The Mystique Of 'Equitable Subrogation With Respect To Extinguished Common Law Rights': Time For A New Label – 'The Equitable Indemnity Principle'

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After about 300 years of published English jurisprudence, it is fair to say that a settled explanation has been arrived at for most authoritative legal principles. It is only the relevant facts that may determine whether or not an established legal principle will be applied. The reverse is true for equitable subrogation: the factual matrix upon which it will be applied is well settled, being either the request by the Defendant of the Plaintiff or legal compulsion resulting in the Plaintiff having satisfied the Defendant's financial obligation to a creditor. However, this topic is plagued by poor taxonomy, legal fiction, and a fundamental misconception that Institutional Equity has the capacity to revive extinguished common law rights, which has meant that the endeavour to arrive at settled doctrine has not been achieved. Whilst the law remains to settle upon an appropriate name for the principle under discussion, this article is an attempt to dispel some of the myths about the topic and to introduce some sense of doctrinal certainty.

Introduction

The Equitable Indemnity Principle is about a long-established, but doctrinally unsettled principle. In its most fundamental form, P the payer has an entitlement against D the debtor where P at the request of D (or by some form of legal compulsion) satisfies a financial obligation owed by D to D's creditor. Notwithstanding how this matrix may otherwise be described, none of the creditor's rights and obligations play any part in the doctrine that underpins the principle. Whilst the Payer's entitlement is established at the time of satisfaction of the debt, it may not sue until the financial obligation owed by the Debtor to the creditor has been wholly satisfied.

As part of Institutional Equity, the payer's entitlement is personal and, at least on the first instance, the Payer is the Plaintiff and the Debtor is the Defendant, and the Plaintiff sues in its own name.

Whilst the justice of the principle is long-established in English jurisprudence, remarkedly the doctrine in Australia has diverged from that in the UK. Since about 2000, unjust enrichment has been regarded as applying to the UK and unconscionability is the prevailing theory in Australia.

Generally, the law on the topic remains unsettled with the reality being that the law has not even settled on an appropriate name for the principle. Some names include Remedial Subrogation, Legal Subrogation, Equitable Subrogation, Reviving Subrogation, Equitable Subrogation with Respect to Extinguished Common Law Rights, and plain Subrogation. Whilst the common law and Institutional Equity are separate areas of law with the two being mutually exclusive,[1] there prevails in some quarters a misconception that although a Plaintiff may not sue until the creditor has been paid out, the common law rights of the creditor are somehow kept alive after extinguishment for the benefit of the Plaintiff. Metaphors like the

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[1] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269; cf *Boscawen v Bajwa* [1996] 1 WLR 328, 335; *Kation Pty Ltd v Lamru Pty Ltd* (2009) 257 ALR 336, 340–341. See also *Civil Proceedings Act 2011* (Qld), s 7(3).

Plaintiff 'stands in the shoes of the creditor' and that the creditor's rights 'are kept alive', although regarded as legal fiction, were common, particularly before the year 2000.

Whilst there is some doctrinal certainty in that Institutional Equity does not modify or assign rights, it provides a remedial answer [2] and the principle in Institutional Equity under discussion in this article is a remedy of last resort, being availably only where the Plaintiff has no other legal principle on which it may rely.[3] The words of Lord Hoffman in 1999 still ring true today: 'My Lords, the subject of subrogation is bedevilled by problems of terminology and classification which are calculated to cause confusion.'[4]

How then may a Plaintiff know what entitlement they might or might not have when faced with these circumstances? What legal principle may they have resort to, if any, and who do they sue? Do they joint the creditor in the action? Likewise for the Defendant, upon what legal principles may they defend, if any, and do they join the creditor in the action?

The answers to such questions necessarily lie in the law, but the answer to any legal issue necessarily starts with the relevant facts. In matters of complicated legal issues and doctrine, the facts need to be distilled into their simplest possible form to be best understood. This is the case with respect to the Equitable Indemnity Principle: problems with respect to doctrine may not be resolved without first understanding the factual matrix, and the relevant factual matrix must be distilled to its base case so that the doctrine may be applied.

