of the Law of Property Act 1925 which impose a trust whenever there are successive interests in freehold

land do not apply to a fee simple interest subject to a condition subsequent, and section 7 of the 1925 Act specifically provides that a fee simple subject to a right of entry is to be treated as a fee simple absolute (i.e. not subject to a contingency) and is therefore capable of being legal rather than merely equitable (a distinction we consider further in section 8.3 below).

The second difference is in the attitude of the law. A determinable contingency is regarded more or less neutrally, as an event marking the passing of benefit from one person to another. Rights of entry or forfeiture, on the other hand, are regarded as essentially punitive. The contingency making them exercisable tends to be a breach of an obligation, or the happening of an event which the grantor of the interest wanted to discourage (classically in family settlements, inappropriately marrying or not marrying). This has led to two consequences. The first is that the courts have tended to construe conditions subsequent much more strictly than determinable conditions. The second is that equity has evolved an extensive jurisdiction to grant relief against forfeiture of an interest by the exercise of a right of entry or forfeiture, on the basis that the right was conferred only as security for performance of the obligation, and if that can be secured in some other way, the interest ought to be allowed to continue.

8.2.5.3. Distinguishing determinable and forfeitable interests

Despite this real distinction between determinable and forfeitable interests, and the very real difference in their consequences and effects, the courts have traditionally regarded it as a matter of form rather than substance, allowing it to depend on the wording used rather than the intention of the grantor. So, a grant of a right to enjoyment 'during' a state of affairs, or 'while' it continues or even 'until' it stops, will usually be taken to create a determinable interest, automatically ending when the contingency arises, while a right of enjoyment 'provided that' or 'on condition that' a future event does not happen, or 'but [terminable] if' it does happen, will create an interest subject to a condition subsequent.

8.2.6. Requirement of certainty

Whether a contingency triggers off enjoyment, measures the duration of an interest, or confers on someone a right to terminate it prematurely, the contingency must be certain. If it is not certain, it will be void, the consequences of which are considered in section 8.2.7 below.

However, 'certainty' is a notoriously slippery concept. The basic rule in this context is that a contingency must be certain in the sense of being objectively ascertainable as a matter of fact, even if difficult to prove in practice. So, if I give you an option to buy my land next Wednesday 'if the weather is bad on the immediately preceding Tuesday', your option is void because the contingency is uncertain: bad weather is a matter of opinion not a matter of fact ('if more than one inch of rain falls in my garden on Tuesday' would do). Another way of putting it, and one that makes sense of the rule, is that the contingency must be

such that, *at the time when the parties need to know*, it will be objectively ascertainable whether or not the contingency has occurred. So, I can direct my trustees to pay the income of a £10,000 trust fund to the Royal Shakespeare Company 'while it continues its present policy of regularly staging plays by Shakespeare' but not 'for so long as the present high standard of verse-speaking in its Shakespeare productions is maintained'. In such a gift, where income is to be paid indefinitely unless and until a contingency occurs, the trustees need to be able to ascertain the point at which to stop paying. In the first case the trustees should have no difficulty in spotting an official change in policy (which presumably would require some formal process or public announcement) whereas in the second it would be a matter of subjective judgment whether, at any particular point in time, standards of verse-speaking could be said to be no longer what they were.

However, the line between subjective judgment and objective ascertainment is not always tightly drawn, and the courts are more flexible in some cases than in others. For example, forfeiting contingencies tend to be construed more strictly than those measuring duration (another real distinction between interests subject to a condition precedent and determinable interests), whereas those that trigger off entitlement are construed less strictly than either.

Further, in some cases, the courts are not satisfied with objective ascertainability at the point when the parties need to know, and require in addition that the parties should be able to predict in advance when, if at all, the contingency will occur. This very narrow concept of certainty has recently been reaffirmed as the one appropriate to the long-established rule that the duration of a lease must be certain. When measuring the permissible duration of leases, the lease will not be valid unless each party knows from the outset the maximum duration of its liability under the lease. This means that, although I can create a valid trust of my land for my daughter 'until the highways authority certifies that the land is required by the local authority for road-widening purposes' (because although we do not know when, if ever, this will happen, we do know that we will know that it has happened when it does happen), I cannot lease the same land to her for a duration described as 'until the highways authority certifies the land is required by the local authority for road-widening purposes': see *Prudential Assurance* v. *London Residuary Body* [1992] 2 AC 386, in which the House of Lords reaffirmed the strict rules for certainty of duration of leases, considered in Chapter 17 where the effect of such a grant, and the rationale of the rule, are considered in more detail.

8.2.7. Successive interests in land and the doctrine of tenures and estates

As we saw in Chapter 6, the primary method of classifying interests in land is by duration. This is true of interests carrying general rights of enjoyment to land, and also of some rights of particular user such as easements and profits, but for the moment we will focus on general use rights. There are two distinct systems in operation here. One is the ancient system of tenures and estates, and the other is

the rather more recent leasehold system which has been grafted onto the tenure and estates system.

8.2.7.1. Tenures and estates

This classification by duration of enjoyment is derived from the ancient feudal doctrines of tenures and estates, although very little of the elaborate feudal structure now remains, apart from the terminology. As explained in Chapter 6, the feudal theory was that land was 'owned' by the Crown, and let out to subjects on various types of holding ('tenures') which required the holder to perform services for the Crown in exchange for enjoyment of the land, each type of tenure requiring a different type of service. A holder of a tenure from the Crown could then 'subinfeudate' (in effect, sublet, although modern lease terminology is best avoided here). This would mean that the right to enjoy the land would be sub-contracted to someone else, for a different (or even the same) type of tenure, in return for services to be performed by the sub-holder to the original holder, and the sub-holder could then himself sub-subinfeudate to someone else. Consequently, a pyramid of tenures could build up, so that, in respect of any given piece of land, there would be one person who held directly from the Crown, delivering the appropriate services, and then a chain of sub- and sub-sub-holders, each sub-contracting rights of enjoyment in exchange for services, down to the person who actually had physical use of the land.

Each of these tenures could last for various permissible durations ('estates'). So, in feudal theory, 'tenure' described the nature of the land-holding – what you had to do in order to be permitted to enjoy the land – and 'estate' described the duration of the holding – how long this enjoyment would be permitted to last.

Detailed knowledge of the different types of tenure and estate that could exist is no longer necessary for an understanding of our present system. However, it does help to appreciate the underlying principles of sovereignty and power, the inherently personal nature of the system, and the way it was engrafted onto the pre-existing land-holding and land-using systems. This assumed contemporary significance in Australia when the courts had to consider the legal effect of imposing the common law tenures and estates systems on aboriginal land use patterns, and reference should be made here to the analyses of the concepts of tenures and estates given in the judgments in *Mabo (No. 2)* extracted in Chapter 4, and also to Simpson, *A History of the Land Law*. Three other general points might be made here. First, it is probably more accurate to regard feudal theory as an *ex post facto* rationalisation of the Norman conquest rather than as a factual description of how interests in land were in fact created and allocated following the Norman conquest. Secondly, whether literally true or not, the feudal structure almost certainly did not wholly supplant pre-existing property interests, nor was it spread uniformly over the whole country: customary rights and public rights (fishing, navigation, rights of way etc.) are probably pre-feudal in nature.

Thirdly, later developments were pragmatic rather than principled, with legislators showing no interest in preserving the coherence of the feudal structure, so that, even if feudal theory did once give an accurate picture of land-holding, it very soon ceased to do so.

We have never formally abolished this system of classifying land interests according to tenure and estate. However, it has become rationalised and simplified to such an extent that it now does little more than explain the terminology we use when describing land interests, and gives some coherence to what would otherwise seem to be puzzlingly arbitrary rules about what we can and cannot do with land interests in our system.

The most dramatic simplification has been in relation to tenure. Only one of these feudal tenures now survives – freehold tenure – and there are no longer any incidents or services attached to it. Also, it has long been impossible for a holder of land by any tenure to subinfeudate. Since there had always been a natural process of elimination of tenures by forfeiture to the Crown (for example, on dying without an heir) the inevitable result was the eventual collapse of the tenurial pyramid. The consequence of these changes is that all land in this country is now held by freehold tenure (with some relatively trivial Crown land exceptions): a landowner does not own her piece of land, she holds it of the Crown by freehold tenure. But holding land by freehold tenure is identical in effect to owning it: the tenure holder does not have to make any payments or perform any services to the Crown, and is fully entitled to full ownership-type rights in the land, except in so far as she has passed some or all of them on to someone else by using one of the modern fragmentation devices described in this chapter.

As far as estates are concerned, the present system bears less resemblance to its feudal origins. There are now only two types of estate deriving from the feudal system. The first is the fee simple estate (sometimes called the freehold estate), a genuine relic of the feudal system, which denotes indefinite, or perpetual, duration. The second is the life estate, which measures duration by reference to a specific person's life. This also is a genuine relic of the feudal system, but it is now of little significance because it is confined to equitable interests under a trust of land – the only way in which land can be held for a duration measured by reference to a life is for it to be held on trust for a person whose interest has that duration.

So, a person who we would regard as owner of a piece of land technically does not own the land but holds it by freehold tenure for an estate in fee simple. Section 1 of the Law of Property Act 1925 then refines this further by providing that the property interest that such a person has will not be a legal interest (more properly termed a legal estate) unless the fee simple estate is absolute (in the sense of being unconditional) and in possession (as opposed to in reversion or in remainder). Putting all this together, it means that the person who appears to the outside world to be the full owner of land holds the land by freehold tenure for a legal estate in fee simple which is absolute and in possession.

8.2.7.2. Estates in particular use rights

Estates are also used to measure the duration of particular use rights, most notably easements and profits. Easements and profits are usually granted for a fee simple duration (i.e. to last perpetually) and the same applies to those that arise by long use through prescription (logically, since prescription is based on a presumed original grant, as we see in Chapter 13). They can also be granted for a leasehold duration (see below). Again, section 1 of the Law of Property Act 1925 has refined this further, and provides that easements and profits will only take effect as legal interests if for a duration equivalent to an estate in fee simple which is absolute (i.e. unconditional) and in possession (as opposed to in remainder or in reversion), or if for a leasehold duration which is absolute. The permissible leasehold durations are outlined below.

8.2.7.3. Leases

The leasehold system developed separately from the tenures and estates system, but was grafted onto it so that the two are now fully integrated. Confusingly, terminology borrowed from the tenurial system is sometimes used in relation to leases, so one occasionally sees a reference to a leasehold estate or leasehold tenure, but this has nothing to do with the feudal-based tenures and estates system. ‘Leasehold estate’ or ‘leasehold tenure’ simply denotes an interest in land which lasts for a leasehold duration or to an entitlement to possession of land for a leasehold duration. Also, the term ‘tenant’, which would once have been used to describe someone who holds a feudal tenure, is now generally used to describe the person who holds a lease.

A lease is an entitlement to possession of land for a prescribed duration. The four permissible types of duration are explained below. A lease can only come into existence by being carved out of a fee simple interest or out of a lease for a longer duration. In other words, a fee simple owner (i.e. a person who holds land by freehold tenure for an estate in fee simple absolute in possession) creates a lease of the land by granting to the lessee the right to possession of the land for one of the four permissible durations, and a person who already holds a lease can grant someone else a sublease by granting him possession for a lesser duration.

Leases are categorised according to their duration. The only permissible categories are a fixed-term lease (where possession is granted for a fixed length of time), a periodic lease (which continues indefinitely for successive periods, usually of a week, a month, a year or two years, until terminated by either party serving notice to quit on the other), a tenancy at will (which can be terminated by either party at any time) and a tenancy at sufferance (where the tenant is present only at the sufferance of the landlord, and can be made to leave at any time). We look at all this in more detail in Chapter 17.

