

Title

Equity's ancient good-faith-purchaser-for-value-without-notice (BFP) doctrine remains a critical component of trust jurisprudence: The practical considerations for today's settlors, trustees, beneficiaries, and third-party transferees of entrusted properties.

Text

Nowadays, if a student in a U.S. law school brushes up against BFP doctrine at all, it is likely to be at the intersection of Property and Contracts. Assume the rightful owner of a painting contracts to sell it to a museum. Instead of transferring to the museum legal title to the painting pursuant to the terms of the contract, the owner proceeds in exchange for something of equivalent value to transfer legal title to a third party who is unaware of (and could not reasonably be expected to be aware of) the contract's existence. The BFP may keep the painting. "Where the equities are equal, the law shall prevail" goes the maxim. As the museum and the third-party purchaser are equally innocent, equity declines to interfere with the purchaser's legal title. The museum, of course, has an action against the transferor for breaching the contract. Had the transferor stolen the painting, he would not have had good title to the painting and thus could not have effectively conveyed the painting to anyone, including a BFP. This in a nutshell is the applicable black-letter law. Nuances and exceptions, statutory and otherwise, are beyond the scope of this posting.

BFP doctrine, however, takes center stage when it comes to the law of trusts. Recall that legal title to entrusted property is in the trustee. As to the world, the trustee is the owner of the property. This definitive attribute of the trust relationship has enormous practical significance. Assume one is trustee of a noncharitable trust an express purpose of which is to retain and curate a valuable painting. In blatant violation of the trust's terms the trustee conveys the legal title to a BFP. The BFP may keep the painting, the trust beneficiaries and the BFP being equally innocent of the travesty. The "equities" are equal in other words. Of course, the beneficiaries (and possibly the settlor as well) would have an action in equity against the trustee personally for breach of trust. And the sales proceeds themselves, of course, are rightfully trust property.

Some observations: First, BFP doctrine is nowhere covered in the Uniform Trust Code. Second, most, if not all, American law schools no longer require that their students take Equity. Third, Equity is no longer on the list of subjects to be tested on the bar-exam. Finally, that a trustee of a trust may effectively convey its property to a BFP in flagrant violation of its terms is one more reason why trustee selection is serious business. Prospective settlors and their advisors take note. BFP doctrine in the trust context is taken up generally in §8.15.63 of *Loring and Rounds: A Trustee's Handbook* (2022), which section is reproduced in the appendix below. The Handbook is available for purchase at <https://law-store.wolterskluwer.com/s/product/loring-rounds-a-trustees-handbook-2022e-misb/01t4R00000OVWE4QAP>.

Appendix

§8.15.63 Doctrine of Bona Fide Purchase; the BFP [from *Loring and Rounds: A Trustee's Handbook* (2022), available for purchase at <https://law-store.wolterskluwer.com/s/product/loring-rounds-a-trustees-handbook-2022e-misb/01t4R00000OVWE4QAP>].

If my trustee conveys the land to a third person who well knows that the trustee holds for my use, I shall have a remedy in the Chancery against both of them: as well against the buyer as against the trustee; for in conscience he buys my land.—1471 English decision¹⁰⁶⁹

The rule of purchase for value without notice or bona fide purchase is an affirmative defense to a claim for restitution, a topic that is taken up in §7.2.3.3 of this handbook. “One who purchases an asset for value, without notice of competing claims, takes the asset subject to prior legal interests, but free of equitable interests to which the asset was subject in the hands of the grantor.”¹⁰⁷⁰ In the trust context that simply means that a trustee generally may transfer his or her title to the trust property to a BFP, who will take the property free of trust. The Restatement (Third) of Trusts is fully in accord.¹⁰⁷¹ The trustee, however, cannot convey to the purchaser a more extensive *legal title* than the trustee had to begin with.¹⁰⁷² Thus, if the trustee acquires title via forged documentation, the trustee cannot convey the title to a BFP, the trustee’s title being void *ab initio*.¹⁰⁷³

The BFP concept's legal backdrop. When a trustee sells trust property to a third person and the transaction is not in breach of trust, the third person holds the property free of trust.¹⁰⁷⁴ On the other hand, when a trustee *in breach of trust* transfers to a third person title to an item of trust property, the transferee takes it subject to the trust and to the beneficiary's equitable interests thereunder. Otherwise, the transferee would be unjustly enriched.¹⁰⁷⁵ This is the case even if the

¹⁰⁶⁹Y.B. 11 Edw. 4, Trin., fol. 8, pl. 13 (1471), translated in Frederic William Maitland, *Maitland Selected Essays* 166 (H.D. Hazeltine ed., Cambridge Press 1936).