What is the Equitable Indemnity Principle? The Base Case

The base case functions where D the debtor owes a financial obligation to a creditor and where, at the request of D or by legal compulsion,[5] and without any contractual obligation between D and P,[6] P satisfies part or all of the financial obligation owed by D to their creditor. If P assumes an obligation or makes a payment for the benefit of D then, absent a request by D or legal compulsion, D will not be obliged to indemnify P.[7]

So D owes a creditor and P pays out the creditor. D then fails or refuses to return value P. The law finds this unconscionable and P as the Plaintiff sues D as the Defendant. The creditor is not a party to any court action and does not form part of the party matrix. This description is often represented on the basis that the creditor, although its common law rights against D have been extinguished, has some role in the party matrix.[8] This is one of the contributors to confusion of doctrine.

Whilst the entitlement of the payer starts at the time of satisfaction of the debt,[9] the rights of the creditor are paramount and no claim may be brought by P against D until the financial

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[2] *Orakpo v Manson Investments Ltd* [1977] 1 WLR 347, 357; H Bergs, 'Rights, Wrongs and Remedies' (2000) 20 *Oxford Journal of Legal Studies* 1, 16; see also P W Young, C Croft and M L Smith, *On Equity* (Lawbook Co, 2009) 868 for the definition of 'remedy'.

[3] *Butler v Rice* [1910] 2 Ch 277; *Ghana Commercial Bank v Chandiram* [1960] AC 732; *Cochrane v Cochrane* (1985) 3 NSWLR 403, 405; *Barba v De Prima* [2018] NSWSC 601, [52].

[4] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 237 [D]–[E].

[5] *Exhall v Partridge* (1799) 101 ER 1405; *Dawson v Linton* (1822) 5 B & Ald 521, 523; *Brooks Wharf and Bull Wharf Ltd v Goodman Brothers* [1937] 1 KB 534; *Chief Executive, Department of Justice and Attorney General v Hambleton* [2013] QSC 356.

[6] *Coshott v Parker* [2015] NSWSC 998.

[7] *Owen v Tate* [1976] QB 402, 411–412.

[8] Denis S K Ong, *Ong on Subrogation* (Federation Press, 2014) 1.

[9] *Boscawen v Bajwa* [1996] 1 WLR 328, 345.

obligation owed by D to the creditor has been satisfied in full.[10] In Institutional Equity, the rights of P are in personam[11] and the action is brought by P in her or her own name. The law does not appear to explain the rationale behind the principle that P may not bring a claim whilst any balance remains owing to the creditor by D. If that is the case, it may be that if a remedy was granted to P whilst D still owed money to the creditor, then that might adversely affect D's capacity to pay the creditor, thereby diminishing the paramountcy of the creditor's position. What is beyond doubt is that no claim may be brought by P against D until the financial obligation owed by D to the creditor has been extinguished.[12]

The principle arises purely in Institutional Equity, not at common law, in circumstances where P may be obliged to the creditor (as in the surety paradigm) or where P may not be obliged to the creditor.[13] Whilst in the main the principle is applied where the creditor held security over the property of D[14] prior to the satisfaction by P of the financial obligation owed by D to the creditor, the principle may just as appropriately apply to unsecured financial obligations.[15] The test of unconscionability is described in *Boscawen v Bajwa*, when dealing with the claim of a surety, is that 'the equity arises from the conduct of the parties on well settled principles and in defined circumstances which make it unconscionable for the defendant to deny the proprietary interest claimed by the plaintiff.'[16]

The principle will apply whether the payment is made directly by the Payer to the creditor, or by the Payer to the debtor on the basis that the Debtor will then pay the creditor. In such latter circumstances the Plaintiff may need to establish the true nature of the transaction was not a loan.[17]

Once the base case is understood it is then possible to inquire into any conceptual problems that frustrate the endeavour to arrive at a settled doctrine. With respect to the Equitable Indemnity Principle there are many problems to be overcome, thrown up perhaps by the informality of Institutional Equity and its discretionary nature, but nevertheless real problems with respect to the use of metaphor and imprecision of language is endemic.