For all practical purposes, ‘lease’ means the same as ‘tenancy’. The former tends to be used for longer fixed-term interests and the latter for shorter and periodic interests, and for interests at will and at sufferance.

8.2.8. Restrictions on the power to create future interests

If I am the holder of a property interest in a resource and the property interest is in possession and is of unlimited duration, then I am free to exploit or preserve the resource as I like (subject to rules about not harming others etc.). I can consume, preserve or alienate the capital, and use or save or otherwise exploit as much of the income value as I like. In classic economic theory, this promotes the most efficient use of the resource in which I have the interest: if someone values it more highly than I do because he could use it more efficiently, there are no obstacles to prevent its transfer from me to him at a price advantageous to each of us.

However, if I exercise my freedom to do as I like with the resource by creating successive limited interests in it, then I am limiting the freedom of action of my successors to make use of the resource in the way they consider most appropriate. Unsurprisingly, therefore, there have always been limitations on the power of an owner to fragment ownership by dividing it up into successive interests of limited duration. These rules – the most important of which is the rule against perpetuities – are outside the scope of this book, but essentially they involve restricting the owner's right to create unlimited successive future interests by invalidating the offending future interests. For an analysis of these rules, their present effect and utility, and recommendations for their reform, reference should be made to Law Commission, *The Rule Against Perpetuities and Excessive Accumulations* (Law Commission Report No. 251, 1998).

8.3. Legal and equitable interests

In this jurisdiction, all property interests can be categorised as either legal or equitable. There are three questions to be considered here. First, what does the distinction between legal and equitable mean? Secondly, which interests are legal and which are equitable? And, thirdly, what are the consequences of categorising an interest as legal rather than equitable?

8.3.1. Origin of the legal/equitable distinction

Equitable interests were originally those property interests that were recognised by the Chancery courts but not by the common law courts. There were several circumstances in which the Chancery courts would regard someone other than the legal title holder as having a proprietary interest in a thing. These can be divided into two main types – the 'failed formality' type of interest, and the 'novel' type of interest.

8.3.1.1. Failed formality interests

This is essentially a matter of title and is dealt with in detail in Chapters 10 and 12, but for present purposes the important point is that the common law would (and still does) require various specific formalities to be complied with before it would

recognise that a property interest had been transferred or granted by one person to another. For example, if I want to grant you a ten-year lease of my house, I must do so by executing a deed: if I do not use a deed, you will not get a legal lease even if you move in and pay the agreed rent and we both act throughout the ten years as if you had the lease which I have purported to grant you. However, the Chancery courts were more flexible, and in certain circumstances they would regard you as having a lease even though all the requirements for creating a valid legal lease had not been observed. You would then have an equitable lease rather than a legal lease. This still applies today, and it applies to any type of property interest: all property interests that can be legal (fee simple interests in land, leases, mortgages, easements, choses in action such as the right to sue on a debt) can also be equitable, and the way to tell whether the interest is legal or equitable is to look at the way in which it was created or transferred to the present holder.

8.3.1.2. Novel interests

In addition, the Chancery courts created or recognised some proprietary interests which had no legal equivalent. As Neave *et al.*, in *Sackville and Neave* explain, these were interests 'developed by equity to mitigate the harshness of rigid common law rules and to satisfy a commercial need which the common law left unfulfilled'. The most obvious example is the one that arose out of equity's creation of the institution of the trust, which split entitlement to benefit from a thing from management and control of it. This was done by requiring the legal owner of a thing to use it not for his own benefit but for the benefit of someone else. The proprietary interest of the beneficiary is equitable, and there is no legal counterpart. The equitable interest of a beneficiary under a trust is not the only novel property interest created by equity and which has no legal equivalent. Others include the restrictive covenant (considered in Chapter 6), estate contracts and options to purchase (considered in Chapter 12), and both the charge and the mortgagor's equity of redemption (Chapter 18). Consequently, although there are equitable equivalents of all interests that can exist as legal interests, the reverse is not true: some equitable interests have no legal equivalent.

8.3.2. Legal and equitable interests now

Once the jurisdictions of the common law and Chancery courts were merged, all courts recognised both legal and equitable property interests, but continued to categorise them as legal or equitable, depending on the jurisdiction in which they originated and the way in which they were created or transferred. This distinction between legal and equitable status has been perpetuated, for reasons which will become apparent below, but some significant changes in the content of each category have been made by statute. First, there have been some additions: whenever a new property interest is now created by statute, it will be expressly stated whether the interest is to be legal or equitable. So, for example, the spouse's statutory right of occupation in the matrimonial home created by the Matrimonial

Homes Act 1967 (now in the Family Law Act 1996) and considered in Chapter 9 is stated to take effect 'as if' it were an equitable interest.

Secondly, some long-established property interests have been recategorised. This has been particularly significant in relation to interests in land.

8.3.2.1. Interests in land

In the case of land, the most significant recategorisation was made by the Law of Property Act 1925, which aimed to limit the number of legal interests that could co-exist in any one piece of land. As part of this process, it recategorised some legal interests as equitable and produced a short, definitive and closed list of interests which could be legal. As a result, some types of interest such as a life estate in land, which before 1925 could be either legal or equitable depending on how it was created, can now only be equitable. This definitive list of legal interests appears as section 1 of the Law of Property Act 1925. Any interest that appears on this list can be either legal or equitable: which it is, in any particular case, will depend on how it was created or transferred to the present holder. Any interest not on the list can only be equitable, unless it is a novel interest subsequently created by statute and expressly stated to take effect as if it was legal.

8.3.2.2. Interests in goods

The structure of legal and equitable interests in goods is much less complex. Legal (as opposed to equitable) ownership of goods is often said to be indivisible: the only legal interests recognised are ownership, mortgage (although since in goods this involves transfer of ownership it is not really a separate category) and bailment. Since, as we see in Chapter 17, the proprietary status of bailment is not beyond dispute, this leaves a very short list indeed. Apart from these, all other interests in goods are equitable.

8.3.3. The significance of the legal/equitable distinction

The major differences between legal and equitable interests are that the formalities necessary for their creation and transfer are different, and, in general, legal interests are enforceable against a wider range of third parties than equitable interests. Both these points are dealt with in detail in Chapters 12–14.

8.3.4. Three common fallacies

At the risk of introducing confusion where none was felt before, it is worth mentioning here three common fallacies about the distinction between equitable and beneficial interests and trusts and beneficial interests, and the interrelation of legal and equitable interests. They are all considered further by Lord Browne-Wilkinson in *Westdeutsche Landesbank* v. *Islington London Borough Council* [1996] AC 669 (Extract 8.1 below).

8.3.4.1. Equitable interests and beneficial interests

Because the interest of a beneficiary under a trust is such a well-known equitable interest, the terms 'beneficial interest' and 'equitable interest' are often confused and used interchangeably, as if they mean the same thing. They do not. The interest of a beneficiary under a trust is a beneficial interest, and a legal owner of a thing who is entitled to it for his own benefit is sometimes referred to as the legal and beneficial owner. The beneficial interest of a beneficiary under a trust in necessarily an equitable interest, but, as we have seen, it is just one of many different types of equitable interest – an equitable interest is not necessarily a beneficial interest.

8.3.4.2. Over-identification of equitable interests with trusts

The second fallacy follows on from the first. It is often assumed that a trust arises whenever ownership is fragmented between legal and equitable interest holders, and whenever a legal title holder has no right to beneficial use. Neither is true. The first is self-evident: if I grant you a restrictive covenant or an equitable charge over my legal fee simple interest in land, no trust arises. The second is apparent from the next section in this chapter: there are many other ways of fragmenting management, control and benefit apart from by using a trust.

8.3.4.3. Absolute ownership does not include equitable beneficial ownership

The third fallacy is the assumption that an absolute owner has both legal ownership and the (or an) equitable beneficial interest in the thing. This arises out of a fundamental misunderstanding of the way fragmentation of property interests works. The equitable interests of beneficiaries under a trust are beneficial interests, in the sense that they are interests that carry with them a right to the benefit of the property. However, not all interests that include the right to take the benefit of the property are equitable interests (consider, for example, legal leases). Most importantly for present purposes, absolute owners (in the Honoré sense) are entitled to the benefit of the thing owned, but it would be wrong to say that they have an equitable interest in the thing: it is their legal interest in the thing that entitles them to beneficial enjoyment, and will continue to do so unless and until either they transfer it to someone else by a legal disposition, or equity steps in and allocates it elsewhere, by recognising someone other than a legal interest holder as the person entitled to beneficial enjoyment.

Extract 8.1 ***Westdeutsche Landesbank Girozentrale*** **v.** ***Islington London Borough Council*** **[1996] AC 669**

[In the *Westdeutsche* case, the bank had paid money over to the local authority pursuant to a contract which was subsequently held to be void (because it was held to be *ultra vires* for a local authority to enter into a finance agreement of that type). When the local authority received the money, it paid it into a bank account also

containing money from other sources: at that point, neither the local authority nor the bank knew that there was anything wrong with the transaction. Once it was established that the transaction was *ultra vires*, it was accepted that the local authority had to repay the money, but the bank argued that, because the money was paid under a void contract, the local authority held it on resulting trust for the bank. The House of Lords rejected the bank's argument. During the course of his judgment, Lord Browne-Wilkinson said this:]

The bank submitted that, since the contract was void, title did not pass at the date of payment either at law or in equity. The legal title of the bank was extinguished as soon as the money was paid into the mixed account, whereupon the legal title became vested in the local authority. But, it was argued, this did not affect the *equitable* interest, which remained vested in the bank (the retention of title point). It was submitted that, whenever the legal interest in property is vested in one person and the equitable interest in another, the owner of the legal interest holds it on trust for the owner of the equitable title: 'the separation of the legal from the equitable interest necessarily imports a trust.' . . .

THE BREADTH OF THE SUBMISSION

Although the actual question in issue on the appeal is a narrow one, on the arguments presented it is necessary to consider fundamental principles of trust law. Does the recipient of money under a contract subsequently found to be void for mistake or as being *ultra vires* hold the moneys received on trust even where he had no knowledge at any relevant time that the contract was void? If he does hold on trust, such trust must arise at the date of receipt or, at the latest, at the date the legal title of the payer is extinguished by mixing moneys in a bank account: in the present case it does not matter at which of those dates the legal title was extinguished. If there is a trust two consequences follow: (a) the recipient will be personally liable, regardless of fault, for any subsequent payment away of the moneys to third parties even though, at the date of such payment, the 'trustee' was still ignorant of the existence of any trust (see [Burrows, 'Swaps and the Friction Between Common Law and Equity' (1995) 3 *Restitution Law Review* 15]); (b) as from the date of the establishment of the trust (i.e. receipt or mixing of the moneys by the 'trustee') the original payer will have an equitable proprietary interest in the moneys so long as they are traceable into whomsoever's hands they come other than a purchaser for value of the legal interest without notice. Therefore, although in the present case the only question directly in issue is the personal liability of the local authority as a trustee, it is not possible to hold the local authority liable without imposing a trust which, in other cases, will create property rights affecting third parties because moneys received under a void contract are 'trust property'.