¹⁰⁷⁰Restatement (Third) of Restitution and Unjust Enrichment §66 cmt. a.

¹⁰⁷¹See Restatement (Third) of Trusts §108(2).

¹⁰⁷²Restatement (Third) of Restitution and Unjust Enrichment §66 cmt. a.

¹⁰⁷³See *Young Sook Yi v. Seung Jin Oh*, No. B275195, 2017 Cal. App. Unpub. LEXIS 5484 (Aug. 8, 2017) (unpublished).

¹⁰⁷⁴5 Scott & Ascher §29.1.

¹⁰⁷⁵See §8.15.78 of this handbook (unjust enrichment).

transfer is a breach of trust occasioned by the death of the trustee.¹⁰⁷⁶ In other words, the transferee, if innocent, is a resulting trustee of the subject property, and if not innocent, then a constructive trustee of it.¹⁰⁷⁷ As such, he may be ordered by the court in the exercise of its equitable powers to reconvey the title back to the trustee or to his successor in office.¹⁰⁷⁸ The doctrine of bona fide purchase is an exception to this general rule.¹⁰⁷⁹

The equitable rights of the good-faith purchaser for value (BFP). If the transferee is a bona fide or good-faith purchaser for full value (BFP) of the item of property, the transferee may keep the item,¹⁰⁸⁰ or transfer it on to a fourth party free of the trust and its attendant equities, *notwithstanding the fact that the initial transfer was occasioned by a breach of trust.*¹⁰⁸¹ The rights of the trust beneficiary to that property are subordinated to those of the BFP, and to those who take lawfully from the BFP, as the BFP has not been unjustly enriched.¹⁰⁸² The transfer of a specific item of trust property by the trustee to a BFP also cuts off any nonpossessory vested equitable reversionary interest which the settlor may have in that property that could have become possessory upon imposition of a resulting trust.¹⁰⁸³ It also would cut off the rights of anyone who had succeeded to that interest by assignment, on account of the settlor's death, or otherwise.¹⁰⁸⁴ The rights of the beneficiary of a purchase money resulting trust are similarly cut off by a transfer to a BFP.¹⁰⁸⁵

¹⁰⁷⁶See generally 5 Scott & Ascher §29.1.6.1 (Devolution on Death of Trustee); §3.4.3 of this handbook (death of trustee).

¹⁰⁷⁷See generally §§3.3 of this handbook (the constructive trust); 7.2.3.1.6 of this handbook (the constructive trust as a procedural equitable remedy); 4.1.1.1 of this handbook (the resulting trust).

¹⁰⁷⁸See generally §7.2.3.1 of this handbook (tracing and accounting for proceeds and profits).

¹⁰⁷⁹See generally Restatement of Restitution §172 (the defense of bona fide purchase).

¹⁰⁸⁰See generally Scott & Ascher §13.1; Restatement of Restitution §172 (the defense of bona fide purchase).

¹⁰⁸¹See generally 5 Scott & Ascher §29.6.1 (Transferee from Bona Fide Purchaser); Restatement of Restitution §172 (the defense of bona fide purchase). Should the trustee reacquire the property from a BFP, the property will again become subject to the terms of the trust. 5 Scott & Ascher §29.6.2 (Retransfer by Bona Fide Purchaser to Trustee); Restatement of Restitution §176 (retransfer by bona fide purchaser). So too if a prior transferee with notice reacquires the property from a BFP. See generally 5 Scott & Ascher §29.6.3 (Retransfer by Bona Fide Purchaser to Transferee with Notice).

¹⁰⁸²Restatement of Restitution §172 (the defense of bona fide purchase); §8.15.78 of this handbook (unjust enrichment).

¹⁰⁸³See generally 6 Scott & Ascher §40.5 (Transfer by Trustee); §4.1.1.1 of this handbook (the resulting trust and the equitable reversionary interest).

¹⁰⁸⁴Restatement of Restitution §172 (the defense of bona fide purchase).

¹⁰⁸⁵See generally 6 Scott & Ascher §43.13 (Rights of Creditors of Trustee When Beneficiary of Purchase-Money Resulting Trust Is Estopped); §3.3 of this handbook (the purchase-money resulting trust generally); Restatement of Restitution §172 (the defense of bona fide purchase).

