

Transactions at an Undervalue – Beneficial Interests and Declarations of Trust

Lyle v Bedborough [2021] EWHC 220 (Ch)

I. Facts

The Property was purchased in the joint names of Mr and Mrs Bedborough in 1994. In 2008 the Respondents' evidence is that they entered into an oral agreement by which Mr Bedborough would transfer his interest to Mrs Bedborough (the "2008 Agreement"). In December 2012, the Respondents entered into a declaration of trust by which they declared that they held their interests in the Property as tenants in common for Mr Bedborough as to a 5% share and Mrs Bedborough as to a 95% share (the "2012 Declaration").

Mr Bedborough relied upon the 2008 Agreement, being beyond the 5-year relevant period under S.339 on the Insolvency Act 1986, whilst the Applicant Trustees denied the 2008 Agreement had any effect with the only transfer being made pursuant to the 2012 Declaration, within the relevant period and at an undervalue.

II. Decision

The 2008 Agreement

The Respondents' case was that the 2008 Agreement came into existence following purely oral discussions between them. The court was particularly astute in these circumstances to seek transparent and reliable evidence given the self-interest of the Respondents and the lack of first-hand knowledge of the Applicants. The Respondents purchased the Property with the benefit of a joint mortgage with the deposit for the purchase provided by Mr Bedborough alone. Mr Bedborough also made all mortgage interest payments between 1997 and 2012. The Property was registered in joint names by TR1 which did not include a declaration of trust. The court held that the Respondents held the Property as joint tenants.

The court found that the Respondents did discuss the potential transfer of an interest in the Property in 2008 but that the evidence of what was discussed was imprecise. The court concluded that Mr Bedborough said he was prepared to transfer his interest to his wife but that this did not give rise to a constructive trust for the following reasons:

- There was no common intention that Mrs Bedborough should own the entire equitable interest forthwith (original emphasis).
- The Respondents realised some legal formalities would be needed to effect a transfer including the signing of additional documents.
- Mrs Bedborough did not approach the discussions thinking or expecting that they would themselves give her any greater interest in the Property.
- There remained extant issues to be considered and finalised including how future mortgage contributions would be managed.

- Neither Respondent left the 2008 discussions thinking that Mrs Bedborough would definitely ask Mr Bedborough to execute legal documents transferring the Property to her.
- The Respondents therefore realised that their discussions in 2008 were of no legal effect and at most set out an understanding as to what would, or might, happen to the Property in the future.

The 2008 Agreement, being entirely oral, could not have effected an express conveyance of a beneficial interest¹ nor could it have constituted a binding contract for a disposition of an interest in land.²

The interest could nonetheless have been transferred by way of common intention constructive trust, requiring (1) a common intention that the Property was no longer to be held as joint tenants and (2) Mrs Bedborough needed to have relied on the existence of that common intention to her detriment.

The court found that the requisite common intention was absent in this case.

The 2012 Declaration

The court held that the 2012 Declaration was valid and fell within the two-year period prior to the date of the bankruptcy. Mr Bedborough transferred a 45% interest in the Property with an unencumbered valued of £153,450.

The incoming value given by Mrs Bedborough was an agreement to pay £20,000 and her agreement not to seek further recompense from a £50,000 contribution towards renovations to the Property. It did not consist to any extent of any compromise of pending or threatened divorce proceedings or any associated right to seek a property adjustment order as Mrs Bedborough did not compromise her rights to seek relief in this regard.

The court valued the second element of consideration at nil upon reaching the conclusion that Mrs Bedborough was not entitled to an equitable account for her contributions and the value of any unliquidated claim given up was therefore valueless. The transaction effected by the 2012 Declaration was therefore made at an undervalue.

Remedial Order

The court did not accept that reversing the transaction conferred a windfall upon the Trustees. It was not appropriate to judge the value to be restored as at 2012, rather the date of the order was appropriate. The court was not apprised of the current value of the Property at the date of trial and therefore considered an order reversing the effect of the transfer was most suitable, rather than a purely monetary award.

As to returning Mrs Bedborough's consideration of £20,000 the court ordered that Mrs Bedborough was to receive a payment for the same, plus interest from December 2012 to the date of payment, from the proceeds of sale of the Property after expenses of the bankruptcy and before a distribution to HMRC.