THE PRACTICAL CONSEQUENCES OF THE BANK'S ARGUMENT

Before considering the legal merits of the submission, it is important to appreciate the practical consequences which ensue if the bank's arguments are correct. Those who suggest that a resulting trust should arise in these circumstances accept that the

creation of an equitable proprietary interest under the trust can have unfortunate, and adverse, effects if the original recipient of the moneys becomes insolvent: the moneys, if traceable in the hands of the recipient, are trust moneys and not available for the creditors of the recipient. However, the creation of an equitable proprietary interest in moneys received under a void contract is capable of having adverse effects quite apart from insolvency. The proprietary interest under the unknown trust will, quite apart from insolvency, be enforceable against any recipient of the property other than the purchaser for value of a legal interest without notice . . .

THE RELEVANT PRINCIPLES OF TRUST LAW

(i) Equity operates on the conscience of the owner of the legal interest. In the case of a trust, the conscience of the legal owner requires him to carry out the purposes for which the property was vested in him (express or implied trust) or which the law imposes on him by reason of his unconscionable conduct (constructive trust).
(ii) Since the equitable jurisdiction to enforce trusts depends upon the conscience of the holder of the legal interest being affected, he cannot be a trustee of the property if and so long as he is ignorant of the facts alleged to affect his conscience, i.e. until he is aware that he is intended to hold the property for the benefit of others in the case of an express or implied trust, or, in the case of a constructive trust, of the factors which are alleged to affect his conscience.
(iii) In order to establish a trust there must be identifiable trust property. The only apparent exception to this rule is a constructive trust imposed on a person who dishonestly assists in a breach of trust who may come under fiduciary duties even if he does not receive identifiable trust property.
(iv) Once a trust is established, as from the date of its establishment the beneficiary has, in equity, a proprietary interest in the trust property, which proprietary interest will be enforceable in equity against any subsequent holder of the property (whether the original property or substituted property into which it can be traced) other than a purchaser for value of the legal interest without notice.

These propositions are fundamental to the law of trusts and I would have thought uncontroversial. However, proposition (ii) may call for some expansion. There are cases where property has been put into the name of X without X's knowledge but in circumstances where no gift to X was intended . . . These cases are explicable on the ground that, by the time action was brought, X or his successors in title have become aware of the facts which gave rise to a resulting trust; his conscience was affected as from the time of such discovery and *thereafter* he held on a resulting trust under which the property was recovered from him. There is, so far as I am aware, no authority which decides that X was a trustee, and therefore accountable for his deeds, at any time before he was aware of the circumstances which gave rise to a resulting trust.

Those basic principles are inconsistent with the case being advanced by the bank. The latest time at which there was any possibility of identifying the 'trust property' was the date on which the moneys in the mixed bank account of the local authority ceased to be traceable when the local authority's account went into overdraft in June 1987. At that date, the local authority had no knowledge of the invalidity of the contract but regarded

the moneys as its own to spend as it thought fit. There was therefore never a time at which both (a) there was defined trust property and (b) the conscience of the local authority in relation to such defined trust property was affected. The basic requirements of a trust were never satisfied ...

THE RETENTION OF TITLE POINT

It is said that, since the bank only intended to part with its beneficial ownership of the moneys in performance of a *valid* contract, neither the legal nor the equitable title passed to the local authority at the date of payment. The legal title vested in the local authority by operation of law when the moneys became mixed in the bank account but, it is said, the bank 'retained' its equitable title.

I think this argument is fallacious. A person solely entitled to the full beneficial ownership of money or property, both at law and in equity, does not enjoy an equitable interest in that property. The legal title carries with it all rights. Unless and until there is a separation of the legal and equitable estates, there is no separate equitable title. Therefore, to talk about the bank 'retaining' its equitable interest is meaningless. The only question is whether the circumstances under which the money was paid were such as, in equity, to impose a trust on the local authority. If so, an equitable interest arose for the first time under that trust.

This proposition is supported by ... *Vandervell* v. *Inland Revenue Commissioners* [1967] 2 AC 291 at 311, 317 *per* Lord Upjohn and Lord Donovan, *Commissioner of Stamp Duties* v. *Livingston* [1965] AC 694 at 712 [see Notes and Questions 8.2 below] and Underhill and Hayton, *Law of Trusts and Trustees* (15th edn, 1995), p. 866.

THE SEPARATION OF TITLE POINT

The bank's submission, at its widest, is that, if the legal title is in A but the equitable interest in B, A holds as trustee for B.

Again, I think this argument is fallacious. There are many cases where B enjoys rights which, in equity, are enforceable against the legal owner, A, without A being a trustee, for example an equitable right to redeem a mortgage, equitable easements, restrictive covenants, the right to rectification ... Even in cases where the whole beneficial interest is vested in B and the bare legal interest is in A, A is not necessarily a trustee, for example where title to land is acquired by estoppel as against the legal owner; a mortgagee who has fully discharged his indebtedness enforces his right to recover the mortgaged property in a redemption action, not an action for breach of trust.

The bank contended that where, *under a pre-existing trust*, B is entitled to an equitable interest in trust property, if the trust property comes into the hands of a third party, X (not being a purchaser for value of the legal interest without notice), B is entitled to enforce his equitable interest against the property in the hands of X because X is a trustee for B. In my view the third party, X, is not necessarily a trustee for B: B's equitable right is enforceable against the property in just the same way as any other specifically enforceable equitable right can be enforced against a third party. Even if the third party, X, is not aware that what he has received is trust property B is entitled to

assert his title in that property. If X has the necessary degree of knowledge, X may himself become a constructive trustee for B on the basis of knowing receipt. But unless he has the requisite degree of knowledge he is not personally liable to account as trustee: *Re Diplock's Estate* [[1951] AC 251] and *Re Montagu's Settlement Trusts* [1987] Ch 264. Therefore, innocent receipt of property by X subject to an existing equitable interest does not by itself make X a trustee despite the severance of the legal and equitable titles. Underhill and Hayton, *Law of Trusts and Trustees*, pp. 369–70, while accepting that X is under no personal liability to account unless and until he becomes aware of B's rights, does describe X as being a constructive trustee. This may only be a question of semantics: on either footing, in the present case the local authority could not have become accountable for profits until it knew that the contract was void.

RESULTING TRUST

This is not a case in which the bank had any equitable interest which pre-dated receipt by the local authority of the upfront payment. Therefore, in order to show that the local authority became a trustee, the bank must demonstrate circumstances which raised a trust for the first time either at the date on which the local authority received the money or at the date on which payment into the mixed account was made. Counsel for the bank specifically disavowed any claim based on a constructive trust. This was plainly right because the local authority had no relevant knowledge sufficient to raise a constructive trust at any time before the moneys, upon the bank account going into overdraft, became untraceable. Once there ceased to be an identifiable trust fund, the local authority could not become a trustee: *Re Goldcorp Exchange Ltd (in receivership)* [1995] 1 AC 74 [see further Chapter 12]. Therefore, as the argument for the bank recognised, the only possible trust which could be established was a resulting trust arising from the circumstances in which the local authority received the upfront payment.

Under existing law a resulting trust arises in two sets of circumstances:

(A) Where A makes a voluntary payment to B or pays (wholly or in part) for the purchase of property which is vested either in B alone or in the joint names of A and B, there is a presumption that A did not intend to make a gift to B: the money or property is held on trust for A (if he is the sole provider of the money) or in the case of a joint purchase by A and B in shares proportionate to their contributions. It is important to stress that this is only a *presumption*, which presumption is easily rebutted either by the counter-presumption of advancement or by direct evidence of A's intention to make an outright transfer: see *Underhill and Hayton*, pp. 317 *et seq.*, *Vandervell* v. *Inland Revenue Commissioners* [1967] 2 AC 291 at 312 *et seq.* and *Re Vandervell's Trusts (No. 2)* [1974] Ch 269 at 288 *et seq.*

(B) Where A transfers property to B *on express trusts*, but the trusts declared do not exhaust the whole beneficial interest: *ibid.* and *Barclays Bank Ltd* v. *Quistclose Investments Ltd* [1970] AC 567.

Both types of resulting trust are traditionally regarded as examples of trusts giving effect to the common intention of the parties. A resulting trust is not imposed by law

against the intentions of the trustee (as is a constructive trust) but gives effect to his presumed intention. Megarry J in *Re Vandervell's Trusts (No. 2)* suggests that a resulting trust of type (B) does not depend on intention but operates automatically. I am not convinced that this is right. If the settlor has expressly, or by necessary implication, abandoned any beneficial interest in the trust property, there is in my view no resulting trust: the undisposed-of equitable interest vests in the Crown as *bona vacantia*: see *Re West Sussex Constabulary's Widows, Children and Benevolent (1930) Fund Trusts* [1971] Ch 1.

Applying these conventional principles of resulting trust to the present case, the bank's claim must fail. There was no transfer of money to the local authority on express trusts: therefore a resulting trust of type (B) above could not arise. As to type (A) above, any presumption of resulting trust is rebutted since it is demonstrated that the bank paid, and the local authority received, the upfront payment with the intention that the moneys so paid should become the absolute property of the local authority. It is true that the parties were under a misapprehension that the payment was made in pursuance of a valid contract. But that does not alter the actual intentions of the parties at the date the payment was made or the moneys were mixed in the bank account. As the article by William Swadling, 'A New Role for Resulting Trusts?' (1996) 16 *Legal Studies* 110 at 133 demonstrates, the presumption of resulting trust is rebutted by evidence of any intention inconsistent with such a trust, not only by evidence of an intention to make a gift.

Professor Birks, 'Restitution and Resulting Trusts', in *Equity and Contemporary Legal Developments*, p. 335 at p. 360, while accepting that the principles I have stated represent 'a very conservative form' of definition of a resulting trust, argues from restitutionary principles that the definition should be extended so as to cover a perceived gap in the law of 'subtractive unjust enrichment' (p. 368) so as to give a plaintiff a proprietary remedy when he has transferred value under a mistake or under a contract the consideration for which wholly fails. He suggests that a resulting trust should arise wherever the money is paid under a mistake (because such mistake vitiates the actual intention) or when money is paid on a condition which is not subsequently satisfied.

As one would expect, the argument is tightly reasoned but I am not persuaded. The search for a perceived need to strengthen the remedies of a plaintiff claiming in restitution involves, to my mind, a distortion of trust principles. First, the argument elides rights in property (which is the only proper subject-matter of a trust) into rights in 'the value transferred' (see p. 361). A trust can only arise where there is defined trust property: it is therefore not consistent with trust principles to say that a person is a trustee of property which cannot be defined. Second, Professor Birks' approach appears to assume (e.g. in the case of a transfer of value made under a contract the consideration for which subsequently fails) that the recipient will be deemed to have been a trustee from the date of his original receipt of money, i.e. the trust arises at a time when the 'trustee' does not, and cannot, know that there is going to be a total failure of consideration. This result is incompatible with the basic premise on which all trust law is built, namely, that the conscience of the trustee is affected. Unless and until

> the trustee is aware of the factors which give rise to the supposed trust, there is nothing which can affect his conscience. Thus neither in the case of a subsequent failure of consideration nor in the case of a payment under a contract subsequently found to be void for mistake or failure of condition will there be circumstances, at the date of receipt, which can impinge on the conscience of the recipient, thereby making him a trustee.

Notes and Questions 8.1

Explain why, according to Lord Browne-Wilkinson, the consequences he notes under the headings 'The breadth of the submission' and 'The practical consequences of the bank's argument' must follow if the local authority holds the money on trust for the bank (see further section 14.2 below on the enforceability and priority of property interests).

