Secret trusts

In this month’s CPD we are going to look at a secret trusts and ensure that the student can identify and distinguish between the two different types of secret trusts. The paper will also ensure we understand the justification for enforcing the two types of secret trusts and make sure we are aware of the problems which are associated with these trusts.

The starting point to remember is that a secret trust is an equitable obligation communicated to an intended trustee during the testator’s lifetime, but this trust will be attached to a gift arising from the testators will.

There are two types of secret trust which can arise 1) a full secret trust and 2) a half secret trust. The first arises where the existence of the trust as well as is terms are concealed from the will, however the testator would have communicated the terms of the trust to the trustee during his lifetime.

If we compare this to a half secret trust which arises where the will acknowledges the existence of the trust but the terms of the trust are concealed on the face of the will and again the terms of the trust are communicated to the trustees in the testators lifetime.

Remember a testator who wishes to create a trust over his property upon his death is required to express this intention as well as the terms of the trust in his will. The formalities necessary to create a valid will are required to be complied with.

These formalities necessary to create a valid will are required to be complied with. These formalities are enacted in section 9 of the Wills Act 1837. The basic requirement is the need for a written will which is signed by the testator and witnessed by two or more witnesses.

The secret trust is an exception to this rule because in limited circumstances where a testator has not fully complied with the formalities as given under section 9 of the Wills Act 1837, equity will nevertheless impose a duty upon the party acquiring the property under the will (legatee or devises) to carry out their wishes of the testator. This will require the legatee or devisee to hold the property upon trust for the secret beneficiaries.

On a testator's death the will becomes a public document and wills are consequently open to the public scrutiny. The testator may wish to make provision, after his death, for what he considers to be some embarrassing object, such as a mistress or an illegitimate child. To avoid such a problem he may make a gift by his will to an intended trustee, subject to an understanding to hold property for the benefit of the secret beneficiary.

A fully secret trust is an obligation which is fully concealed on the face of the will. The obligation is communicated to the legatee during the lifetime of the testator and the will transfers the property to the legatee without the mention of the existence of a trust, i.e. the existence and the terms of the trust are fully concealed on the face of the instrument creating the trust, namely the will, for example a disposition by will ‘to A absolutely’.
Whereas a half-secret trust is intended when the will indicates or acknowledges the existence of the trust but the terms are concealed from the testators will. The trustee will then take the property on terms as communicated of the terms effected inter vivos, for example a disposition by will ‘to A on trust for purpose communicated to him’.

Thus, assuming there has been a valid communication of the terms of the trust has been acknowledged on the face of the will or not. This is important, for the two types of secret trusts are subject to different rules.

In enforcing secret trusts, equity does not contradict section 9 of the Wills Act 1837 because the trust operates outside the Wills Act. This is the dehors theory.

The bare minimum requirements are a validly executed will which transfers property to the trustees whether named as such under the will or not; and the acceptance by the trustees inter vivos of an equitable obligation.

Section 15 of the Wills Act 1837 is not applicable in this context. Section 15 of the 1837 Act enacts that an attesting witness loses his interest under the will. It will be recalled that one of the formalities under the Wills Act 1837 involves two or more attesting witnesses.

The Wills Act 1968 amended this requirement to allow additional attesting witnesses exceeding two to acquire property under the testators will. Accordingly, if there are three attesting witness under a will and one of these has been bequeathed property under the will, that witness’s interest will not lapse. In Re Young [1951] Ch 344 the court decided that the secret trust operated outside the will in the sense that it was immaterial that one of the intended beneficiaries under the trust, as distinct from the will, witnessed the will.

A variation of the dehors theory is to the effect that the trust is created inter vivos and outside or independently of the will. The notion here is that the trust is created by reason of the personal obligation accepted by the legatee. Thus, the argument proceeds on the assumption that the date of the creation of the trust is during the lifetime of the settlor.

The theory is fundamentally flawed in both trust and probate law. On the date of the communication of the terms of the trust to the legatee (trustee) the trustee has not acquired the intended property. Thus, there cannot be a valid trust. In probate law a will speaks from the date of the death of the testator. Before this date the legatee has merely a hope of acquiring a benefit under the will.