Critical elements of the BFP doctrine. For the transferee to be a BFP of property held in an express trust, the transferee must neither have had notice,¹⁰⁸⁶ actual or constructive,¹⁰⁸⁷ of the trustee's breach of trust and must have paid value¹⁰⁸⁸ for the item. And title must have passed.¹⁰⁸⁹ Even the indenture trustee of a corporate trust may pass good title to a BFP.¹⁰⁹⁰ Moreover, nowadays a BFP would have no duty to the trust beneficiaries to see to it that the trustee properly applies the purchase price.¹⁰⁹¹ Since time immemorial, however, it has been the case that if the transferee pays no consideration, he or she takes subject to the express trust. Innocence is no defense. Justice Holmes explained in an 1897 Massachusetts case:

A person to whose hands a trust fund comes by conveyance from the original trustee is chargeable as a trustee in his turn if he takes it without consideration, whether he has notice of the trust or not. This has been settled for 300 years,—since the time of uses. “If the feoffees enfeoff one without consideration it is to the first use although it be without notice.” Y.B. 14 Hen. VIII. p. 9, pl. 5: Chudleigh’s Case, 1 Coke, 120, 122b.¹⁰⁹²

The restitutionary claimant versus the judicial lien creditor. Assume the trustee wrongfully makes off with an identifiable asset of the trust estate, say, an oil painting. A personal creditor of the trustee obtains a judicial lien on the painting. Who prevails, the restitutionary claimant, *i.e.*, the trust beneficiary (the trust) or the judicial lien creditor? “When the question is adjudicated as a matter of common law and equity, unmodified by statute, the answer uniformly given is that a

¹⁰⁸⁶See generally 5 Scott & Ascher §29.1.5 (Transferee with Notice); §8.3.6 of this handbook (negotiable instruments and the duty of third parties to inquire into the trustee's authority); Restatement of Restitution §174 (notice); Restatement (Third) of Restitution and Unjust Enrichment §69 (notice).

¹⁰⁸⁷“A broad definition of notice for these and similar purposes is widely accepted. ‘Notice’ is a legal category that combines actual knowledge with imputed knowledge. While imputed knowledge is described in practice under such various headings as ‘statutory notice,’ ‘record notice,’ ‘constructive notice,’ and ‘inquiry notice,’ or by reference to a person’s ‘duty of inquiry,’ the different labels attach to what is essentially a common idea. In particular circumstances, and for a variety of reasons, the law will treat a person as knowing a fact without requiring that such knowledge be proven directly.” Restatement (Third) of Restitution and Unjust Enrichments §69 cmt. a., illus. 7 & illus.13.

¹⁰⁸⁸5 Scott & Ascher §29.1.6; Restatement of Restitution §173 (value).

¹⁰⁸⁹See generally §5.4.2 of this handbook (rights of the beneficiary as against transferees of the underlying property, including BFPs); Restatement of Restitution §172 (a BFP must have acquired title); Restatement of Restitution §175 (transfer after notice). The trustee also could cut off the rights of the beneficiaries to the item by transferring title to a non-BFP in breach of trust who then transfers the item on to a BFP. The beneficiaries would then have recourse against the non-BFP for the sales proceeds. See generally 5 Scott & Ascher §29.1.4.

¹⁰⁹⁰See generally §9.31 of this handbook (corporate trusts; trusts to secure creditors; the Trust Indenture Act of 1939; protecting bondholders).

¹⁰⁹¹See generally §8.15.69 of this handbook (third-party liability for trustee's misapplication of payments to trustee; the purchaser's duty to monitor the trustee's application of the purchase price).

¹⁰⁹²Otis v. Otis, 167 Mass. 245, 246, 45 N.E. 737 (1897).

judicial lien creditor is not a purchaser for value; so that whereas a bona fide purchaser would indeed take the contested asset free of the ‘equities’ of...restitutionary claimants..., a creditor’s judicial lien can reach only the ‘actual estate’ of the debtor, subject to any adverse claim to which it was subject in the debtor’s hands.”¹⁰⁹³ In other words, the beneficiary (the trust) prevails. The general topic of equitable restitution is taken up in §7.2.3.3 of this handbook.

Trustee takes title to the sale proceeds from the BFP subject to the terms of the trust. In the case of a transfer of entrusted assets to a BFP incident to a breach of trust, the trustee, of course, takes title to the sale proceeds subject to the terms of the trust. Thus, all is not lost as far as the beneficiary is concerned. Moreover, the beneficiary would still have recourse *against the trustee personally* for any residual harm to the equitable interest that had been occasioned by the breach. For coverage of the practical applications of the bona fide purchase doctrine, the reader is referred to §5.4.2 of this handbook and §8.3.2 of this handbook.