The Problem and How to Solve It

There appears to be a number of root causes for this dilemma including poor taxonomy,[18] the adoption of no settled view of doctrine over time, the divergence in view as between the law in the UK and Australia,[19] and an absence of a set of base rules. The need for clear doctrine in the interests of coherency in the law should be axiomatic. With respect to the Equitable Indemnity Principle as it applies in the UK, the question of how to achieve coherency was answered to some extent in *Appleyard*[20] which set out a list of principles which can be summarised as follows, borrowing the words used in that case.

[10] *Re Howe; Ex parte Brett* (1871) LR 6 CH App 838, 841; *Duncan, Fox & Co v North & South Wales Bank* (1880) 6 AC 1; *Dixon v Steel* [1901] 2 Ch 602, 607; *Re Octaviar Ltd (No 8)* [2009] QSC 202, [77]–[80].
[11] This is one distinction with true subrogation where a claimant must sue in the name of another party.
[12] R Goode, *Goode on Legal Problems of Credit and Security* (Sweet & Maxwell, 4th ed, 2008).
[13] *Coshott v Parker* [2015] NSWSC 998.
[14] *Highland v Exception Holdings Pty Ltd (in liq)* [2006] NSWCA 318, [91].
[15] See, eg, *Coshott v Parker* [2015] NSWSC 998.
[16] *Boscawen v Bajwa* [1996] 1 WLR 328, 335.
[17] *Paul v Speirway Ltd (in liq)* [1976] 1 WLR 220.
[18] See, eg, the works of Peter Birks.
[19] See, eg, the works of Kit Barker and Ross Grantham.
[20] *Cheltenham & Gloucester Plc v Appleyard* [2004] EWCA Civ 291, [32]–[44].

First, subrogation 'embraces more than a single concept': it is sometimes contractual in nature and it is sometimes based on equity.[21] Secondly, subrogation is a remedy primarily aimed at preventing unjust enrichment.[22] Thirdly, subrogation is a flexible remedy, which nonetheless must be applied in a principled fashion.[23] Fourthly, a classic case of subrogation is where P's money is used to pay out a secured creditor and P is entitled to be regarded in equity as having had an assignment to him of the secured creditor's rights.[24] Fifthly, although the classic case of subrogation involves a lender who expected to receive security (in the proprietary sense – eg a mortgage) claiming subrogation to another security, it can apply to personal rights.[25] Sixthly, the fact that a lender of money gets some security does not prevent him from claiming to be subrogated to another security.[26] Seventhly, a lender cannot claim subrogation if he obtains all the security which he bargained for,[27] or where he has specifically bargained on the basis that he would receive no security.[28] Eighthly, the fact that the lender's failure to obtain the security he bargained for was attributable to his negligence is irrelevant.[29] Ninthly, the absence of a common intention on the part of the borrower and the lender that the lender should have security is by no means fatal to a lender's subsequent claim for subrogation.[30] Tenthly, subrogation cannot be invoked so as to put the lender in a better position than that in which would have been if he had obtained all the rights for which he bargained.[31] Eleventhly, it is difficult, and may be impossible, for a lender who has obtained security to invoke subrogation where the security he has obtained gives him all the rights and remedies of security to which he claims to be subrogated.[32] Twelfthly, the capital sum in respect of which a lender is subrogated cannot normally be greater than the amount of the secured debt that has been discharged.[33] Finally, normal equitable principles apply to subrogated rights.[34]

The courts in Australia are yet to set out an appropriate set of base rules, frustrated perhaps by the reluctance in some quarters to accept Institutional Equity and the Common law as distinct areas of law, each with their own distinct language. Such distinction between terms are, for example, 'right' and 'entitlement', 'damages' and 'equitable compensation', 'lien' and 'equitable charge'.

