

DILEMMA OF CREATING A CONSTRUCTIVE TRUST ON ILLEGAL PURPOSE

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Abstract - English law was received to Sri Lankan legal system in two ways mainly; by statutes and by judicial activism. In Sri Lanka present context, Law of trust is governed via substantive law and common law principles, mainly from the Trust Ordinance and by judiciary precedence. For decades the trust ordinance and case laws was consider as the supreme legal authority to adjudicate the legal issues relevant to the area of trust. According to the Trust Ordinance there are several types of trust can be established .Mainly express trust, implied trust (Constructive trust), resulting trust, and charitable trust .For the purpose of this paper, issues relating to the constructive trust is evaluated in detail. Comparing to the other types of trust constructive trust is much controversial. Hence it does not require verbal or documentary expressions to create a trust. In this backdrop doctoring of constructive trust is taken as offensive and defensive weapon by legal practitioners in the area that issues relating to the transactions of property. It should be the responsibility of judiciary to evaluate the cases in a wide spectrum. Since judiciary precedence is conceded as souses of law and it impact to the adjudicating process to establish the justice. Based on this backdrop it is clear that judgments should be competent and constant, if not it creates an ambiguity. This research paper is based to evaluate and indicate how creativity of judiciary impacts to establish the justice even it creates a dilemma: whether constructive trust can create on illegal purpose.

Key words - dilemma, Constructive trust, illegal purpose,

I. INTRODUCTION

The history of equity and trusts concerns the development of the body of rules known as equity, English trust law and its spread into a modern body of trust law around Commonwealth and the USA .The law of trusts was constructed as part of “equity”, a body of principles made by the Courts of Chancery, which sought to correct the strictness of the common law. The trust was an addition to

the law of property, in the situation where one person held legal title to property, but the courts decided it was fair, just or “equitable” that this person be compelled to use it for the benefit of another. This recognized a split between legal and beneficial ownership: the legal owner was referred to as a “trustee” (because he was “entrusted” with property) and the beneficial owner was the “beneficiary”. Trust law is a statutory bias adjudicating system introduced to SL by British when Ceylon was colony. Basically trust issues were adjudicated by Trust Ordinance and it was gradually developed to the area of common law in SL legal regime. In present context trust law is govern by Statutory law (Trust Ordinance) and Common law (judiciary precedence). Judgments of courts should be compatible and rationale without any ambiguity, since such case laws are considered as sources of law. Based on above facts this research is narrow down to evaluate and indicate how creativity of judiciary impacts to establish justice by not restricting to substantive law.

II OBJECTIVE OF THE PAPER

When adjudicating the property law issues connected to the constructive trust, normally courts consider the Trust Ordinance and past case laws to establish the justice. It is observed that in present context courts were taking creative steps to establish the justice when adjudicating issues relevant to Trust law. In this backdrop the objective of this paper is to: evaluate and indicate how creativity of judiciary impacts to establish the justice even it creates a dilemma: whether constructive trust can create on illegal purpose.

III. METHODOLOGY

The study adopts qualitative approach, using comparative study design. The material used in the study including legislation, judicial decisions, books, electronic/internet sources, journal articles. The study is principally an

analysis and comparison of legal provisions (both statutory and common law).

IV. DISCUSSION

A. What is meant by constructive trust

In the area of trust law there are different kind of trust can be created .According to the trust ordinance there are four types of trust is identified .Manly express trust, constructive trust ,resulting trust and charitable trust. As for the purpose of the paper it is important to identify what is mean by constructive trust .According to the Trust Ordinance.

Section 82: An obligation in the nature of a Trust (herein after referred to as a “constructive Trust”) is created in the following cases.

Section 83: Where it does not appear that transferor intended to dispose of beneficial interest.

Where the owner of property transfers or bequeaths it, and it cannot reasonably be inferred consistently with the attendant circumstances that he intended to dispose of the beneficial interest therein, the transferee or legatee must hold such property for the benefit of the owner or his legal representative.