8.4. Fragmentation of management, control and benefit

In this section, we consider mechanisms for fragmenting the management, control and benefit aspects of ownership. These mechanisms can be put into three categories. The first is corporate property holding, where property is held by an artificial legal person such as a company. The second is managerial property holding, where property is held by a non-beneficial owner – in other words, held or controlled by one person for the benefit of another. Examples falling within this second category are where property is held by trustees, or by administrators of the estates of people who have died or gone bankrupt. The third category is group property holding, where property is held not by a single person but by a group of people for their own benefit, whether as co-owners or as communal owners (a distinction we will look at more closely later on).

These three categories are not exclusive: artificial persons can be co-owners and can also hold property on behalf of others as managerial owners. So, for example, it is quite common to have a trust where the trust property is jointly held by two companies on trust for (say) their employees. However, for the present we will consider each category in isolation.

8.4.1. Corporate property holding

A corporation is, in law, a person in its own right and as such it has many of the attributes of a real person – it can hold property, enter into contracts, commit torts and crimes, and sue and be sued in the courts. But of course it cannot itself make decisions to do any of these things, or take any action to implement those decisions – all this has to be done by human persons acting on its behalf. So, while it makes perfect sense to say that a corporation holds property for its own benefit, it is not quite the same thing as saying that a human person holds property for her own benefit. A human person who owns a book can be left to decide for herself what to do

with it, whether to read it, sell it at a profit or a loss, give it away, or destroy it. If a corporation owns the book, none of these things can happen unless some human person decides that they shall happen. Who makes these decisions, and for whose benefit, and who controls the decision-maker?

There are different types of corporation, but by far the most important (numerically and economically) in this jurisdiction is the limited liability company. In a limited liability company, as Harold Demsetz explains in Extract 8.2 below, the company itself owns its assets and its shareholders own shares in the company. The company's assets consist initially of money supplied by the shareholders in exchange for shares in the company issued to them. The shareholders' liability is limited in that they cannot be called on to provide any more money to meet the liabilities of the company: once the company has been formed and the shareholders have paid the full price of their shares over to the company, the only assets available to meet claims by creditors of the company are those owned by the company. In other words, by joining in the formation of a company or buying shares subsequently issued by it, a shareholder chooses how much of his personal wealth to risk in the enterprise to be carried out by the company.

In traditional theory, ownership of the company's assets is fragmented in the following way. Title to the assets is held by the company, but the assets themselves are managed by the board of directors, who are required to use the assets to carry out the purposes for which the company was formed, in order to provide a profit for the shareholders. This profit is distributed to the shareholders by way of dividends on their shares from time to time declared by the board. The board's management of the assets is controlled by the shareholders, who have the power to appoint and dismiss the directors, and whose consent (given by voting at company meetings) is required for the exercise of various powers.

If this model provided an accurate description of the way in which companies operate in practice, then, according to classical economic theory, they ought not to work at all in a market economy. Indeed, Adam Smith (writing before the rise of the limited liability company) thought it was impossible for a company to function efficiently:

> The directors of such companies ... being the managers rather of other people's money than of their own, it cannot well be expected that they should watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch over their own ... Negligence and profusion ... must always prevail, more or less, in the management of such a company. It is upon this account that joint stock companies [the precursor of the modern limited liability company] ... have seldom been able to maintain the competition against private adventurers. They have, accordingly, very seldom succeeded without an exclusive privilege, and frequently have not succeeded with one. Without an exclusive privilege they have commonly mismanaged the trade. With an exclusive privilege they have both mismanaged and confined it. (Smith, *The Wealth of Nations*, vol. II, p. 229)

This objection to corporate ownership is more fundamental than might at first sight appear. The problem is not simply inadequate control over management: as we see below, there are many different ways in which controls can and have been built into the basic corporate mechanism. The real objection, as Berle and Means first pointed out in their classic analysis of corporate property holding in 1932, *The Modern Corporation and Private Property* (Extract 8.3 below), is that corporate ownership subverts the profit function which Adam Smith considered integral to the efficiency and social utility of private property.

However, the fact is that most business enterprises do in practice choose to operate through the medium of a limited liability company, and, contrary to Adam Smith's experience, there is no modern evidence that they do so less efficiently than individually owned businesses. How then can this apparent gap between theory and practice be explained?

One possible answer lies in the fact that the strict division between management, control and benefit described in the traditional analysis of corporate ownership rarely occurs in practice. This is particularly true of the smallest and the largest companies.

Take first the case of small companies, which numerically form the vast proportion of all companies. Most small companies are 'closely held' – i.e. the directors and shareholders are the same people: a study published in 1985 revealed that, in about 80 per cent of British small companies, the directors of the company held 90 per cent or more of the shares (Carsberg *et al.*, *Small Company Financial Reporting*, p. 79). In these companies, the individual shareholder/directors have management and control of the assets and keep all the benefit for themselves, so the division of management, control and benefit is purely notional. Corporate ownership in these cases is therefore practically indistinguishable from individual ownership. Even limited liability is likely to be illusory: individuals trading through close companies will almost certainly be required to mortgage their personal assets and give personal guarantees to secure lending to the company.

In relation to very large companies, the traditional model of corporate ownership is a better match, but it is misleadingly simplistic. For these purposes, largeness can be equated with listing on a stock exchange. These companies of course vary enormously, but there are some typical characteristics that make them radically different from closely held companies. First, in many large companies the board of directors does not manage, but hires and fires others to manage for them. This transforms its function from management to control over management – the function performed in the traditional model by the shareholders. Secondly, control by the board is only part of a complex network of control over management of large companies. In particular, there is massive regulatory control exerted by the listing authorities, partly to protect the interests of the shareholders but mainly to preserve the integrity of the market.

Thirdly, the shareholders have only an attenuated connection with the assets of the company. They have no day-to-day control over management, except in those

comparatively rare cases where a single individual or group of individuals controls a significant proportion of the shares. Leaving aside those exceptional cases, many of the shareholders have never and will never contribute towards the capital of the company. Most of them are not the original suppliers of capital to the enterprise, and although some of them subsequently supplied capital by buying new issues of shares from the company, many of them bought their shares on the stock market, paying the purchase price not to the company but to the shareholder seller. Indeed, many of them have no direct interest in the profitability of the enterprise. While some shareholders buy shares with the long-term aim of earning income in the form of dividends declared on those shares, others do so primarily in order to make a profit on resale of the shares in the market. Consequently, the correlation between the movement of share prices on the stock market and the profitability of the companies in question is not straightforward (see further Hadden, *Company Law and Capitalism*, pp. 71–5, and the review of current theories of correlation between the two by Cheffins, *Company Law: Theory, Structure and Operation*, pp. 54–8).

The allocation of management, control and benefit in these large companies is radically different from that which occurs in the traditional model. Nevertheless, Berle and Means argue that this merely exacerbates the problems of corporate property holding, and that the constraints that make private property efficient and socially beneficial are even less effective in this kind of company than they are in the traditional model.

The Berle and Means thesis was highly influential in its time, as Gregory S. Alexander explains in *Commodity and Propriety* (Extract 8.4 below), although mainstream modern economists concerned with corporate governance now largely reject its assumptions as to the nature of a corporation. On this modern view – the 'nexus of contracts' theory of the company – the artificial legal person, the corporation, is an irrelevance, and the company is more aptly viewed as a network of explicit and implicit bargains entered into voluntarily by individuals who interact on the basis of reciprocal expectations and behaviour. The classic exposition of the nexus of contracts theory is found in 0-Easterbrook and Fischel, *The Economic Structure of Corporate Law*, and see also Cheffins, *Company Law: Theory, Structure and Operation*, pp. 31–47. For a critical analysis rejecting the nexus of contracts approach, see Ireland, 'Company Law and the Myth of Shareholder Ownership': he describes it as 'the company law equivalent of Mrs Thatcher's "there is no such thing as society"'.

Regardless of which theory of the corporation provides the most fruitful approach to questions of corporate governance, for property theorists the Berle and Means thesis remains a useful analysis of the fragmentation of ownership that occurs in corporate property holding and the nature of corporate property holding (see, for example, Jeremy Waldron, *The Right to Private Property*, pp. 57–9, who describes the Berle and Means account as still the best discussion, while taking the

view that corporate property is best seen as ‘a mutation of private property rather than as a distinct form of property in its own right’).

Extract 8.2 Harold Demsetz, ‘Towards a Theory of Property Rights’ (1967) 57 *American Economic Review* 347

The interplay of scale economies, negotiating cost, externalities, and the modification of property rights can be seen in the most notable ‘exception’ to the assertion that ownership tends to be an individual affair: the publicly held corporation. I assume that significant economies of scale in the operation of large corporations is a fact and, also, that large requirements for equity capital can be satisfied more cheaply by acquiring the capital from many purchasers of equity shares. While economies of scale in operating these enterprises exist, economies of scale in the provision of capital do not. Hence, it becomes desirable for many ‘owners’ to form a joint-stock company.

But if all owners participate in each decision that needs to be made by such a company, the scale economies of operating the company will be overcome quickly by high negotiating cost. Hence a delegation of authority for most decisions takes place and, for most of these, a small management group becomes the *de facto* owners. Effective ownership, i.e. effective control of property, is thus legally concentrated in management’s hands. This is the first legal modification, and it takes place in recognition of the high negotiating costs that would otherwise obtain.

The structure of ownership, however, creates some externality difficulties under the law of partnership. If the corporation should fail, partnership law commits each shareholder to meet the debts of the corporation up to the limits of his financial ability. Thus, managerial *de facto* ownership can have considerable external effects on shareholders. Should property rights remain unmodified, this externality would make it exceedingly difficult for entrepreneurs to acquire equity capital from wealthy individuals. (Although these individuals have recourse to reimbursements from other shareholders, litigation costs will be high.) A second legal modification, limited liability, has taken place to reduce the effect of this externality. *De facto* management ownership and limited liability combine to minimize the overall cost of operating large enterprises. Shareholders are essentially lenders of equity capital and not owners, although they do participate in such infrequent decisions as those involving mergers. What shareholders really own are their shares and not the corporation. Ownership in the sense of control again becomes a largely individual affair. The shareholders own their shares, and the president of the corporation and possibly a few other top executives control the corporation.

To further ease the impact of management decisions on shareholders, that is, to minimize the impact of externalities under this ownership form, a further legal modification of rights is required. Unlike partnership law, a shareholder may sell his interest without first obtaining the permission of fellow shareholders or without dissolving the corporation. It thus becomes easy for him to get out if his preferences and those of the management are no longer in harmony. This ‘escape hatch’ is extremely important and has given rise to the organized trading of securities. The

increase in harmony between managers and shareholders brought about by exchange and by competing managerial groups helps to minimize the external effects associated with the corporate ownership structure. Finally, limited liability considerably reduces the cost of exchanging shares by making it unnecessary for a purchaser of shares to examine in great detail the liabilities of the corporation and the assets of other shareholders; these liabilities can adversely affect a purchaser only up to the extent of the price per share.

Extract 8.3 Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property* (New York: Harcourt, Brace & World, 1932), pp. 299–301

[In this classic (and now hotly disputed) analysis of property holding by limited liability companies first published in 1932, Adolf A. Berle and Gardiner C. Means estimated that approximately 300,000 companies then registered in the United States controlled at least 78 per cent of business wealth in the country. This was not spread evenly between all companies: the 200 largest companies were estimated to control between 45 per cent and 53 per cent of all corporate wealth, between 35 per cent and 45 per cent of all business wealth, and between 15 per cent and 25 per cent of national wealth.]