The well-entrenched problem here is even more fundamental with respect to one word that is at the root of the problem: subrogation. A number of labels are prescribed including Remedial Subrogation, Legal Subrogation, Equitable Subrogation, Reviving Subrogation, Equitable Subrogation with Respect to Extinguished Common Law Rights, and Subrogation being the most common terms. It would be fair to say that the most misleading word is 'Subrogation', meaning a substitution of rights, and not an entitlement.

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[21] *Orakpo v Manson Investments Ltd* [1977] 1 WLR 347; cf *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 231 [G]–[H].
[22] *Orakpo v Manson Investments Ltd* [1977] 1 WLR 347; see also *Boscawen v Bajwa* [1996] 1 WLR 328, 335 (Millett LJ) and *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 231 [G]–[H] (Lord Hoffman), 237 [D]–[E] (Lord Clyde).
[23] *Boscawen v Bajwa* [1996] 1 WLR 328, 338–339 (Millet LJ).
[24] *Burston Finance Ltd v Spierway Ltd* [1974] 1 WLR 1648, 1652 [B] – [D].
[25] *Re Wrexham, Mold and Connah's Quay Railway Co* [1899] 1 Ch 440, 458.
[26] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 241 [C]–[D].
[27] *Burston Finance Ltd v Spierway Ltd* [1974] 1 WLR 1648, applying *Capital Finance Co Ltd v Stokes* [1969] 1 Ch 261.
[28] *Paul v Speirway Ltd (in liq)* [1976] 1 WLR 220.
[29] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 235 [E]–[G].
[30] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 232–234.
[31] *Re Wrexham, Mold and Connah's Quay Railway Co* [1899] 1 Ch 440, 447; *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 235–237.
[32] *Burston Finance Ltd v Spierway Ltd* [1974] 1 WLR 1648, 1653 [D]–[E].
[33] *Halifax Mortgage Services v Muirhead* (1998) 76 P&CR 418, 426; *Orakpo v Manson Investments Ltd* [1977] 1 WLR 347.
[34] *Halifax v Omar* [2002] EWCA Civ 121 [81]–[83].

'Subrogation' – a Principal Source of Confusion

The word 'subrogation' appears to have first found its way into English case law in 1851 in an insurance case, *Quebec Fire Insurance Co,*[35] an appeal to the Privy Council from the courts of the lower French provinces of Canada. The word appears to have first been adopted in an English case, *Stringer v English and Scotch Marine Insurance Co*.[36]

In any attempt to find an appropriate theoretical basis for doctrine, use of the label 'subrogation' is prone to mislead and in fact is seen as a root cause of confusion.[37] 'Subrogation' has a specific meaning,[38] meaning an actual substitution of rights, whereas in the principle under review in this article, no process of substitution of rights occurs a fortiori and, just as importantly, no assignment of rights is possible as no rights exist that may be assigned.[39]

The use of the word 'subrogation' itself is a root cause for confusion where the doctrine operates to grant a remedy in Australia purely upon principles in Institutional Equity, and in the UK in unjust enrichment, though neither by way of a substitution of rights. Actual subrogation functions in circumstances where a person is put, legally, in the place of another,[40] however use of the label 'subrogation' continues to be applied to circumstances notwithstanding that no substitution of rights occurs.[41]

This article has used the term 'D' to refer to the Defendant/Debtor and 'P' to refer to the Plaintiff/Payer. These terms are capitalised, but the term 'creditor' is not, and is not given a shorter label. This is a deliberate choice for this article. Many commentators refer to the debtor 'A', owing a debt to the creditor 'B', who is paid out by a third-party payer 'C'. They then say that 'C' takes over the rights of 'B' against 'A'. This itself is emblematic of the confusion in the law, as this very example presumes that the rights of 'B' are integral to allow 'C' to claim against 'A'.