The BFP doctrine is a gloss on an equity maxim. The BFP doctrine is actually incident to an equity maxim: Where there is equal equity, the law shall prevail.¹⁰⁹⁴ Why are the equities between the beneficiary and the BFP equal such that equity will decline to wrest the legal title from the transferee and return it to the trustee or his successor? They are equal because each party is innocent.¹⁰⁹⁵ It is self-evident that the trust beneficiary is innocent.¹⁰⁹⁶ The reason the BFP is innocent is because the BFP neither knowingly participated with the trustee in a breach of trust (recall the lack-of-notice requirement) nor was unjustly enriched (recall the payment-of-full-value requirement).¹⁰⁹⁷ The beneficiary's recourse, if any, is a complaint in equity against the trustee-transferor for breach of trust.¹⁰⁹⁸

Whether moneys paid under a mistake of law to an innocent non-BFP need to be returned. At common law, moneys paid under a *mistake of law* to an innocent non-BFP also were not recoverable.¹⁰⁹⁹ In the trust context, when an insolvent trustee of an express trust misdelivered

¹⁰⁹³Restatement of Restitution and Unjust Enrichment §60 cmt. b.

¹⁰⁹⁴*See generally* §8.12 of this handbook (in part containing a catalog of equity maxims); Restatement of Restitution §172 cmt. a (“The question in such cases is which of two innocent persons should suffer a loss which must be borne by one of them.... The principle which is applied by courts of equity is that they will not throw the loss upon a person who has innocently acquired title to property for value.”).

¹⁰⁹⁵Restatement of Restitution §172 cmt. a.

¹⁰⁹⁶Recall that the trustee, not the beneficiary, has the legal title to the underlying trust property, and thus the power to convey. *See generally* §3.5.2.2 of this handbook (right at law to transfer title).

¹⁰⁹⁷*See generally* 5 Scott & Ascher §§29.1.1 (Bona Fide Purchaser), 29.1.6 (Donee); Restatement of Restitution §172 (the BFP not having been unjustly enriched, there would be no grounds for the court to issue a restitution order against the BFP); §8.15.78 of this handbook (unjust enrichment). *See generally* §8.15.78 of this handbook (unjust enrichment).

¹⁰⁹⁸5 Scott & Ascher §29.1.1 (Bona Fide Purchaser).

¹⁰⁹⁹*See generally* W.A. Lee, *Purifying the Dialect of Equity*, 7(2) Tr. Q. Rev. 16–23 (May 2009) [a STEP publication].

trust property to an innocent non-BFP, the beneficiary was out of luck,¹¹⁰⁰ though the non-BFP had been unjustly enriched.¹¹⁰¹ The Restatement of Restitution has never been in accord.¹¹⁰² The injured beneficiary had no recourse against the transferee, although it is not entirely clear why the innocent transferee would not have held the property upon a resulting trust for the benefit of the beneficiary, or, if not innocent, upon a constructive trust.¹¹⁰³ “In one of the most significant changes of direction in private law in the twentieth century the...[general]...rule was overturned in the House of Lords...by way of a lengthy deconstruction of the precedents and academic literature by Lord Goff of Chieveley.”¹¹⁰⁴ In the trust context the rule is being nibbled away by particular exceptions.¹¹⁰⁵ But back to the BFP.

A naked promise of the purchaser or the cancellation of an antecedent debt of the trustee will generally fall short of the BFP doctrine's value requirement. While the naked promise of a purchaser of property to pay the purchase price or the satisfaction (cancellation) of an antecedent (preexisting) debt the transferor owes to the purchaser may be sufficient consideration for an enforceable contract, neither would satisfy the BFP value requirement.¹¹⁰⁶ This holds true in the case of the promise, absent a statute to the contrary or a sufficient change of position on the part

¹¹⁰⁰See, e.g., *Re Diplock* [1948] Ch. 465 (Eng.).

¹¹⁰¹See generally §8.15.78 of this handbook (unjust enrichment).

¹¹⁰²Restatement of Restitution §44.

¹¹⁰³See generally §3.3 of this handbook (the constructive trust); §7.2.3.1.6 of this handbook (the constructive trust as a procedural equitable remedy); §4.1.1.1 of this handbook (the resulting trust).

¹¹⁰⁴W.A. Lee, *Purifying the Dialect of Equity*, 7(2) Tr. Q. Rev. 19 (May 2009) [a STEP publication] (referring to *Kleinwort Benson v. Lincoln CC* [1999] 2 AC 349 (Eng.)).

¹¹⁰⁵See, e.g., *Re Hastings-Bass* [1975] Ch. 25; [1974] 2 WLR 904 (Eng.).

