

Secret and Half Secret Trusts

For this month's CPD paper we are going to look at the mystery world of secret trusts and the differences 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.

INTRODUCTION

A secret trust is an equitable obligation communicated to an intended trustee during the testator's lifetime. The trust will be attached to a gift, or at least what looks like a gift, arising within the testator's will.

There are two types of secret trust:

- 1) a fully secret trust; and
- 2) a half secret trust.

The distinction between the two types of secret trust is important as the rules for establishing if they are valid differ slightly depending on if the trust is fully or half secret.

HISTORICAL BASIS

On a testator's death when a will is admitted to probate it becomes a public document and is consequently open to 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, without the existence of that person or his provision for them being made known to his family. To avoid such a problem he may make a gift by his will to an intended trustee, subject to an understanding that they will hold property for the benefit of the secret beneficiary.

Fully secret trusts have a long history in English & Welsh trust law. The first cases where the courts upheld secret trusts date from the 17th century, and by the mid 18th century they were being regularly and clearly upheld.

Half secret trusts were less enthusiastically upheld. It wasn't until the case of *Blackwell v Blackwell and others* [1929] AC 318 that the courts finally confirmed their validity. Until that point the common reason for finding against them was that they blatantly 'gave the go-by' the Wills Act 1837. We'll discuss this more later when we consider the criticisms of the enforcement of secret trusts.

DISTINCTION BETWEEN FULLY AND HALF SECRET TRUSTS

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. An example of how this may look on the will itself would be a gift like: 'I give the sum of £250,000 to A absolutely'. To anyone viewing the will this looks like a straightforward gift of money to A. In reality the testator before his death has asked A to hold this sum on trust for B instead.

A half secret trust arises when the will indicates or acknowledges the existence of the trust but the terms are concealed from the testator's will. The trustee will then take the property on the terms of the trust that were communicated to them during the testator's lifetime. In a will this could look like: 'I give the sum of £250,000 to A to hold on trust for the purposes communicated to him'. This time it is clear that A isn't actually the beneficiary of the sum and there is a trust present, but a person viewing the will still has no idea who the real beneficiary is or what the terms of the trust are.

HOW ARE THEY CREATED?

To be valid the secret trust must comply with the requirements set out in the case of *Ottaway and another v Norman* [1972] Ch 698. That is:

1. The testator must intend to subject the trustee (the person who would otherwise take absolutely under the will) to an obligation in favour of the beneficiary;
2. The intention must be communicated to the trustee during the testator's lifetime, this can be either in writing or verbally; and
3. The legatee must accept the obligation.

When it comes to when the 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. by 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 testator's will communication is deemed to be effective on the date of the delivery of the envelope. This was illustrated in the case of *Re Keen* [1937] Ch 236.

When it comes to the legatee accepting the obligation acceptance may exist through acquiescence or silence on their part. Once they are 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's wishes during his lifetime if he does nothing to reject the obligation.

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 acceptance or refusal to the testator during the testator's lifetime did not absolve him from the liability to hold on trust for the purposes known to him.

If there is no agreement between the testator and the legatee whereby the transferee is intended to hold as trustee, the legatee takes the legacy themselves as a beneficiary instead.

If the legatee agreed to hold the property on trust, but the terms of the trust have not been communicated during the testator's lifetime the intended secret trust fails because there has been a failure to communicate the terms of the trust. 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 on resulting trust for the testator's estate. 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.

Complications where there are multiple legatees

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 uninformed legatees are bound by the communication to the informed legatees. Are they under any obligation to hold as trustees, or are they simply beneficiaries?

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 uninformed 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 uninformed legatees are entitled to take the property beneficially. The informed legatees, of course, will hold on trust.

This rule applies to fully secret trust. It does not extend to half secret trusts as the trustee on the face of the will is not entitled to the property beneficially in half secret trust cases.

CRITICISMS OF ENFORCEMENT OF SECRET TRUSTS

Ordinarily 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 are set out in section 9 of the Wills Act 1837, which all Will Writers ought to be familiar with. The key requirements are the need for a will to be made in writing which, signed by the testator and witnessed by two or more witnesses.