In fact, in the Equitable Indemnity Principle, there is no substitution of rights, so the rights of 'B' are irrelevant to the entire exercise of legal reasoning. The base case operates where P the Plaintiff/Payer sues D the Defendant/Debtor directly, because they satisfied D's debt to a creditor. The creditor has no role to play, and P is not a third party, as the claim is directly between P and D. As such, this article uses 'D' and 'P' to remove the incorrect assumption that a substitution of rights occurs.

Once the issue with poor taxonomy with respect to the confusion caused by the inappropriate use of the word 'subrogation', other barriers to understanding arise. The first of these is the unusual departure by the law in Australia from settled UK doctrine. The divergence here is the acceptance in the UK of unjust enrichment as the basis for the doctrine and, in Australia, a

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[35] *Quebec Fire Insurance Co v Augustin St Louis and John Molson* (1851) 7 Moo PC 286. See also M L Marasinghe, 'An Historical Introduction to the Doctrine of Subrogation: the Early History of the Doctrine II' (1976) 10(2) *Valparaiso University Law Review* 275, 285.
[36] *Stringer v English and Scotch Marine Insurance Co* (1868-1869) LR 4 QB 676.
[37] Peter Birks, 'Equity in the Modern Law: an Exercise in Taxonomy' (1996) 26 *Western Australia Law Review* 1, 24.
[38] Kit Barker and Ross Grantham, *Unjust Enrichment* (LexisNexis, 2nd ed, 2018) [15.54], *Australian law Dictionary* (Oxford University Press, 2010) 554.
[39] See *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221; *Saraceni v Mentha (No 2)* [2012] WASC 336 [238].
[40] *Macquarie Dictionary "L – Z"* (Macquarie Dictionary Publishers, 8th ed, 2020); Nicholas Leigh-Jones, John Birds and David Owen (eds), *MacGillivray on Insurance Law* (Sweet & Maxwell, 10th ed, 2002) 568.
[41] See, eg, *Cook v Italiano Family Fruit Company Pty Ltd (in liq)* (2010) 190 FCR 474, 499 [109].

rejection of unjust enrichment and the preference for unconscionability as the basis for the doctrine.

A Further Source of Confusion

To deal with the conflict of opinion as between the UK and Australia,[42] the first common element found is that the Plaintiff must show that the Defendant was enriched at the expense of the Plaintiff: however, in the UK the basis for the doctrine is based in unjust enrichment, and in Australia it is based upon principles found in Institutional Equity that it would be unconscionable for the Defendant not to compensate the Plaintiff to the extent of the value of the benefit enjoyed by the Defendant.

It must be said that the UK view has its supports in Australia, and whilst there is no room in this article to argue either view, it seems clear that unjust enrichment has limited application in Australia.[43] In fact, in the relatively recent High Court of Australia decision of *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd,*[44] the High Court said that 'such a 'principle' does not govern the resolution of this case because the concept of unjust enrichment is not the basis of restitutionary relief in Australian law'.

The UK basis for the principle is that a claim in unjust enrichment is a claim for the recovery of a benefit *unjustly gained*[45] and the principle is only available in circumstances where D's financial obligation, to the creditor, is satisfied by a surety under a prior obligation, or upon the request of the debtor, or by legal compulsion. How can an unjust factor be argued logically in these circumstances?

The sources of confusion and the consequent reasons for unsettled doctrine do not stop here. Perhaps a result of poor taxonomy, but more probably as a result of unsettled doctrine, commentators often deal with concepts and principles that underpin subrogation in the common law and principles that underpin the Equitable Indemnity Principle in the same but confusing context when dealing with insurance law. Certainly, a substitution of rights functions in the insurance law context, in exchange for the indemnity owed by the insurer to the insured, but not where the Equitable Indemnity Principle applies, where the indemnity is owed by the Debtor to the Payer.