The socially beneficent results to be derived from the protection of property are supposed to arise, not from the wealth itself, but from the efforts to acquire wealth. A long line of economists have developed what might be called the traditional logic of profits. They have held that, in striving to acquire wealth, that is, in seeking profits, the individual would, perhaps unconsciously, satisfy the wants of others. By carrying on enterprise he would employ his energy and wealth in such a way as to obtain more wealth. In this effort, he would tend to make for profit those things which were in most demand. Competition among countless producers could be relied upon in general to maintain profits within reasonable limits while temporarily excessive profits in any one line of production would induce an increase of activity in that line with a consequent drop of profits to more reasonable levels. At the same time, it was supposed that the business man's effort to increase his profits would, in general, result in more economical use of the factors of production, each enterprise having to compete with others for the available economic resources. Therefore, it has been argued that, by protecting each man in the possession of his wealth and in the possession of any profits he could make from its use, society would encourage enterprise and thereby facilitate the production and distribution of goods desired by the community at reasonable prices with economic use of labor, capital, and business enterprise. By protecting property rights in the instruments of production, the acquisitive interests of man could thus be more effectively harnessed to the benefit of the community.

It must be seen that, under the condition just described, profits act as a return for the performance of two separate functions. First, they act as an inducement to the individual to risk his wealth in enterprise, and, second, they act as a spur, driving him to exercise his utmost skill in making his enterprise profitable. In the case of a private enterprise the distinction between these two functions does not assume importance. The owner of a

private business receives any profits made and performs the functions not only of risk-taking but of ultimate management as well. It may be that in the past when industry was in the main carried on by a multitude of small private enterprises the community, through protecting property, has induced a large volume of risk-taking and a vigorous conduct of industry in exchange for the profits derived therefrom.

In the modern corporation, with its separation of ownership and control, these two functions of risk and control are, in the main, performed by two different groups of people. Where such a separation is complete one group of individuals, the security holders [here meaning the shareholders and those who provide loan finance for the company] . . . perform the function of risk-takers and suppliers of capital, while a separate group exercises control and ultimate management. In such a case, if profits are to be received only by the security holders, as the traditional logic of property would require, how can they perform both of their traditional economic roles? Are no profits to go to those who exercise control and in whose hands the efficient operation of enterprise ultimately rests?

It is clear that the function of capital supplying and risk-taking must be performed and that the security holder must be compensated if an enterprise is to raise new capital and expand its activity just as the workers must be paid enough to insure the continued supplying of labor and the taking of the risks involved in that labor and in the life based on it. But what if profits can be made more than sufficient to keep the security holders satisfied, more than sufficient to induce new capital to come into the enterprise? Where is the social advantage in setting aside for the security holder, profits in an amount greater than is sufficient to insure the continued supplying of capital and taking of risk? The prospect of additional profits cannot act as a spur on the security holder to make him *operate* the enterprise with more vigour in a way to serve the wants of the community, since he is no longer in control. Such extra profits if given to the security holders would seem to perform no useful economic function.

Furthermore, if all profits are earmarked for the security holder, where is the inducement for those in control to manage the enterprise efficiently? When none of the profits are to be received by them, why should they exert themselves beyond the amount necessary to maintain a reasonably satisfied group of stockholders? *If* the profit motive is the powerful incentive to action which it is supposed to be, and *if* the community is best served when each enterprise is operated with the aim of making the maximum profit, would there not be great social advantage in encouraging the control to seize for themselves any profits over and above the amount necessary as a satisfactory return to capital?

Extract 8.4 Gregory S. Alexander, *Commodity and Propriety: Competing Visions of Property in American Legal Thought 1776–1970* (Chicago: University of Chicago Press, 1997), pp. 342–50

BERLE AND MEANS AND THE PROBLEM OF CORPORATE PROPERTY

By the time of the Great Crash of 1929, it was abundantly clear to anyone who cared to look that the shift to the large corporation as the dominant mode of doing business

and with it, corporate equity and debt instruments as the dominant form of property, was now completed and irreversible. Attacks on the modern industrial corporation by critics like Edward Bellamy and Thorstein Veblen had utterly failed to slow the rapid growth of the business corporation or to weaken its enormous economic power.

The phenomenal growth of corporate power, together with the stock market's crash and the ensuing economic depression, engendered in the 1930s an intellectual milieu of skepticism about the validity of the classical theory of economic behavior. That theory posited that the natural forces of market competition by themselves would force firms to supply the best products that consumers wanted at the lowest possible prices. Those that did not would decline and eventually shut down through a process of natural economic selection. The upshot of this theory was that, since market equilibrium was self-maintaining, government intervention in the workings of the market was unjustified.

A central assumption of this theory was that the same person or group of persons would both supply and manage capital for a business venture. Since they would reap the gains or suffer the losses of their own decisions, self-interest would lead these persons to operate the firm as efficiently as they could. The emergence of the modern industrial corporation undermined that assumption and with it, at least in the view of critics, the coherence of the classical theory itself. Among all of the critiques of that theory and of corporate capitalism generally that appeared between 1890 and 1930, no work was more influential than A. A. Berle and G. C. Means's famous book, *The Modern Corporation and Private Property*.

Berle initiated the project under a grant to Columbia University from the Social Science Research Council and was the book's principal author. Means, who was a member of Columbia's economics faculty, contributed to the study primarily by collecting a substantial body of statistical data documenting the concentration of corporate ownership and the diffused distribution of stockholdings. Berle had joined the Columbia law faculty shortly after a split on that faculty had led several prominent Realists to leave. Despite the departure of important figures like William O. Douglas, Herman Oliphant, and Underhill Moore, however, Legal Realism still exerted considerable influence at Columbia, largely through the presence of Karl Llewellyn and Edwin Patterson. Institutional economics, championed by Robert L. Hale, also remained an important intellectual force at Columbia during the time of the Berle study. The book reflected the influence of both strands of thought.

Berle and Means developed two related claims: first, the central characteristic of the modern corporation is the separation of the control of property from its beneficial ownership; second, corporate managers and beneficial owners (i.e. shareholders) do not share the same incentives, undermining the key assumption of the classical model of the market. Berle and Means connected the two claims together in this central passage:

> It has been assumed that, if the individual is protected in the right both to use his property as he sees fit and to receive the full fruits of its use, his desire for personal

> gain, for profits, can be relied on as an effective incentive to his efficient use of any industrial property he may possess.
>
> In the quasi-public corporation, such an assumption no longer holds. [I]t is no longer the individual himself who uses his wealth. Those in control of that wealth, and therefore in a position to secure industrial efficiency and produce profits, are no longer, as owners, entitled to the bulk of such profits. Those who control the destinies of the typical modern corporation own so insignificant a fraction of the company's stock that the returns from running the corporation profitably accrue to them in only a very minor degree. The stockholders, on the other hand, to whom the profits of the corporation go, cannot be motivated by those profits to a more efficient use of the property, since they have surrendered all disposition of it to those in control of the enterprise.

The implication of these claims for the economic function of property was, they thought, profound. At least in the industrial context, the role of property had fundamentally changed. Property no longer performed the economic function that classical economic theory traditionally ascribed to it. 'Must we not', they asked rhetorically, 'recognize that we are no longer dealing with property in the old sense? Does the traditional logic of property still apply? Because an owner who also exercises control over his wealth is protected in the full receipt of the advantages derived from it, must it necessarily follow that an owner who has surrendered control of his wealth should likewise be protected to the full?'

For Berle and Means, the upshot of these changes in the nature of the business corporation and its concomitant effect on the function of property in the business sector was clear: 'The explosion of the atom of property destroys the basis of the old assumption that the quest for profits will spur the owner of industrial property to its effective [i.e. efficient] use.' Large corporations could not be counted on to serve either the interests of shareholders, as the corporation's owners, or of the public generally. Since self-interest alone was inadequate, the only alternative mechanism for assuring that corporations were governed in the public interest was government regulation. Government had 'to strip itself of the illusion that it might recreate the classical society of small competitors and proceed with the structural reforms needed to stabilize the economy'.

What made *The Modern Corporation and Private Property* so influential was not originality: virtually nothing in the book, certainly none of its major arguments, was completely new. Well-known books by Harvard economists Thomas Nixon Carver and William Z. Ripley had earlier argued that shareholders of large corporations had little, if any, meaningful power over corporate policy. Before them, Thorstein Veblen had developed a similar theory of the evolution of corporate structure. Still earlier, the great English economist Alfred Marshall had pointed out in 1890 that large corporations were 'hampered by . . . conflicts of interest between shareholders and . . . the directors'.

Three factors explain the book's phenomenal success. First, unlike Veblen, Carver and other critics of the corporation, Berle and Means (primarily Means) backed up their criticisms with a substantial body of statistical data. These data were intended to

prove two points: that corporate wealth was concentrated in a few corporations and that ownership of corporate stock was broadly dispersed. The data effectively created the impression that a relatively small group of managers now dominated the nation's economy.

The second factor was the book's timing. The date of its first publication (1933) was ideal. After the stock market crash, the general public was quite receptive to a critical treatment of corporate power. As George Stigler and Claire Friedland have pointed out, '[t]he 1930s was a period of accelerating movement away from a competitive, unregulated market. Reasons for distrusting such a system . . . were in demand for the new rhetoric of public policy, and Berle and Means nicely met that need.' Policy-oriented lawyers and social scientists were no less ready than John Q. American to hear an analysis of corporate governance that emphasized the need for external control. The crash had seemed to validate Carver's and Ripley's earlier predictions of the disastrous consequences of leaving the modern corporation unregulated. The time could not have been more ripe for a study of the modern corporation that focused on its enormous power.

The third factor was the book's functional and institutionalist approach to the study of corporations. Between 1920 and 1930 a debate raged among legal scholars over the 'true' nature of the corporation. The law reviews were filled with articles, most of which were aridly conceptualist, debating whether the corporation is a 'real entity' or merely an aggregation of contractual relationships. By 1930, this debate had run out of intellectual steam. The philosopher John Dewey, who had considerable contact with both the law school and the economics faculties at Columbia and whose work both influenced and was influenced by them, wrote in 1926 that legal writers and courts should disconnect specific issues concerning corporations from disputes over the appropriate conceptual theory of the corporation: how law and society treat the corporation, and what powers the corporation was given, depended on political and economic choices, not on formal analysis.

Heeding Dewey's advice, Berle and Means simply ignored the whole 'real entity' debate. Instead, they focused on how the modern business corporation actually functioned in American society. The functional approach was perfectly suited to Berle and Means's intended audience, for the book was not directed at professional economists, or at least not the academic economic establishment. Its real target was lawyers, especially those academic lawyers who were most interested in and involved with the making of public policy – Legal Realists and their economic allies. Berle and Means's methodology effectively synthesized the institutional perspective of institutional economics and the functionalist outlook of the Legal Realists. Substantively, their analysis echoed the two dominant themes of Progressive and Realist legal-economic writers that the market was a realm of power and that economic institutions were not wholly private in character. In particular, Berle and Means's argument that large corporations were not really private institutions but were actually 'quasi-public' strongly reiterated and bolstered earlier arguments by Hohfeld, Hale, Ely, Commons, and others that there was no categorical distinction between the public and private in market transactions. While the economic profession was not especially

interested in this line of criticism, the academic legal profession, especially its elite stratum, certainly was.