Section 84: Transfer to one for consideration paid by another.

Where property is transferred to one person for a consideration paid or provided by another person, and it appears that such other person did not intend to pay or provide such consideration for the benefit of the transferee, the transferee must hold the property for the benefit of the person paying or providing the consideration.

It is evident that by analyzing the above sections how the constructive trust is created. Constructive trust is formed not by the way that express trust is created. There is no visibility of verbal or written agreement; the obligation is formed due to the conducts of parties. Moreover according to the section 83 the word attendant circumstances specifically indicate that implied conditions having an impact to create a constructive trust. These attendant circumstances must be clearly proven in the courts to create a valid legal constructive trust. Section 84 specifically elaborates the impotence of intentions of the parties. If transfer to one for consideration paid by another and it appears that such other person who did

not intend to pay or provide the such consideration for the benefit of the transferee the property should hold by the transferee for the benefit of the person who provided the consideration. In such instances if intention is prove courts may declare the judgment on benefit of transferor based on constructive trust .This is the core area of the paper comparatively discussed in later .

B. Creation of legal trust

Section 4 of the Trusts Ordinance is contained in Chapter II of the said Ordinance, which deals with the creation of Trusts. Section 4(1), which deals with lawful purpose are as follows:Trust may be created for any lawful purpose. The purpose of a trust is lawful, unless it is

- a. forbidden by law, or
- b. is of such a nature that, if permitted, it would defeat the provisions of any law, or
- c. is fraudulent, or
- d. involves or implies injury to the person or property of another or
- e. the Court regards it as immoral or opposed to public policy.”

Section 98: of the Trusts Ordinance refers to the saving rights of bona fide purchasers and reads as follows:

“Nothing contained in this Chapter shall impair the rights of transferees in good faith for valuable consideration, or create an obligation in evasion of any law for the time being in force.” Section 98 of the Trusts Ordinance, it is to be borne in mind, is contained in Chapter IX of the Trusts Ordinance, which deals with Constructive Trusts.

Section 4(1) of the Trusts Ordinance is specific with regard to the creation of Trusts, which could be for any lawful purpose. The said section has clearly defined the instances, where a trust could be regarded as unlawful

C. Constructive trust is established when Transfer to one for consideration paid by another.

In some circumstances, people do not buy the properties using their names. They buy the properties using another person’s name and after some time the person who paid

consideration asked back the property. By rejecting to give back the property is the area issue aroused, whether the property is transfer based on constructive trust or not is the core area to adjudicate. It is clear that according to the Trust Ordinance, if the constructive trust is form by fluffing the fundamental elements of section 84 it can be applicable. Person who paid the consideration have the right to own the property and transferee must hold the property on benefit of transferor

According to Dr. L.J.M. Cooray refers to the definition given by Keeton, which is as follows:

“The relationship which arises wherever a person called the trustee is compelled in Equity to hold property, whether real or personal, and whether by legal or equitable title for the benefit on some persons (of whom he may be one and who are termed cestuis que trust) or for some object permitted by law, in such a way that the real benefit of the property accrues not to the trustee but to the beneficiaries or other objects of the trust”

But from the Muniyanidi Nachie v Kayambo (2 CALR56) case followed the same judgment in Saroja Nisansala v Aberfoyle (2011 BLR 379) court consider a same methodology even the scope is contradicted by comparing to other cases. It is impotent to analysis these two case laws in depth since the core area of this research paper is based on these two judgments. In Muniyanidi Nachie v Kayambo, the plaintiff was not a citizen in Sri Lanka, when he bought a property convincing the land to his sister’s name. The main intention to convincing the land to his sister is to avoid from tax that he obligate to pay according to the 1963 No 11 Finance Act. After some time P gains the citizenship in SL and asked his sister to re-convey the property to him, by rejecting the request P sue against her sister due to violating the elements of constructive trust. Defendant counselor argued that when Section 98, 4(1) and (2) read together plaintiff do not have valid grounds to establish a constructive trust. Because P has taken an approach to avoid paying tax according to the section 58 of the Finance Act. Due this augment prima Facie it is evident that P’s action is against the sections 4 of the Trust ordinance. Hence Plaintiffs agreement becoming null and void due fraud intention and deviating from revenue law. But adjudicating the issue, court considers that deviating from revenue law only do not make an invalid ground to established a constructive trust.. Parkidner J. pointed out that “according to the section 84 of the Trust ordinance Plaintiff has reasonable grounds to establish a constructive trust. Section 4 does not subject to the issues in revenue