Another Source of Confusion: the Indemnity in the Insurance Law Contract

Some of the basis for confusion may arise out of the fact that both real subrogation and the equitable indemnity principle share the same heritage in cases like the 1748 case of *Randall v Cockran*[46] and the 1851 case of *Quebec Fire Insurance Co*,[47] both insurance law cases but

[42] Mark Leeming, 'Subrogation, Equity and Unjust Enrichment' in J Glister and P Ridge (eds), *Fault Lines in Equity* (Hart Publishing, 2012) 27.

[43] *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89, 156 [151](Gleeson CJ, Gummow, Callinan, Heydon and Crennan JJ); *Lumbers v W Cook Builders Pty Ltd (in liq)* (2008) 232 CLR 635, 664–665 [83]–[85] (Gummow, Hayne, Crennan and Kiefel JJ); *Friend v Brooker* (2009) 239 CLR 129. See also *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269 echoing scepticism previously expressed, inter alia, in *Highland v Exception Holdings Pty Ltd (in liq)* [2006] NSWCA 318 and *Challenger Managed Investments Ltd v Direct Money Corp* [2003] NSWSC 1072.

[44] *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* (2014) 253 CLR 560.

[45] Charles Mitchell, Paul Mitchell and Stephen Watterson, *Goff & Jones: the Law of Unjust Enrichment* (Sweet & Maxwell, 9th ed, 2016) [4.01] quoting *Boake Allen Ltd v HMRC* [2006] EWCA Civ 25, [175] and *Benedetti v Sawiris* [2013] UKSC 50, [13].

[46] *Randall v Cockran* (1748) 1 Ves Sen 98; 27 ER 916. See also *Blaauwpot v Da Costa* (1758) 1 Ed 130.

[47] *Quebec Fire Insurance Co v Augustin St Louis and John Molson* (1851) 7 Moo PC 286.

preceding the development of the modern insurance contracts where the common law rights and obligations of the parties are clearly set out. Particularly, in the context of this discussion, the insurer indemnifies the insured and the insurer, upon satisfaction of that indemnity, is entitled to step into the legal shows of the insured and to sue in the name of the insured[48] to attempt to recover the value of the indemnity.[49]

The scope of subrogation in the insurance contract was summarised by Mason JA in *Sydney Turf Club v Crowley*[50] 'where an insurer is subrogated to the rights of the insured against a third party, the *insured* does not acquire an independent cause of action in his own right. He succeeds to the insured's cause of action against the third party' (emphasis added). The use of the word 'insured' must have meant to be read 'insurer'.

The locus classicus of 'subrogation' takes place in the insurance contract where a true substitution of rights takes place as described in *Sydney Turf Club v Crowley*[51] when referring to the right of subrogation at common law in the insurance contract 'that right of action remains in all respects unaltered; it is brought in the name of the insured and it is subject to all the defences which would be available if the action had been brought by the insured for his own benefit'.

Barker and Grantham in their text *Unjust Enrichment*[52] describe subrogation as a process whereby 'one party is substituted for another for the purpose of allowing the first party to assert the rights held by the latter party against a third party for his or her own benefit'. Regrettably, Barker and Grantham go on to categorise the Equitable Indemnity Principle as a form of substitution of rights as a process 'where a surety discharges a debtor's secured debts he or she may be entitled to 'take over' the security formerly held by the creditor over the debtor's property'.[53]

Whilst historically subrogation and the Equitable Indemnity Principle had the same heritage as part of Institutional Equity,[54] the development of the insurance contract where the right of subrogation became squarely enshrined in contract law, and therefore as part of the common law, is separate and unrelated to circumstances where a person may claim a right to a remedy, and shows a clear distinction between the two.[55] The Equitable Indemnity Principle is based in Institutional Equity, and not contract.[56]

Of the two elements in this statement, reference to the term 'subrogation' and the reason for the existence of the principle are both readily addressed. The reason that 'subrogation' does not assist with answering the question is that the adoption of that term is highly inappropriate as it is immediately suggestive of, and is manifested in, a process of substation of rights more property labelled 'real subrogation' which functions, for example, in insurance law. No process of substitution of rights occurs in the Equitable Indemnity Principle.