PUBLICLY CONTROLLING THE PRIVATE CORPORATION

Berle and Means's most significant contribution was to sketch a theory that would provide an alternative to the affectation doctrine of *Munn* v. *Illinois* as the theoretical foundation for government regulation of corporate activities. As we have already seen, that doctrine provided that there was no constitutional obstacle to legislative regulation of, for example, the rates that businesses charged their customers when the corporation was of the type that was 'affected with a public interest'. In effect, the affectation doctrine denied that such corporations were solely private. While the US Supreme Court did not formally abandon that doctrine until the 1934 decision in *Nebbia* v. *New York*, it lost virtually all intellectual credibility among lawyers well before then. It was, as the Yale Legal Realist Walton Hamilton put it, the product of the view of a generation for whom the then-new fourteenth amendment was part of 'the old constitution'. To a different generation, it sounded (if one was inclined to value liberty of contract above all) suspiciously hostile to property rights or (if one had taken the Realist turn) meaningless, since all businesses were in some sense affected with a public interest. By 1930, its demise as a justification for legal control of corporate activities in general to insure that corporations act for the common welfare was a foregone conclusion.

Berle and Means attempted to fill the gap by advancing a novel theory. They argued that the 'traditional logic of property' did not apply to the modern large corporation. Corporate power should not be exercised for the exclusive benefit of the shareholders but for the benefit of society as a whole. Shareholders are, they argued, passive property owners who have 'released the community from the obligation to protect them to the full extent implied in the doctrine of strict property rights'. This leaves the community in a position to demand that the relationship between corporate property and the community be reconfigured in a way that recognizes that in the context of the modern industrial corporation the public/private distinction had lost much of its credibility:

> Neither the claims of ownership nor those of control can stand against the paramount interests of the community ... Rigid enforcement of property rights as a temporary protection against plundering by control would not stand in the way of modification of these rights in the interest of other groups. When a convincing system of community obligations is worked out and is generally accepted, in that moment the passive property right of today must yield before the larger interests of society ... It is conceivable – indeed it seems almost essential if the corporate system is to survive – that the 'control' of the great corporations should develop into a purely neutral technocracy, balancing a variety of claims by various groups in the community and assigning to each a portion of the income stream on the basis of public policy rather than private cupidity.

The precise content of the obligation that the corporation owes to the community remained obscure. Berle and Means never explained what the specific features of that obligation were or which constituencies are included in the notion of the 'community'. Rather, they vaguely called for something resembling what late twentieth-century corporate lawyers call 'corporate social responsibility'. But it is not entirely clear just how the Berle and Means analysis relates to the modern discourse of corporate social responsibility.

The phrase 'corporate social responsibility' today may mean either of two different ideas. The first is that the officers of large, publicly held corporations should focus exclusively on the shareholders' dominant preference, which is presumed to be profit-maximization, rather than serving their own personal interests. The second meaning grows out of a quite different concern. It advocates what is sometimes called 'corporate voluntarism', that is, corporate actions that sacrifice profit-maximization to pursue other social objectives.

These two ideas have inconsistent implications for legal control over corporate managers. The first idea requires tighter legal control over corporate officers and directors. Corporate voluntarism, on the other hand, requires relaxing legal controls over managers, giving them greater discretion so that they can fulfill their responsibilities to the community.

These two meanings were the subject of a famous debate between Berle and the noted Harvard professor of corporate law, E. Merrick Dodd. Dodd supported the idea of corporate voluntarism, and he was unconcerned that corporate managers would exercise greater discretion in their own interests rather than the interests of social groups in addition to shareholders. He based his confidence on the theory that

> [p]ower over the lives of others tends to create on the part of those most worthy to exercise it a sense of responsibility. The managers, who along with the subordinate employees are part of the group which is contributing to the success of the enterprise by day-to-day efforts, may easily come to feel as strong a community of interest with their fellow workers as with a group of investors whose only connection with the enterprise is that they or their predecessors in interest invested money in it.

Berle regarded this view as wildly naive. He simply did not think that corporate managers could be trusted to act in the interest of anyone other than themselves if they were given discretion to do so. Because of the separation of control from ownership, private property no longer performed, in the industrial setting, its disciplining role. Therefore, management powers had to be subjected to some form of legal control. One possible form is the requirement that managers act exclusively in the interest of shareholders. That approach, which Berle analogized to the controls that equity places on trustees, adopted the profit-maximization version of corporate responsibility.

Berle considered strict, trustee-like controls over corporate managers to be clearly preferable to open-ended managerial discretion, if those two were the only available options. His reluctance to abandon profit-maximization as the sole objective of corporate officers and directors was rooted in social welfare considerations.

Doubtless reflecting anxiety about the economic insecurity that millions of Americans were then facing during the Great Depression, he wrote, 'When [corporate property] and the income stream upon which [corporate stockholders] rely are irresponsibly dealt with, a large portion of the group merely devolves upon the community; and there is presented a staggering bill for relief, old age pensions, sickness-aid, and the like.' Removing from shareholders their economic security so that corporate property could be used to serve the interests of other groups was simply robbing Peter to pay Paul unless the government simultaneously adopts 'a system ... by which responsibility for control of national wealth and income is so apportioned and enforced that the community as a whole, or at least the great bulk of it, is properly taken care of'.

Berle presented his obligation-to-the-community theory as a third way, an alternative to the 'managerial discretion' theory and the 'strict property rights of shareholders' theory. He recognized that this theory had to be clearly developed, but he warned that 'you cannot abandon emphasis on "the view that business corporations exist for the sole purpose of making profits for their stockholders" until such time as you are prepared to offer a clear and reasonably enforceable scheme of responsibilities to someone else'. Once the shareholders' interests were adequately taken care of, though, the community had a legitimate claim to have other groups' interests protected as well. These included 'fair wages, security to employees, reasonable service to their public, and stabilization of business'. A program along those lines might well shift some corporate profits from shareholders to employees and other groups to whom corporations conventionally do not owe fiduciary duties, but so long as the shareholders' basic welfare needs were served, they had no legitimate basis for demanding that their profits be maximized. The corporation was, after all, a quasi-public institution, and its legal obligations had to be defined consistently with its character.

Subsequent to writing *The Modern Corporation and Private Property*, Berle's views became more obscure still. In 1954, he conceded that his dispute with Dodd 'has been settled (at least for the time being)' squarely in favor of Professor Dodd's contention. He now considered corporate management to be free to practice social responsibility. Still later, however, he asserted that his concession was only that things had changed in fact, not that they had changed for the better. 'Things being as they are', he wrote, 'I am unabashed in endeavoring to seek the best use of a social and legal situation whose existence can neither be denied nor changed.'

Berle never got around to describing an alternative 'scheme of responsibilities' for corporations. Oddly enough, he did not support proposals to reconstitute boards of directors to include representatives of employees or consumers or calls formally to redefine the goals of management.

8.4.2. Managerial property holding

There are a number of other property holding mechanisms which involve the separation of title and benefit, in the sense that the property holder is not only precluded from taking a personal benefit from the property but is also put under positive duties to administer it for the benefit of others. The most well known of these mechanisms is the trust, evolved by equity precisely for this purpose, but

there are other analogous situations where the law cannot or will not allow a property holder to continue to enjoy the benefit of the property. The most obvious circumstances in which such situations arise is where a property holder dies or is made bankrupt. However, although these situations are analogous to each other and to the trust, there are important differences between them. There has been a tendency to overlook these differences and assume that all such managerial property holding mechanisms must conform analytically to the trust model – in particular, to assume that, since the property holder is no longer entitled to benefit from the property, there must be someone else who is entitled to the benefit in precisely the same way as a beneficiary under a trust is entitled to benefit. However, as we see below, the courts have rejected such attempts to force all types of managerial property holding into the trusts straitjacket, and now accept that different allocations of management, control and benefit are appropriate in these very different circumstances.

8.4.2.1. Trust

In a trust, title to property is held by one or more trustees who are required to use it not for their own benefit but for the specific purpose of the trust. This might be to carry out a specified, usually charitable, purpose, or it might be to administer the property for the benefit of specified people – the beneficiaries. For example, I might transfer £10,000 to you on terms that you will hold it on trust for my two children until they have reached the age of eighteen. This would usually (subject to the precise terms I impose) mean that you will have to invest the £10,000 so that it produces an income, and then you will have to make sure that that income is spent on the children while they are under eighteen, and then hand over half the capital representing the original £10,000 to each child on her eighteenth birthday.

This is not the only way in which a trust can come into existence. Instead of transferring the £10,000 to you to hold on trust for my children, I might have made myself trustee of it, by declaring that I hold it on trust for them. These are both examples of an express creation of a trust. But a trust might also be imposed on me by the law (historically, by equity) whether I intend it to happen or not, either via a resulting trust in the circumstances Lord Browne-Wilkinson describes in the extract from *Westdeutsche Landesbank* v. *Islington London Borough Council* given above, or via a constructive trust. A constructive trust is imposed in circumstances where the court regards it as unconscionable for the legal title holder to use the property for his own benefit. So, for example, if you and I buy a house together in my name, but on the common understanding that it is to be ours jointly, and on the strength of this you pay half the mortgage payments, equity will impose a constructive trust on me so that I am required to hold the title to the house on trust for us jointly (*Lloyds Bank plc* v. *Rosset* [1990] 1 AC 107).

Here we are not concerned with how a trust comes into existence. What we are interested in is how ownership is fragmented once property is subjected to a trust, however that came about. So, to go back to the first example, if I give you £10,000

to hold on trust for my children, what is the position of each of us – you the trustee, me the creator of the trust or settlor, and the children as beneficiaries?

The trustee

It is clear that you as trustee hold the title to the £10,000 and to the investments you buy with the money. In this sense, you can be said to be the owner, but this ownership is of no value to you because you are not allowed to take any benefit from these assets for yourself. In fact, one can go further and say that this ownership has a negative value in your hands. I would not expect you to take it on except as a favour to me, or for payment, because it will involve you taking on positive duties to take care of the assets and to ensure they produce a good return for my children and are used exclusively for their benefit. You can therefore be said to have title to the £10,000 and any investments from time to time representing it, and the right, power and duty to manage them, but no benefit from them.

The settlor

It is equally well established, although perhaps not so obvious, that I as the person who created the trust, the settlor, cease to have any role once the trust is set up. I have transferred my title to you, and unless I specifically reserved a right to benefit for myself in some way, or reserved rights or powers to direct you what to do (both unlikely in practice) I no longer have any say in what happens to anything, not even a right to object if you commit any breach of the duties I have imposed on you. The fact that trust law has evolved in such a way that the settlor is left with no function is less surprising when you consider how often trusts have to operate without a settlor: many expressly created trusts are made by will (so the settlor has died by the time the trust comes into operation) or because the settlor knows she will be unable to manage the assets personally and those not expressly created but imposed by law never had a settlor.

The beneficiaries

The position of the beneficiaries is more complex. In general terms, they clearly have the benefit of the trust property, in that you as trustee are under a duty to manage it on their behalf, but how is that duty enforced, and can the beneficiaries be said to have any interest in the property held on trust for them, as opposed to in any payments you might eventually make to them out of the trust?

The answer to the first question is that it is the courts who invented the trust in the first place, and they retain a supervisory jurisdiction over them. In practice, this means that they enforce the duties of the trustees, on application made to them by the beneficiaries.

A crucial element in the interest of a beneficiary is therefore the right to apply to the court for redress if the trustees fail in carrying out any of their duties. This is a chose in action, and is in itself a valuable property interest. Is it, however, possible to go further and say that the beneficiary has a property interest in the trust

property itself? Could one say, for example (and ignoring for the moment the question of whether minors can hold property interests), that my children have any interest in the £10,000 you hold on trust for them, or in any investments you buy with it to hold on their behalf?