¹¹⁰⁶5 Scott & Ascher §§29.3 (Value), 29.3.5 (Promise as Value) (“For this purpose, then, it would appear that it is not the making but the performance of the promise that constitutes value”). In this regard, see 5 Scott & Ascher §§29.3.2 (Payment of Value Prior to Transfer) (“Since the purchaser has paid value for the property and has already received it, a court of equity will not deprive him or her of it merely because the payment of the purchase price and the transfer of title did not occur simultaneously”), 29.3.3 (Payment of Value After Transfer) (“A transferee of trust property who pays value for the transfer is a bona fide purchaser although he or she pays for the property subsequent to the transfer as long as both the transfer and the payment occur before the transferee has notice that the transfer is in breach of trust”), 29.3.7 (Satisfaction of Antecedent Debt as Value) (“Although the general rule in a majority of the states is that a creditor who receives property in satisfaction of the debt is not a purchaser for value, the rule does not apply to...negotiable instruments or money”). Under general equitable principles, the trust beneficiaries may not compel the innocent transferee to perform in lieu of surrendering the subject property. See generally 5 Scott & Ascher §29.3.5. Were the beneficiaries entitled to elect between performance and surrender, any decline in the value of the subject property would be borne by the innocent transferee and any gain would accrue to the trust beneficiaries. If the value of the subject property were to decline, for example, the beneficiaries would surely elect performance over surrender if permitted to do so, thus enriching themselves at the expense of the innocent transferee.

of the transferee.¹¹⁰⁷ In the case of the antecedent debt, it holds true as well, with some exceptions.

Exceptions to the antecedent-debt-cancellation impediment. Here are some of the exceptions: There was a release of security by the transferee; or the property transferred was a negotiable instrument or money; or there was a sufficient change of position on the part of the transferee.¹¹⁰⁸ When it is trust money that transfers in satisfaction of an antecedent personal debt of the trustee, the innocent personal creditor of the trustee is said to be a bona fide payee.¹¹⁰⁹ The creditor is not “liable in restitution” to the trust beneficiaries, provided the creditor received payment without notice of their equitable claim.¹¹¹⁰ The beneficiaries’ (the trust’s) recourse is only against the trustee.

Thus, if a trustee in breach of trust transfers trust property to an innocent third party who then cancels a debt that the trustee personally owes the third party,¹¹¹¹ the third party is unlikely to be a BFP, unless one of the exceptions enumerated in the prior paragraph applies. This would certainly be the case if the entrusted property were transferred in breach of trust merely as security for the debt, although there are some commercial paper and other statutory exceptions even here.¹¹¹² There are also some equitable exceptions, *e.g.*, if the innocent transferee releases other security or there is a substantial change of the transferee’s position.¹¹¹³ Also, if an innocent third party were to make a secured personal loan to the trustee, the third party might well be a BFP, even if the trustee in breach of trust eventually secures the loan with trust property.¹¹¹⁴ In other words, the third party may hold the subject property as security, provided the third party had no notice of the breach prior to the transfer of the security.¹¹¹⁵ The key here is that we do not have an antecedent or preexisting

¹¹⁰⁷See Restatement of Restitution §173 cmt. e (promise as value); 5 Scott & Ascher §29.3.5 (noting that a land recording statute may provide that a promise to pay for property in the future satisfies the BFP value requirement with respect to a transaction covered by the statute). The Uniform Commercial Code §3-303(a)(4) provides that the purchaser’s own negotiable instrument, *i.e.*, a negotiable instrument under which the purchaser is the promisor, would satisfy the BFP value requirement. See also 5 Scott & Ascher §29.3.5 (promise in form of negotiable instrument). A negotiable instrument held by the purchaser under which a third party is the promisor “unquestionably” would. 5 Scott & Ascher §29.3.5.

¹¹⁰⁸5 Scott & Ascher §29.3.7.

¹¹⁰⁹See Restatement (Third) of Restitution and Unjust Enrichment §67, illus. 3.

¹¹¹⁰See Restatement (Third) of Restitution and Unjust Enrichment §67, illus. 3.

¹¹¹¹See generally §8.3.1 of this handbook (the trustee’s personal creditors and the trustee’s spouse). See also 5 Scott & Ascher §§29.3.9 (Assignee for Creditors) (“When a debtor makes an assignment for the benefit of creditors, the assignee is not a purchaser for value”), 29.3.10 (Trustee in Bankruptcy) (“Indeed, numerous cases have held that the trustee in bankruptcy is not for this purpose a bona fide purchaser and does not take the property of the bankrupt free of equities”).

¹¹¹²5 Scott & Ascher §29.3.8 (Security for Antecedent Debt as Value).

¹¹¹³5 Scott & Ascher §29.3.8.