law” judgments were delivered in favor to plaintiff. In Saroja Nisanasala v Aberfoyle courts consider the same rational what was taken in the Muniyanidi Nachie’s case .At the stage of hearing both learned Counsel agreed that the apple could be argued on the basis of the following questions:

1. Could the plaintiff –respondent in the circumstances of the case, plead a constructive trust?
2. Is the trust alleged by the plaintiff-respondent contradicted with provisions in section 4(1) and 98 of the Trust Ordinance?

Summary of the held is as follows

- a. An act could not be treated as invalid constructive trust simply due to illegality
- b. Section 4 (1) of the TO as stated earlier clearly refers to the fact that a trust may be created for any lawful purpose, The unlawful purposes, which would forbid a Trust being created, are specifically referred to in section 4(1) .Learned Counsel for the appelland took up the position that the intention to avoid the payment of 100% as tax on the land transaction would clearly show the objective of the plaintiffs respondent’s action. However unlawful intention alone cannot make the contact illegal.
- c. Section 58(1) read with section 59 of the Finance Act had imposed a tax and empowered the Commissioner of Inland Revenue to recover the tax if in default due to the non-payment form the person whom it has become due.
- d. Section 59of the Finance Act, with the effect of the non-payment of the tax, clearly stated that the commissioner of IR, upon notification of such default by the registrar of land or lands or the company as the case may be, shall take step for the recovery of the tax deemed to be in default.

By analyzing the above two cases prima Facie evident that these two judgments arecontradicting with the Statutory provisions of Trust Ordinance. With this backdrop it create dilemma whether constructive trust is able to formulate on illegal purpose. But according to the judgment in Saroja Nisansala’s case mentioned that “unlawful intention and unlawful purpose alone cannot make the contact illegal” To justify these arguments counsels of plaintiff-respondent sited following source:

Dr. L.J.M. Cooray in his work on the subject of Trust has discussed the nature of an unlawful trust. According to Dr. Cooray, if sections 4 and 98 of the Trusts Ordinance had been omitted, the general law of the land would have prevented the operation of trusts for unlawful purposes. Referring to trusts for unlawful purposes, Dr. Cooray refers to Prof. Weeramantry's Treatise on the Law of Contracts. Prof. Weeramantry, referring to the breach of revenue regulations clearly states that the mere "breach of revenue regulations would not itself render illegal a contract in respect of which they are imposed". It could also be argued that what the plaintiff-respondent intended by purchasing the property in the name of the appellant was not to breach the revenue legislation, as in any event, at the stage of a re-transfer and at the stage of registration of the said land, the plaintiff-respondent would have to make the payment of tax in terms of the Finance Act.

Act could not be treated as invalid simply due to illegality. In *Fernando v Ramanathan* ((1913) 16 N.L.R. 337), a Full Bench at that time, had decided that a deed is not invalid on the ground of illegality because it is contrary to what may be termed the policy of an Ordinance. Considering the implied statutory prohibitions, Prof. Weeramantry has referred to the decision in *Mohideen v Saibo* ((1913) 17 N.L.R. 17), *Georgiades v Klompje* ((1943) T.P.D. 15) and "Pollock" and had stated that:

"Where a statute merely imposes a penalty on the performance of certain acts without declaring such acts to be illegal or void, the question arises whether such acts are void. In such cases we must look to the intention of the legislature to see whether the imposition of the penalty implies such a prohibition as to make the resulting contract void. The imposition by the legislature of a penalty on any specific act or omission is prima facie equivalent according to "Pollock" to an express prohibition. Such provision is however, only prima facie evidence and is not enough by itself to make a contract to do that act illegal or void."