One immediate apparent difficulty can be cleared out of the way to start with, and this is the precise identity of the assets in which they might be said to have an interest. There are two reasons why we might hesitate to say that they have an interest in the original £10,000, or in any of the specific investments you buy with it. The first is that expenses will be incurred in the administration of the trust, and taxes will be payable in respect of the assets you are holding on trust. You as trustee are not of course expected to pay these out of your own pocket: you will pay them out of the trust assets. The beneficiaries can therefore never assume that any particular asset will be given to them or even used for their direct benefit: you might instead decide to sell it to raise the money to pay taxes and expenses. The second is that, because you as trustee have the duty to invest the money, you must be free to buy and sell specific assets at your discretion without asking or even telling the children, and you must also have the power to sell any given asset freed from any obligation that it should be used for the benefit of the children. For these reasons, it is difficult to see how the children can be said to have any interest in any particular assets, except in the very general sense that they have the right to insist that they are used only for purposes authorised by the trust. This was the conclusion reached by the minority in the House of Lords in the classic case, *Baker* v. *Archer-Shee* [1927] AC 844. The majority view – that the beneficiary did have an interest in each investment – is understandable in the taxation context they were considering, but would be an inaccurate analysis of the beneficiary's position if taken outside that context.

However, there is a more convincing analysis not canvassed in the *Archer-Shee* case. If viewed more abstractly, it can be seen that what you as trustee are holding is a *fund*, a fluctuating body of assets from time to time representing the original £10,000, out of which you as trustee deduct the proper expenses of the fund, and the balance of which must ultimately go to the children and to no one else. Viewed in this light, it is perfectly intelligible to say that, while the children have no property interest in any specific asset vested in you as trustee, they do have an interest in the abstract fund represented by the assets you hold from time to time on their behalf. This is the analysis implicitly accepted by both the Court of Appeal and the House of Lords in another taxation case, *Gartside* v. *Inland Revenue Commissioners* [1968] AC 553, although they differed over the question of when a beneficiary can be said to have an interest, in the sense of an entitlement to benefit, as opposed to an expectancy of benefiting. For further analysis of the idea of property in a fund see Nolan, 'Property in a Fund'.

8.4.2.2. Administration of property on death

Since property interests are, by definition, not personal to the interest holder, it follows that, when a person dies holding a property interest, that property interest

continues to exist. This does not of course apply to interests whose duration is fixed by reference to the holder's lifetime. Take, for example, the case of an option to purchase an interest in land, which is itself an interest in land for the reasons given in section 12.3.4 below. If I was to grant you an option to purchase the freehold interest in my house at any time during your lifetime for £100,000, the option will automatically expire when you die, whereas if we had agreed that the option was exercisable at any time over the next fifty years, the option will continue for the full fifty-year period despite your death before then.

So what actually happens to that option if you die before the fifty-year period is up? Ultimately, all your property (the option included) will go to whichever of your relatives becomes qualified to take under sections 45 and 46 of the Administration of Estates Act 1925 as amended, unless you left a will directing that it should go elsewhere. However, this cannot happen instantaneously when you die. Someone has to carry out the bureaucratic task of sorting out what property you had, paying all your debts out of it (which may involve selling some or all of it), and identifying who is now entitled to what out of what is left. You, the testator, can choose who is to carry out that task by appointing that person as executor in your will, and, if you do that, then the title to all your property will automatically vest in that person when you die (sections 1 and 3 of the Administration of Estates Act 1925). If you do not appoint an executor, anyone claiming an interest in your property can apply to the court to be appointed as an administrator to carry out the same functions. This will necessarily take some time, and so pending the appointment of an administrator the title to all your property vests in a public official, the Public Trustee, who has no function other than to hold the nominal title until it can be passed on to an administrator (section 9 of the 1925 Act, as substituted by section 14 of the Law of Property (Miscellaneous Provisions) Act 1994).

Your executor or administrator (collectively called 'personal representatives') will not only have title to your property but will also have extensive powers to deal with it while carrying out the administration of your affairs. The Administration of Estates Act 1925 as amended gives personal representatives powers equivalent to those held by trustees over trust property and clearly, since their function is to get your property together, pay off your debts and their expenses and then pass the balance on to your beneficiaries, they can be said to be under a duty to exercise these powers over your property for the benefit of these prospective beneficiaries. They are certainly not entitled to exercise them for their own benefit. Does this mean that the people who will ultimately take the net assets left after administration of your estate have a beneficial interest in your property during the course of the administration, just as a beneficiary under a trust would have? This question has caused some confusion in the past. It had been argued that, when you die holding property beneficially, the beneficial interest must be somewhere pending its ultimate transfer to your beneficiaries. It cannot be in abeyance. It cannot be held by your personal representatives because, like trustees, although they are

nominally the owners they are not allowed to use the property for their own benefit. Therefore, the argument goes, they must be holding it for the benefit of the prospective beneficiaries, and therefore those beneficiaries must be taken to have the beneficial interest in your assets from the moment you die. This, however, is a very mechanistic view of property interests. Just because it is possible to split the nominal title and the beneficial interest in property between two people through the mechanism of a trust, it does not necessarily follow that, whenever someone holds only the nominal title to property (i.e. they hold property that they are not allowed to use for their own benefit), there must be someone else somewhere who holds the beneficial interest. The title holder may be holding the property for some abstract purpose (consider, for example, the trustees of a charitable trust) or with the duty to administer it for the benefit of some as yet unascertained persons. Provided there is in place some mechanism for ensuring that the title holders do indeed use the property for the requisite purposes and not for their own benefit, there is no practical reason why anyone else should have to have property rights either in the specific assets themselves or (as in a trust) in the fund comprising those assets and their net proceeds. In *Commissioner of Stamp Duties (Queensland)* v. *Livingston* [1965] AC 694 (extracted at www.cambridge.org/propertylaw/), it was finally established that this is the correct analysis of how the property of a deceased person is held pending its transfer by the personal representatives to those who are ultimately identified as the appropriate beneficiaries. One might say that the beneficial interest is in abeyance from the date of death until the net estate is distributed, or, perhaps more accurately, one might say that there simply is no beneficial property interest during that period. Ownership has been fragmented in such a way that management has been allocated to one person and control to another (or others: see below) but no one has a proprietary right to benefit.

8.4.2.3. Bankruptcy and liquidation

A similar situation arises when a property holder becomes insolvent, but there are some significant differences. In the case of company liquidations (but not individual bankruptcy) the split between title, management and control is more complex. Given the already existing fragmentation of control, management and benefit existing in a solvent company, this is unsurprising. What happens on liquidation is that title to the company's assets remains in the company, but the directors lose all their management powers. From that point onwards, the company can act only through the liquidator, who takes on all the directors' powers and also enjoys additional statutory powers to enable him to get in all the company's assets, ascertain all its liabilities and then distribute the assets among the creditors. Once this process has been completed, the company is wound up and formally ceases to exist. Although this may look superficially similar to the task carried out by the administrator of the assets of someone who has died, the important difference is that the liquidator is an officer of the court with powers and duties

to scrutinise both the behaviour of the company's directors in the period leading up to insolvency, and transactions entered into by the company during that period.

In the bankruptcy of an individual, the trustee in bankruptcy performs very similar functions, but also takes on title to all the bankrupt's assets. Title to the property of a bankrupt automatically transfers from the bankrupt to her trustee in bankruptcy as soon as the bankruptcy order is made, and the trustee then has statutory powers and duties essentially the same to those enjoyed by a liquidator.

An additional complicating factor in both liquidation and bankruptcy is that there is a significant process to be gone through before it can be established who will receive what payments from the estate. Anyone who thinks they may be entitled must first put in a proof of their claim, and it is for the liquidator or trustee in bankruptcy to determine the admissibility and value of each claim. Contingent claims, claims for future debts and claims for as yet unascertained amounts are all allowable (for example, a claim for damages for personal injury where neither liability nor quantum has yet been settled) and the liquidator or trustee in bankruptcy must put a value on each of these (subject to a right of appeal to the court). At the outset, the question of precisely who is a prospective beneficiary, and precisely what their interest might be, is therefore much less clear than it is in the case of an estate of a deceased person.

Given these factors, it is not surprising that the courts have had no difficulty in concluding that neither the creditors nor anyone else has a beneficial interest in the insolvent's assets pending completion of the liquidation or bankruptcy, as we see from *Ayerst* v. *C&K (Construction) Ltd* [1976] AC 167, extracted at www.cambridge.org/propertylaw/.

Notes and Questions 8.2

1 Read *Commissioner of Stamp Duties* v. *Livingston* [1965] AC 694, either in full or as extracted at www.cambridge.org/propertylaw/, and consider the following:

   (1) The court acknowledged that someone in Mrs Coulsdon's position has a 'transmissible interest' in the unadministered estate, in the sense that, if she dies, the right to receive the benefit under the testator's will will pass to whoever becomes entitled to *her* property on *her* death. Similarly, if instead of dying she had become bankrupt when the testator's estate was still in the course of administration, her right to receive the benefit under the testator's will would have passed automatically to her trustee in bankruptcy. According to Viscount Radcliffe, what is the nature of this transmissible right that she holds at this point? Is it a property right? If yes, why was it not a 'beneficial interest in real property in Queensland or . . . beneficial personal property [interest] locally situate in Queensland'?

   (2) According to Viscount Radcliffe, why is an unadministered estate incapable of forming a trust fund? Do you agree? See section 8.4.2.1 (under the heading 'The beneficiaries') above on the idea of property in a fund.

(3) If by his will Mr Livingston had left his widow a specific item he owned – perhaps the house where they lived, or his wedding ring – should Mrs Coulsdon be taken to have any property interest in that item pending completion of the administration by the executors?

(4) Compare the position of executors with that of (a) company directors (b) trustees and (c) liquidators. In each case, who has title to the assets? Who the right/power to manage them? For whose benefit must they exercise those rights/powers? What is the mechanism for ensuring (i) that they do not exercise them for their own benefit and (ii) that they do exercise them to realise the maximum benefit for those intended to benefit?

2 Read *Ayerst* v. *C&K (Construction) Ltd* [1976] AC 167, either in full or as extracted at www.cambridge.org/propertylaw/. In argument, counsel for the taxpayer argued that the mere fact that restrictions are imposed by law or contract on an owner's right to use his property does not deprive him of the beneficial ownership of it:

> In the case of a tree preservation order one is deprived of the right to cut it down but not of the beneficial ownership. A company in liquidation, though it must pay its creditors, holds its property for its own benefit. Its assets remain its assets though they must be dealt with in a particular way [by the liquidator, acting as a 'superior director' of the company] . . . The liquidator has fiduciary duties imposed by statute but is not really a trustee. The beneficial ownership is not in the creditors . . . A company only ceases to be the beneficial owner of its assets if the beneficial ownership passes to someone else. A man remains the beneficial owner of his property, however much the law may restrain the use of it.

Do you agree that an owner of a tree subject to a tree preservation order remains beneficial owner of it? Do you agree with the final sentence? Is there a valid distinction to be drawn between a person who is prohibited from using her property, and a person who is required to use it wholly for the benefit of someone else?

8.5. Group ownership

Only legal entities can hold private property interests. Human beings, corporations and partnerships come within the category of legal entity, but many other socially recognised groupings (for example, married couples, families, parent and subsidiary companies, and unincorporated associations) do not, even though there may be a legally recognised relationship between the members of the group. However, it is possible for two or more legal entities to hold the same private property interest simultaneously, through private co-ownership.