¹¹¹⁴5 Scott & Ascher §29.3.8.

¹¹¹⁵5 Scott & Ascher §29.3.8.

debt.¹¹¹⁶

What generally qualifies as value in the BFP context. On the other hand, a present assignment to the trustee of enforceable contractual rights which the transferee has against a third person could satisfy the BFP value requirement.¹¹¹⁷ So, too, could the passage of cash, real estate, or tangible personal property, or the rendering of personal services.¹¹¹⁸ If the purchaser makes an enforceable promise to pay a third person in exchange for the entrusted property, that too may satisfy the BFP value requirement: “The purchaser is also protected if he or she has made a promise to a third person on which the purchaser would be liable even if the purchaser were compelled to surrender the property purchased.”¹¹¹⁹

On the other hand, if a transferee has made only partial payment of the purchase price before acquiring notice of the breach of trust, then all the subject property may well have to be returned to the trust estate upon the transferee's getting back the partial payment.¹¹²⁰ Finally, “...[I]f a third person lends money to the trustee personally; and, subsequently, the trustee lends trust funds to the same person, who has no notice that the borrowed funds are trust funds, the third person can set off the two claims.”¹¹²¹

Whether in the BFP context value means fair market value. Value does not necessarily mean fair market value.¹¹²² A BFP is generally entitled to the benefit of the bargain.¹¹²³ A great disparity

¹¹¹⁶5 Scott & Ascher §29.3.8.

¹¹¹⁷5 Scott & Ascher §29.3.1 (Present Value). Assume the transferee owns a bond that has been issued by a corporation. A transfer of the bond to the transferor-trustee is an example of an assignment of contractual rights against a third party, namely the bond issuer. Such an assignment would satisfy the BFP value requirement. *See generally* §9.31 of this handbook (corporate trusts; trusts to secure creditors; the Trust Indenture Act of 1939; protecting bondholders).

¹¹¹⁸5 Scott & Ascher §29.3.1 (Present Value). If in exchange for some entrusted property, say an engagement ring and a wedding ring, the innocent transferee marries the trustee, could the transferee be a BFP such that the equitable rights of the trust beneficiaries to the rings are cut off? Possibly so! *See* 5 Scott & Ascher §29.3.5. Their recourse then would be just against the trustee. A mere promise to marry, however, would not satisfy the BFP value requirement. 5 Scott & Ascher §29.3.5. Thus, if the fiancée acquired actual or constructive knowledge of the breach of trust before the wedding, the rings would have to be returned to the trust estate.

¹¹¹⁹5 Scott & Ascher §29.3.5 (When Purchaser's Promise Is Enforceable).

¹¹²⁰5 Scott & Ascher §29.3.6 (Partial Payment) (citing a few cases where the transferee could keep the property provided the balance of the purchase price was paid into the trust estate).

¹¹²¹5 Scott & Ascher §30.3 (Set-Off of Claim of Third Person Against Trustee). *See generally* §6.2.1.2 of this handbook (duty [of trustee] to segregate and earmark trust property (duty not to commingle)).

¹¹²²Restatement of Restitution §173 cmt. b (“The transfer is for value although the consideration is of less value than the property transferred”).

¹¹²³5 Scott & Ascher §29.3.1 (Present Value).

in value between what the transferee paid for the subject property and what it is actually worth, on the other hand, “may indicate that the purchaser knew or should have known that the transferor was committing a breach of trust or other wrong in making the transfer,” or that that the transferee was actually a donee rather than a purchaser.¹¹²⁴

Consideration versus value. What qualifies as consideration in the contract context will not necessarily qualify as value in the BFP context. Take an innocent transferee’s executory or unperformed promise to a trustee that is made in exchange for wrongfully transferred trust property. “[T]he uniform rule at common law is that an executory promise (secured or unsecured) is not value for purposes of bona fide purchase.”¹¹²⁵ On the other hand, the making of an executory or unperformed promise can give rise to an enforceable contract.