III. Transfers of Beneficial Interests and Declarations of Trust

Lyle highlights the fundamental first question to be asked when considering S.339 undervalue and S.423 applications, namely has there been an effective transaction which can be unwound? The clawback provisions exist to unwind otherwise effective transactions and the problem can be particularly acute in

¹ S.53(1)(c) Law of Property Act 1925

² s2 of the Law of Property Miscellaneous Provisions Act 1989

the context of transfers of beneficial interests in land, often in the context of transfers between spouses or cohabiting couples.

The transfer of a beneficial interest alone is most often effected by one of the following methods:

- 1) An executed document expressing an immediate intention to transfer the interest vested in him to the assignee, the emphasis on the intention for an immediate transfer cannot be overstated³; or
- 2) Where the equitable chose is a beneficial interest under a trust, by executing a document directing the trustee to transfer the interest to the assignee or directing the trustee thenceforth to hold the interest on trust for the assignee.

Practitioners should also be aware of the following potential characterisations of a transaction:

- 1) As an agreement for value to assign which, if capable of being specifically performed, can give rise to an immediately effective constructive trust of the beneficial share.⁴
- 2) Surrendering a beneficial interest to enlarge the interest of another.

As can be seen from *Lyle*, questions of the conditionality of a transfer and whether the transfer was intended to take effect immediately or upon the completion of further formalities will be central to assessing whether the transfer was effective.

The most common and straightforward method of transferring a share in a jointly owned property is to utilise the TR1 form for a combined transfer of legal and beneficial interests.⁵ However, it will be important to note when first examining a case whether the TR1 purports to have been used for this dual purpose. Where it does not, its principal function is to transfer legal title and evidence of a sufficient written transfer of equitable rights should be sought out.

If no express written transfer can be identified, those seeking to challenge a transaction may be left to rely upon a common intention constructive trust. This is inherently difficult given the relevant intentions are those of the co-owners whose interests will often be adverse to those of the challenging party, as was the case in *Lyle*.

The potential consequences of an unnoticed failure to transfer a beneficial interest can be severe. Where a beneficial interest in a dwelling-house in fact remains with a bankrupt and meets the S.283A sole or principal residence criteria, it will vest in the trustee(s) automatically. From which point time begins to run towards the 3-year reversioning limit. The court cannot retrospectively extend time when 3 years has elapsed.

³ “The intention must be a “final and settled” intention to transfer, and not one which is qualified or contingent or a mere revocable mandate.²⁹³ The intention must also be to assign immediately (“there and then”).” Guest on the Law of Assignment, 3rd Ed at 1-44

⁴ Guest on the Law of Assignment 3rd Ed at 3-30

⁵ The usual method where a partner wholly disposes of their interest to a co-owner

The scope of S.283A includes the dwelling being the sole or principal residence at the time of the bankruptcy of (1) the bankrupt, (2) the bankrupt's spouse or civil partner or (3) a *former* spouse or civil partner.

***Re Munir* [2021] EWHC 278 (Ch) – Sham Declarations of Trust**

The final points of consideration are the principles which apply to declarations of trust sought to be challenged on the basis that they are in fact sham transactions.

The court in *Munir* recently considered a number of declarations of trust in the context of a claim seeking a declaration that the trusts were shams or a S.423 order in the alternative. The decision provides a useful exposition of the law in concerning shams. The key principles for reference are:

- The court will look for an intention, shared by all parties to the relevant document to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create. The inquiry is as to subjective intentions.
- The court may examine external evidence when assessing whether a document is a sham, including the parties' explanations, circumstantial evidence and subsequent conduct.
- In the case of unilaterally declared document, such as a declaration of trust, it is the intention of the settlor alone which is relevant. This is so where the settlor and trustee are one and the same person.
- Where a trust deed is made with a separate trustee as a party although a common intention between the settlor and any trustee is required, it is sufficient that the trustee went along with the settlor's wishes or did not care what he or she was signing.
- A sham transaction will still remain a sham transaction even if one of the parties to it merely went along with the shammer not either knowing or caring about what he or she was signing. e
Such a person would still be a party to the sham.

These principles are worth bearing in mind when, as often occurs, a surprise trust deed is introduced into the narrative of a case. Insolvency Practitioners and creditors will often find themselves at a disadvantage in running a sham argument given the focus of the inquiry is upon the subjective intentions of parties other than those challenging the transaction. In such cases emphasis can be placed on:

- The wording of the trust instrument.
- Any mention, or lack thereof, by beneficiaries of the trust or those who can be expected to have knowledge of a trust and to rely upon its provisions.
- The explanation for the late production of a trust deed.
- The use of a trust deed as a "rainy day instrument" not intended to have effect but to be available to give a false impression of the ownership of an asset when and if required.

James Saunders

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