Private co-ownership must be distinguished from public ownership and communal ownership. We considered the differences between private ownership, public ownership and communal ownership in Chapter 2. As we saw there, in

the case of communal property rights, as a member of the community you cannot be excluded from use and benefit by any other member of the community but you do not have any separate or separable property right that can be sold or bequeathed to anyone else: the only way in which any person can become or cease to be entitled to use and benefit is by joining or leaving the community. Private co-ownership resembles communal ownership in that no co-owner can be excluded from use and benefit by any other co-owner, and no co-owner has a separate interest during the co-ownership. However, it differs from communal ownership in that, in general (subject to exceptions explained below), in private co-ownership each co-owner has a *separable share* in the co-owned property, and, once it has been notionally separated off, that share can be sold or bequeathed to someone else, who thereby becomes a new member of the co-ownership group. By the same token, every private co-owner continues to have a proprietary entitlement unless and until it is positively transferred to someone else (or, in the case of a joint holder who dies before severing his interest, until he dies: see below).

It will be apparent from the above that, in this jurisdiction we do not recognise private co-ownership where the right to participate is defined by reference to status. In other words, the co-owners must comprise a fixed (as opposed to a fluctuating) group of ascertained legal entities. In fact, the *only* types of co-ownership that we now recognise are ownership in common and joint ownership (usually called tenancy in common and joint tenancy where the co-owned interest is an interest in land).

In ownership in common, each co-ownership has a defined but not yet separated off (and not necessarily equal) share in the co-owned interest. For example, you and I might own a car in common, with me having a one-fifth and you having a four-fifths share. We are each equally entitled to the use and benefit of the car, in the sense that neither of us can exclude the other from any part of it (although see below as to what happens if we fail to agree on a *modus vivendi*). Neither of us can sell or otherwise deal with the car except with the co-operation of the other. If, however, the car is hired out or sold, I will be entitled to a one-fifth share in the hire fee or sale price and you will take the other four-fifths. Although I cannot sell the car itself without your co-operation, I can at any time sell or give my one-fifth *share* in it to anyone else (in which case of course I will take the whole of any sale proceeds of my share) and you can do the same with your four-fifths. And, if either of us dies, our respective share will go to our personal representatives, to be passed on to whoever becomes entitled to inherit our property.

Joint ownership differs from ownership in common in one crucial respect. Instead of each co-owner having a defined but not yet separated off share, as in ownership in common, each joint owner is fully entitled to the whole of the co-owned interest, subject only to the exactly similar entitlement of each of the other joint owners. Furthermore, no individual joint owner can sell or give away his joint ownership interest. However, what he can *always* do (subject to the exceptions below) is to convert his joint ownership interest into an interest in

common, which he can then either keep as a separable but as yet unseparated share in the co-ownership, or sell or give away, as he chooses. He can do this unilaterally at any time provided (if he is an individual) it is done before he dies. If he dies without having converted his joint interest into an interest in common (and an attempt to do so by will is too late) then on his death his interest expires, and the other joint interests are correspondingly enlarged. If during his lifetime he attempts to deal separately with his own interest under the joint ownership (for example, by purporting to sell or mortgage it) this will *automatically of itself* sever his interest from the joint ownership – i.e. convert his joint interest into an interest in common – and the purported sale or mortgage or whatever will take effect over what is now his interest in common.

In practical terms, therefore, joint owners can separate off their interests as easily as can tenants in common, except in the cases considered below where the joint tenancy is made unseverable by statute. This leaves only two differences between joint ownership and ownership in common which are of any importance in practice. First, in any joint ownership, the entitlements of each joint owner are necessarily equal, so if there are five joint owners and one severs (i.e. converts her joint interest into an interest in common) she will now hold a one-fifth share and the other four will jointly hold a four-fifths share (her action has no effect on the relationship between the other four – they remain joint owners of their share). Secondly, as already explained, when a joint owner dies, her interest expires and the entitlement of the survivors is correspondingly enlarged, whereas, when an owner in common dies, he dies owning a share which is passed on to whoever inherits his property and the entitlements of the other owners in common are not affected in any way. In technical terms, joint owners have a right of survivorship (as each dies, the survivors' entitlements enlarge, until the last survivor takes everything) whereas owners in common do not.

In all other respects, however, joint ownership and ownership in common are identical in effect. Like owners in common, joint owners can only dispose of or deal with the jointly owned asset by acting in unison, and any proceeds of any dealing or disposition are divisible rateably between them (in the case of joint ownership, necessarily in equal shares). Meanwhile, however, just as in the case of ownership in common, no joint owner can be excluded from the use and benefit of the jointly owned asset or any part of it by any other joint owner.

It will be apparent from the above that, in practice, private co-ownership, whether by ownership in common or by joint ownership, would often be unworkable without mechanisms for resolving disputes and enforcing co-operation between the owners. We consider these mechanisms in Chapter 16, but one of them, applicable only to co-owned interests in land, must be briefly mentioned here. This is the automatic imposition of a trust on all co-owned interests in land. Specifically, when co-owners acquire an interest in land, it automatically vests in them (or in whoever they nominate, or, if they fail to nominate anyone and there are more than four of them, in the first four of them named as co-owners in the

vesting document) as trustees, to hold on a special statutory trust – the trust of land – now regulated by the Trusts of Land and Appointment of Trustees Act 1996. Under this trust, the trustees hold the interest in question on trust for all the co-owners as beneficiaries. Both the trustees' nominal title and the beneficial interest are co-owned. However, the trustees *must* hold the nominal title as joint owners (and any attempt to sever and convert a trustee's interest into an interest in common will be ineffective), whereas the beneficial interest can be held by the beneficiaries either in common or jointly, and, if jointly, then any beneficiary is free to sever and convert her joint entitlement into an interest in common at any time. The advantages of using the trust mechanism as a means of regulating the relationships between the co-owners themselves, and between them as a group and outsiders, is considered in detail in Chapter 16. However, for present purposes the relevant point is that it enables management to be separated from benefit, and confers management either on a single person (the co-owners can, if they want, decide to have only one trustee although for reasons which are considered in section 14.4 below this is rare and inadvisable) or on a limited group who are subject to the court's supervisory jurisdiction over trustees, and who can only act effectively in concert (because of the compulsory joint tenancy) and none of whom has a separable share (again because of the compulsory joint tenancy). This has advantages even when each co-owner is both a trustee and a beneficiary. This occurs very frequently – for example, if husband and wife decide to co-own their matrimonial home, they will nowadays probably decide to both hold the legal title to the fee simple, which must then be held by them jointly on trust for themselves either as beneficial tenants in common or as beneficial joint tenants. The advantage of imposing a trust even in such simple cases as this is that it then brings into operation statutory machinery (now contained in the 1996 Act) which gives the court effective powers to adjudicate between the co-owners when disputes arise. See further Chapter 16.

8.6. General and particular use rights

Some property interests allow the holder to make general use of the resource in question, whether for a limited or unlimited periods of time, and whether solely or in conjunction with others. Others, however, allow the holder to make only a limited, specific use of a resource over which some other person has general use rights. As we see in Chapter 9, the courts are particularly reluctant to expand the range of specific, or particular, use rights which are recognised as property rights.

Particular use rights encompass private, communal and public property rights. They fall within two general categories: rights to *use* someone else's land in a particular way (to walk across it, or have your drainage pipes run through it, or use it for recreational purposes) and rights to take a specific resource from someone else's land (to extract gravel from it, or cut down and take away trees or crops growing on it). We look at most of these rights – communal and public rights to

make a particular use of someone else's land, and rights to take resources from someone else's land – in Chapters 5 and 13. Here we concentrate on easements – i.e. private proprietary rights to make a particular use of someone else's land.

The modern statement of the requirements to be satisfied before a right can be classified as an easement appears in the judgment of Evershed MR in *Re Ellenborough Park* [1956] Ch 131, extracted at www.cambridge.org/propertylaw/. One of the points that is clear from his judgment is that, unlike a profit, an easement cannot exist in gross: it must be appurtenant to the land it benefits, and cannot be severed from that land and traded separately as a free-standing property right. Why is this? There are (at least) two possible answers. One of them is that the law will not give proprietary status to a right to make use of (and therefore diminish the value of) someone else's land unless that right enhances the value/utility of another piece of land: because land is in limited supply, no piece of land should be permanently diminished in value by the imposition of a proprietary burden (which will hinder development and change of use and restrict the uses that can be made of the land, and therefore make it less easy to sell, and increase the complexity and therefore the cost of the sale process) unless it will produce a corresponding permanent enhancement of the value of some other piece of land – the production of an increase in wealth generally is not sufficient. This would explain why I can have a proprietary right to use part of your land as a car park to serve my adjoining office and shop development (as in *London & Blenheim Estates Ltd* v. *Ladbroke Retail Parks Ltd* [1992] 1 WLR 1278), but cannot have a proprietary right to use it as a car park to enhance my business of running car parks.

The second possible answer is that the link between the use of one piece of land and the enhancement of the value of another piece of land provides a reasonably precise but flexible measure for quantifying the measure of the burden on the burdened land. If we know that a right of way over a pathway in a garden is for the benefit of the adjoining house and garden, this tells us the type and quantity of the traffic the path can expect to have to bear over the years. This explanation is consistent with the allied rule that a change in the character of the benefited land which has the effect of increasing or altering the nature of the burden on the burdened land extinguishes the easement (see *Atwood* v. *Bovis Homes Ltd* [2000] 3 WLR 1842).

Notes and Questions 8.3

1 Read *Re Ellenborough Park* [1956] Ch 131, either in full or as extracted at www.cambridge.org/propertylaw/, and consider the following:
   (1) Explain what is meant by the following:
      (a) an easement cannot exist in gross;
      (b) an easement must accommodate the dominant tenement;
      (c) a right cannot be an easement unless it is capable of forming the subject-matter of a grant.

(2) How do you distinguish a right that accommodates the dominant land from a right that provides a benefit to the owners/occupiers of the dominant land? Is it relevant to consider whether the dominant land would fetch a higher price if sold with the benefit of the right?

2 What, if any, are the objections to categorising the following as easements:
(a) car-parking rights (see the first instance decision in *London & Blenheim Estates Ltd* v. *Ladbroke Retail Parks Ltd* [1992] 1 WLR 1278);
(b) rights to wander at will over the servient land; and
(c) a right to a 'prospect' (i.e. a view over neighbouring land) or a right to the passage of radio/television signals across neighbouring land (see *Hunter* v. *Canary Wharf*, discussed in Chapter 6 above).

3 If the owner of the dominant land benefiting from an easement acquires additional adjoining land, should she be entitled to exercise the easement for the benefit of the additional land as well as for the benefit of the original dominant land? Compare *Harris* v. *Flower* (1904) 74 LJ Ch 127, CA, laying down the basic rule that the dominant land cannot be unilaterally extended in this way (applied and confirmed by the Court of Appeal in *Peacock* v. *Custins* [2001] 13 EG 152, at least partly on the basis that the original grantor could have extracted a higher price for the right if it was then known that it would, in effect, provide a greater benefit for the grantee) with *National Trust* v. *White* [1987] 1 WLR 907, where the Court of Appeal held that the benefit of the right of way extended to additional land acquired by the National Trust to make a car park for visitors to the archaeological site on the original dominant land.

4 The burden imposed on the servient land by an easement is a purely negative one. Consequently (unless the grantor and grantee agree otherwise), the servient owner is under no duty to carry out work to facilitate the exercise of the right: for example, she is not liable to maintain or carry out repairs to a path over which the dominant owner has a right of way. The dominant owner may himself carry out maintenance and repair work to a track over which he has a right of way, but may not improve it (*Mills* v. *Silver* [1991] 2 WLR 324). Sometimes the grant of an easement is expressly made subject to the dominant owner contributing towards repair and maintenance costs: on what basis is such an obligation enforceable against successors in title of the original dominant owner? (See *Hallsall* v. *Brizell* [1957] Ch 169.)