Burdens of proof as between the transferee of entrusted property (the BFP candidate) and the beneficiary. In litigation over whether a transferee of trust property is entitled to BFP status, there is a split of authority on the question of whether the burden of proof is on the transferee to prove that the transferee is a BFP or on the beneficiary to prove that the transferee is not.¹¹²⁶

Whether the transferee of an entrusted chose in action may be a BFP. One can certainly be a BFP of entrusted real property, and of entrusted tangible personal property, as well. As to an entrusted chose in action, the law is not entirely settled. “If the chose in action takes the form of a negotiable instrument, it is, of course, well settled that a holder in due course takes free and clear not only of any trust on which the instrument was previously held, but also of any defense of any party to the instrument,”¹¹²⁷ unless we have an assignment for the benefit of creditors.¹¹²⁸ If the entrusted chose of action is not a negotiable instrument, New York apparently takes the position that *as between the trust beneficiary and the transferee*, the interests of the beneficiary trump those of the transferee, even if the transferee would otherwise qualify as a BFP. Neither the Restatement of Trusts nor the Restatement of Contracts is in accord.¹¹²⁹

BFPs of transferable equitable interests. It seems reasonably settled that equity is as deferential to BFPs of equitable interests as it is to BFPs of legal interests. Thus, the trustee of shares of beneficial interest in a mutual fund, which are essentially equitable interests in another

¹¹²⁴5 Scott & Ascher §29.3.1 (Present Value); Restatement of Restitution §172 cmt. b (present value).

¹¹²⁵Restatement (Third) of Restitution and Unjust Enrichment §68 cmt. e.

¹¹²⁶5 Scott & Ascher §29.1.1.

¹¹²⁷5 Scott & Ascher §29.1.1. *See generally* §8.3.6 of this handbook (negotiable instruments and the duty of third parties to inquire into the trustee's authority) and §8.15.68 of this handbook (holder in due course (trust application)).

¹¹²⁸*See generally* 5 Scott & Ascher §29.3.9 (Assignee for Creditors).

¹¹²⁹Restatement (Second) of Trusts §284 cmt. b & illus. 1; Restatement (Second) of Contracts §343. *See generally* 5 Scott & Ascher §29.1.1 (noting also that “[e]ven in states in which assignees of other choses in action take subject to latent equities, the purchaser of a chose in action represented by a specialty takes free of any trust on which it is held, even if it is not negotiable, if the purchaser gives value and has no notice of the equity”).

trust, has the power to irrevocably convey the shares to a BFP.¹¹³⁰

Equity will not enforce a contract that is the product of a breach of trust if title has yet to pass to a BFP. On the other hand, if a trustee *in breach of trust* enters into a contract with someone who would be a BFP were title to pass, equity will not enforce the contract.¹¹³¹ “A court will not compel a trustee to complete a breach of trust.”¹¹³² The Restatement (Third) of Restitution and Unjust Enrichment is generally in accord.¹¹³³ So too if a trustee obtains nonnegotiable contractual rights fraudulently and purports to transfer them on to a BFP, the BFP may not seek the aid of equity in enforcing those rights.¹¹³⁴ “This is...[also]...an application of the principle that an assignee of a nonnegotiable chose in action takes subject to equitable defenses of the obligor.”¹¹³⁵

Decanting trust property in breach of trust for the benefit of a third party who would otherwise be a BFP. Equity will not permit a trustee in breach of trust to declare himself trustee of the subject property for the benefit of a third party who would otherwise qualify as a BFP. The equitable rights of the trust beneficiaries will trump those of the third party, no matter how innocent the third party may be, unless the beneficiaries by words or conduct have somehow misled the third party into believing that the trustee possessed the authority to bestow on the third party an equitable interest in the subject property.¹¹³⁶ Such behavior on the parts of the beneficiaries would in equity “estop” them from asserting their superior equitable claims.¹¹³⁷ Should the equitable rights of the innocent third party be “cut off” because they are not prior in time, the third party still might be able to recoup from the beneficiaries any expenditures that the third party made to the property to the extent they inured to the benefit of the beneficiaries.¹¹³⁸ If the beneficiaries were not unjustly enriched, only the trustee, then the third party's only recourse would be to seek indemnity from the trustee personally.¹¹³⁹

¹¹³⁰See generally 5 Scott & Ascher §29.1.2 (Conveyance of Equitable Interest).

¹¹³¹5 Scott & Ascher §29.1.2 (Conveyance of Equitable Interest); Restatement of Restitution §175 cmt. a & cmt. b.

¹¹³²5 Scott & Ascher §29.1.2 (Conveyance of Equitable Interest). See generally §5.4.2 of this handbook (rights of the beneficiary as against transferees of the underlying property, including BFPs).

¹¹³³Restatement (Third) of Restitution and Unjust Enrichment §66, illus. 13.

¹¹³⁴5 Scott & Ascher §29.1.2 (Conveyance of Equitable Interest).

¹¹³⁵5 Scott & Ascher §29.1.2.

¹¹³⁶5 Scott & Ascher §29.1.3.

¹¹³⁷5 Scott & Ascher §29.1.3.

¹¹³⁸5 Scott & Ascher §29.1.3.