Traditionally, the trust property is transferred by will on condition that the trustee) who takes under the will as legatee or devisee) holds the property subject to an agreement entered into between the testator and himself. Likewise, the secret trust principles will extend to intestacies. There are occasions where the settlor decides not to make a will on the faith of a promise by his next of kin to dispose of the property in accordance with the settlors wishes as disclosed to him during the lifetime of the settlor.

The theoretical justification for enforcing secret trust is to prevent fraud. The court originally applied the maxim ‘Equity will not allow a statute to be used as an engine for fraud’. The
statute in this respect is the Wills Act 1837. The jurisdiction adopted by the courts in order to enforce secret trusts was to prevent the legatee or devisee fraudulently denying the binding nature of his promise and attempting to set up section 9 of the Wills Act 1837 as a defence, for example if, during his lifetime, a testator (T) made an agreement with (A) to the effect that on T’s death, £50,000 would be transferred to him to hold on trust for B and T made a will to that effect. Following T’s death, it would be a fraud on the estate of T and B for A to deny the agreement, or non-compliance with section 9 of the Wills Act 1837 and claim property beneficially.

The persons who may be the victims of the fraud by the legatee are the testator and the beneficiaries under the intended secret trust. Consequently the court will step in and compel A to honor his agreement.

But half-secret trust cannot be justified on this basis, for the will transfers the property to the persons named as trustees and such persons are not allowed to take property beneficially. The trustee may not profit from his fraud. If the intended half-secret trust fails, a resulting trust will be set up. The effect is that this notion of the fraud theory cannot justify the existence of half-secret trusts.

An alternative basis for enforcing secret trusts is the transfer and declaration theory. The approach here is that the will transfers the property to the trustee, subject to an express, conditional declaration of trust executed by the testator outside the will. The secret trust becomes effective when the trustee acquires the property under the testators will, subject to the valid declaration.

The court steps in and compels the trustee to carry out the wishes of the testator as indicated on the death of the testator and specifically when the legatee acquires the property. The trust is not created inter vivos, but on death, and subject to an inter vivos declaration or communication of the testator wishes. This approach was advocated by Lord Summer in Blackwell v Blackwell [1929] AC 318:

‘The court of equity finds a man in the position of an absolute legal owner of a sum of money which has been bequeathed to him under a valid will and it declares that, on proof of certain facts relating to the motives of the testator, it will not allow the legal owner to exercise his legal rights to do what he wishes with the property. In other words it lets him take what the will gives him and then makes him apply it as the Court of Conscience directs, and it does so in order to give effect to the wishes of the testator, which would not otherwise be effectual’

Therefore there are a set of requirements which need to be fulfilled to enforce a secret trust, the first is a claimant is required to prove that the testator, during his lifetime, communicated the terms of the trust to the legatee.

When it comes to when communication of the terms of the trust must take place there is a key distinction between fully and half secret trusts. With a fully secret trust the communication of the trust to the trustees can take place at any point in the testator’s lifetime. With a half-secret trust the communication must take place before the execution of the Will.
The communication may take place directly by means of an oral statement or in writing outside the will. In addition, communication may take place constructively, i.e. delivery of a sealed envelope containing the terms of the trust to the trustee which is headed ‘Not to be opened before my death’. Provided that the trustee is aware that the contents of the envelope is connected with the testators will, communication is deemed to be effective on the date of the delivery of an envelope as illustrated in the case of *Re Keen* [1937] Ch 236.

The second requirement is the trustee is required to accept the trust obligation under the testator’s lifetime. This may be manifested by means of an acknowledgement by the legatee (trustee) to be bound by the terms of the trust.

Alternatively, acceptance may exist through acquiescence or silence on the part of the legatee. Once the legatee is aware of the intention of the testator and his intention is complete in the sense that all the terms have been communicated to the legatee, he is bound to hold on trust for those purposes. The legatee is not required to do anything positive to demonstrate acceptance, he is deemed to accept the terms of the trust once he is aware of the testator wishes during his lifetime.