Learned Counsel for the appellant contended that in terms of section 4(1) of the Trusts Ordinance there is no possibility of relying on a Trust, when the purpose is illegal:

Section 4(1) of the Trusts Ordinance as stated earlier clearly refers to the fact that a trust may be created for any lawful purpose. The unlawful purposes, which would forbid a Trust being created, are specifically referred to in section 4(1). Learned Counsel for the appellant took up the position that the intention to avoid the payment of

100% as tax on the land transaction would clearly show the objective of the plaintiff-respondent's action. However, unlawful intention alone cannot make the contract illegal. Referring to unlawful intentions, Prof. G.L. Peiris (Some Aspects of the Law of Unjust Enrichment in South Africa and Ceylon) states that,

"A significant development in the modern law is that an unlawful intention, bilaterally entertained, is no longer an absolute bar to restitution. This principle was recognized for South African law in 1939 in *Jajbhay v Cassim* where Stratford, C.J. declared that "the rule expressed in the maxim in pari delicto potior est conditio defendentis is not one that can or ought to be applied in all cases. It is subject to exceptions which, in each case, must be found to exist only by regard to the principle of public policy." Watermeyer, J.A. said: "the principle underlying the general rule is that the Courts will discourage illegal transactions, but the exceptions show that where it is necessary to prevent injustice or to promote public policy, they will not rightly enforce the rule." This view has been authoritatively accepted as applicable to the law of Ceylon."

IV. CONCLUSION

It is evident that, no material had been adduced before the Court to show that the transaction in question had been for an unlawful purpose in terms of section 4(1) of the Trusts Ordinance. By analyzing above facts it indicts that justifications are made to prove that "unlawful intention and unlawful purpose alone cannot make the contact illegal". With this backdrop it creates a dilemma whether there is possibility to create a constructive trust on illegal purpose. It should be noted that law must establish the justice, if this case were interpreted as illegal transaction only by limiting to substantive law entire course will be null and void. It will be an injustice to the person who made the consideration. It is evident that rational behind this judgment was to establish the justice based on principles of equity and fairness. Also it is significant to emphasize the augment what was cited by plaintiff-respondent by justified the "unlawful intention and unlawful purpose alone cannot make the contact illegal". It clearly indicates that law should be necessary to prevent injustice. It is essential to appreciate to Dr. Shiranin A. Bandaranayake C J to her judgment by mentioning that "Considering the submissions made by both learned Counsel for the appellant as well as the plaintiff-respondent it is apparent that no arguments were put forward by the appellant that if it was allowed, the transaction which took place between the appellant and the plaintiff-respondent would defeat

the provisions of any law. Similarly no material was put forward to substantiate the fact that the said transaction is not one which is forbidden by law, fraudulent, involves or implies injury to the person or property of another and the Court regards it as immoral or opposed to public.” If above facts were put forwarded precisely the judgment may have taken a different conclusion. It is obvious that even dilemmas were created court were able to establish the justice by analyzing case in wider spectrum without restrictive to traditional methodology. Finally it should be noted that from above analysis following principles were derived and it makes an impact to the Sri Lanka legal regime.

1. Contract could not be treated as invalid simply due to illegality.
2. Unlawful intention, bilaterally entertained is no longer an absolute bar to restitution,
3. Unlawful intention cannot make the contract illegal.
4. Breach of revenue regulations would not itself render illegal a contract in respect of which they are imposed
5. Any transaction to be unlawful; parties should adduce to the courts to prove unlawfulness.
6. If any transaction defeats the provisions of any law, forbidden by law, fraudulent involves implies injury to person or property and regards it as immoral or opposed to public policy such transactions will be null and void.

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