¹¹³⁹5 Scott & Ascher §29.1.3. The trustee in breach of trust might contract with a third party to sell a parcel of entrusted land. The third party pays the full purchase price to the trustee, who then misappropriates the funds. Title has yet to pass. The contract is unenforceable in equity as it was entered

Multiple assignments of the same trust property. If a *trust beneficiary* first assigns the beneficiary's equitable interest to *X*, a BFP, and then subsequently purports to assign the very same interest to *Y*, who would otherwise qualify as a BFP, *X* being first in time prevails over *Y*.¹¹⁴⁰ “Where the equities are equal, the first in time shall prevail: *qui prior est tempore, potior est jure*.”¹¹⁴¹ Multiple assignments of an equitable interest are not to be confused with the following situation: A trustee not in breach of trust contracts to sell an item of trust property to *X*, who would be a BFP were title to pass, and then subsequently actually does transfer title to the item to *Y*, a BFP. In that case, *X*, though first in time, loses.¹¹⁴² Granted, had title not passed, equity would specifically enforce *X*'s contract, it being first in time.¹¹⁴³

When the transfer by the trustee is incident to an illegal transaction. What if the trustee in breach of trust transfers trust funds to a third party incident to an illegal transaction, *e.g.*, to pay off a personal illegal gambling debt? Can the third party ever be a BFP? Yes. If the third party pays full value, is unaware of the trust, and is unaware “of the circumstances that make the transaction illegal.”¹¹⁴⁴ Otherwise, the third party takes the funds subject to the trust.¹¹⁴⁵

Passage of title to entrusted property incident to murder or divorce. Even one who succeeds to property held in a revocable trust by feloniously and intentionally killing its settlor may pass good title to a BFP, although he or she is deemed to have disclaimed the property.¹¹⁴⁶ Likewise, one who divorces the settlor of a revocable trust and in so doing forfeits any interest he or she may have in the subject property may still pass good title to it to a BFP.¹¹⁴⁷

The public policy underpinnings of the BFP doctrine. The doctrine of bona fide purchase is not just “commercially expedient.”¹¹⁴⁸ Without it, the institution of the trust itself would be a very different one. The ability of a trustee to convey in breach of trust to a BFP is what allows us to say: “The trustee is the owner of the underlying trust property.”¹¹⁴⁹ The inability of the trustee, with some procedural exceptions, to get away with conveying in breach of trust to a non-BFP is

into in breach of trust. Nor is the third party entitled to a lien on the property itself. This is because no benefit accrued to the beneficiaries as a result of the transaction.

¹¹⁴⁰5 Scott & Ascher §29.1.2 (Conveyance of Equitable Interest). *See generally* §5.3.2 of this handbook (voluntary transfers of the equitable (beneficial) interest).

¹¹⁴¹*See generally* §8.12 of this handbook (containing a catalog of equity maxims).

¹¹⁴²5 Scott & Ascher §29.1.3.

¹¹⁴³5 Scott & Ascher §29.1.3.

¹¹⁴⁴5 Scott & Ascher §29.1.7 (Transferee in an Illegal Transaction).

¹¹⁴⁵5 Scott & Ascher §§29.1.7 (Transferee in an Illegal Transaction), 29.1.10 (Extent of Liability of Transferee in an Illegal Transaction).

¹¹⁴⁶UPC §2-803(i).

¹¹⁴⁷UPC §2-804(h).

¹¹⁴⁸Scott & Ascher §13.1.

¹¹⁴⁹*See generally* §3.5.2.2 of this handbook (right at law to transfer title).

what allows us to say: “The beneficiary as well has a proprietary interest in the underlying trust property.”¹¹⁵⁰ It is these overlapping interests in the underlying property of a trust that distinguishes the trust from its contract-based civil law trust analogs on the European continent, South America, and elsewhere.¹¹⁵¹

Cross-references. For coverage of the practical applications of the bona fide purchase doctrine, the reader is referred to §5.4.2 of this handbook and §8.3.2 of this handbook. For a discussion of the differences between the BFP, a creature of equity, and the holder in due course, a creature of law, the reader is referred to §8.3.6 of this handbook and §8.15.68 of this handbook. The impermissible appointee of a special power of appointment may pass good title to a BFP, a topic we take up in §8.15.26 of this handbook. At one time even a good faith purchaser for value might have had an affirmative obligation to see to it that the funds paid to the trustee as consideration for the entrusted asset were properly applied as per the terms of the trust. This is a topic that is taken up in §8.15.69 of this handbook.

¹¹⁵⁰Scott & Ascher §13.1.

¹¹⁵¹*See generally* §8.12.1 of this handbook (civil law alternatives to the trust).