Brightman J, in *Ottway Norman* [1972] Ch 698 identified the basic requirements for a fully secret trust:

‘It will be convenient to call the person upon whom such a trust is imposed the “primary donee” and the beneficiary under the trust “secondary donee”. The essential elements which must be proved to exits are:

1) *The intention of the testator to subject the primary donee to an obligation in favour of the secondary donee;*  
2) *Communication of that intention to the primary donee: and*  
3) *The acceptance of the obligation by the primary donee either expressly or by acquiescence, it is immaterial whether these elements precede or succeed the will of the donor,“*

Where the legatee does not wish to be bound by the terms of the trust communicated to him he is under an obligation to notify the testator of his refusal during the testator’s lifetime. Failure to accomplish this means that the legatee is bound by the terms communicated to him. In *Moss v Cooper* (1861) 1 J & H 352 it was decided that a legatee’s failure to communicate his attention to the testator during the latter’s lifetime did not absolve him from the liability to hold on trust for purpose known to him.

If there is no agreement between the testator and the legatee whereby the transferee is intended to hold as trustee, the transferee takes beneficially and may set up section 9 of the Wills Act 1837 as a defence here is between a legacy and a legacy upon trust.
If the transferee agreed to hold the property on trust, but the terms of the trust have not been communicated during the testator’s lifetime, the transferee will hold the property on resulting trust for the testator’s heir.

The intended secret trust fails because there has been a failure to communicate the terms of the trust to the legatee during the lifetime of the testator. But, since the legatee is aware that he is required to hold on trust and acquires the property on the basis of this understanding, he holds the same on resulting trust for the testator. This principle was applied in Re Boyes (1884) 26 Ch D 531.

In the case of Re Boyes the testator by their will transferred property to a legatee, having secured an agreement from the legatee to hold on trust. The testator died before he communicated the terms to the legatee. The court decided that the intended secret trust failed but a resulting trust was created for the testator’s heirs.

A fully secret trust obligation normally takes the form of the legatee (trustee) holding the property on trust for the secret beneficiary. Alternatively, the obligation may involve the legatee executing a will in favour of the secret beneficiary. In this event, the legatee may enjoy the property beneficially during his lifetime, but the obligation undertaken requires him to transfer the relevant property by his will to the named beneficiary. Accordingly, there are two beneficiaries involved in the transaction the ‘primary beneficiary’ who acquires an interest for life and the ‘secondary beneficiary’ who is entitled to acquire the property under the will of the primary beneficiary.

Where a testator leaves property to two or more legatees, but informs one or some of them (but not all of them) of the terms of the trust, the issue arises as to whether the uniformed legatee are bound by the communication to the informed legatees. The solution here depends on the communication and the status of the legatees. If (a) the communication was made to the legatees before or at the time of the execution of the will and (b) they take as joint tenants, the uniformed legatees are bound to hold for the purposes communicated to the informed legatees.

The reason commonly ascribed to this principle is that no one is allowed to take property beneficially under fraud committed by another. But if any of the above conditions are not satisfied, the uniformed legatees are entitled to take the property beneficially; the reason stated for this aspect of the rule is that the gift is not tainted with any fraud in procuring the execution of the will.

Thus, if some of the legatees were told of the terms of the trust after the execution of the will but during the lifetime of the testator, the uniformed legatees will take part of the property beneficially. The informed legatees, of course, will hold on trust. In Re Stead [1900] 1 Ch 237, Farwell J reviewed the authorities between a gift made on the faith of an antecedent promise and a gift left unrevoked on the faith of a subsequent promise to carry out the testator’s wishes. He added however, that he was bound by the principle. This rule may not be extended to half secret trusts for the trustee on the face of the will is not entitled to the property beneficially.
Conclusion

This paper has given a brief outline of the use of secret trusts and how these can be created in comparison to those which we are more familiar with, for example express trusts such as discretionary or immediate post death interest trusts. Hopefully you now have a greater understanding of how these trusts work in practice and can advise clients who wish to create these types trusts of the potential dangers.