The enforcement of secret trusts appears to be in direct conflict with the formalities of the Wills Act 1837. Policy reasons requiring wills to be in writing and executed a certain way appear to go out the

window when it comes to enforcing secret trusts; they appear to be a glaring exception to the usual rules.

Three separate legal theories have arisen to justify the enforcement of secret trusts. Lead commentators all seem to agree that none of these theories are actually logical, but secret trusts are enforced nonetheless.

1. Secret trusts operate outside of the will (the 'dehors theory').

The dehors theory states that secret trusts are enforceable and not in contradiction of the Wills Act 1837 because they operate outside of the will. They're therefore not a succession law issue at all, but part of the law of trusts. The obvious problem with this theory is how it can possibly justify half secret trusts. A half secret trust operates at least half within the will.

2. Avoidance of fraud

Another theoretical justification for enforcing secret trusts is to prevent fraud. One of the equitable maxims is 'Equity will not allow a statute to be used as an instrument for fraud'. The approach adopted by the courts in order to enforce secret trusts was to prevent the fraudulently denying the binding nature of his promise and attempting to set up section 9 of the Wills Act 1837 as a defence – or using the Wills Act 1827 as an instrument for his fraud. By way of 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 on B for A to deny the agreement, relying on non-compliance with section 9 of the Wills Act 1837 to claim the money for himself as a beneficiary.

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.

3. Half secret trusts are analogous with the doctrine of incorporation by reference

This is a bizarre attempt at justifying half secret trusts as the doctrine of incorporation by reference has nothing to do with secrecy. A document incorporated by reference becomes part of the will and is admissible to probate with it, becoming a public document. This is the exact scenario that a secret trust is set up to avoid

MISCELLANEOUS COMPLICATIONS

What if the trustee dies before the testator?

In an ordinary express trust the death of the trustee before the testator would not cause an issue. The trust would still take effect and another trustee would be appointed to take the deceased trustee's place. This is another principal of equity supported by the maxim "Equity will not allow a trust to fail for want of a trustee".

If the trustee of a secret trust predeceases the testator though this can cause a problem. Say the testator left a gift to Y expressed as a gift to him beneficially, e.g "I give the sum of £50,000 to Y". On the

face of it this is an absolute gift to Y so if Y dies before the testator the gift lapses. It was suggested in the case of *Re Maddock* [1902] 2 Ch 220 that a fully secret trust (like the one expressed above) would fail completely.

It is suggested that a half-secret trust could survive the trustee predeceasing as it is clear in the will that the legacy is subject to a trust. There is no authority on this though as the point has never been tested in a court. In any event it would rely on someone other than the trustee being aware of the terms of the secret trust.

What if the trustee of the secret trust witnesses the will?

Under section 15 of the Wills Act 1837 a beneficiary under a will loses their benefit under it if they act as a witness to the will, or if their spouse or civil partner acts as a witness. The question is does this principle extend to the trustee of a secret trust?

In the case of a fully secret trust the gift would be void if the legatee acted as a witness as on the face of the will it appears as a gift to that legatee, so their acting as a witness would forfeit the legacy. In the case of a half-secret trust the gift would not be void, as it is clear on the face of the will that it is not a gift to the legatee absolutely, but for them to hold on trust so their status as a trustee is made clear.

The logical follow up question is what if the secret beneficiary witnesses the will? In *Re Young* [1951] Ch 344 it was held that the beneficiary of a half secret trust would not lose his entitlement if he acted as a witness as the benefit is not derived from the will but from the trust. There is no authority on the position with fully secret trusts, but it is likely that the same principle would apply.

CONCLUSION

This paper has given a brief outline of the use of secret trusts and how these can be created. 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.

Important Reminder:

These notes are produced solely for the benefit of SWW members when completing the July 2020 CPD test to gain 1 hour of structured CPD towards their annual quota. The notes do not represent legal advice and no reliance can be made on the content of the notes in any or individual specific client circumstances. Having read the notes members should cement their understanding by considering further reading around the subject – cases details can be found by searching the case references using BAILII or GOOGLE.