There is no doubt that subrogation in the insurance contract rests upon the common intention of the parties giving effect to an indemnity embodied in the contract;[57] however, this is not the

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48 *The Owners Strata Plan 56587 v TMG Developments Ltd* [2007] NSWCA 1364.
49 *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 231 (Lord Hoffman).
50 *Sydney Turf Club v Crowley* [1971] 1 NSWLR 724, 734.
51 *Sydney Turf Club v Crowley* [1971] 1 NSWLR 724, 734.
52 Kit Barker and Ross Grantham, *Unjust Enrichment* (LexisNexis, 2nd ed, 2018) 648 [15.54].
53 Kit Barker and Ross Grantham, *Unjust Enrichment* (LexisNexis, 2nd ed, 2018) 648 [15.54].
54 Such as in *Randall v Cockran* (1748) 1 Ves Sen 98; 27 ER 916 and Quebec Fire Insurance Co v Augustin St Louis and John Molson (1851) 7 Moo PC 286.
55 Such as in *Drew v Lockett* (1863) 32 Beav 499; 55 ER 196.
56 *Aldrich v Cooper* (1803) 8 Ves 382, 389 (Lord Eldon).
57 *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 231 (Lord Hoffman).

case in the Equitable Indemnity Principle where the principle operates ipso jure (by operation of law).[58]

The Indemnity Theory

In *Duncan, Fox & Co v North & South Wales Bank,*[59] a surety case, the Court held that the Plaintiff's claim 'in no way depends on contract but is the result of the equity of indemnification attendant to the suretyship'.

On the basis that a person, a surety, has agreed to pay another person's financial obligation, the law provides that the other person should indemnify the surety to the extent of the payment (if made).[60] The same applies where a person, at the request of the debtor[61] or by legal compulsion[62] satisfies a financial obligation owed by the debtor to a creditor. The indemnity attaches to the debtor, personally, from the time of payment.

If there is any correlation between the Equitable Indemnity Principle and real subrogation as it applies to insurance law, it is that an indemnity exists in both, but that is where the similarity ceases. The former is part of Institutional Equity, whilst the latter is part of the common law.

The influence of the indemnity in the Equitable Indemnity Principle was confirmed by the High Court in *Bofinger v Kingsway Group Ltd*[63] where the High Court, when restating the positive obligation of the law to fashion the remedy to suit the circumstances[64] and said with respect to the claim to the principle, 'the nature of the present case and the particular facts engage the law respecting sureties, their obligations to indemnify the creditor and the right to indemnity by the principal debtor, and the operation of the doctrine of equity associated with the term 'subrogation'.

However, an historical analysis of the law is not only appropriate, but instructive in the sense that some base principles underpinning doctrine are found in early reported cases and are influential in the modern law. For example, the point made in 1863 in *Drew v Lockett,*[65] that the payer was entitled to the rights the creditor could have had the benefit of, and not the actual rights of the creditor, was applied in *Bofinger v Kingsway Group Ltd*[66] in 2009.

Contributions to Doctrine 1700–1999: the Formative Period in the UK

In the period 1700 to 1999 authoritative statements of doctrine, although somewhat rudimentary early in this period, were evident in cases like *Randall v Cockran* and *Quebec Fire Insurance Co*. In early examples of insurances cases, the Latin phrase 'nemo debet locupletari ex aliena jactura' ('no-one should be enriched by another person's loss') rang true and the payer Plaintiff succeeded upon notions of natural justice, although at the end of this period, some misleading statements of principle have prevailed and the law remained unsettled, as evidenced by Lord Hoffman's statement in *Banque* that 'the subject of

[58] See, eg, M L Marasinghe, 'An Historical Introduction to the Doctrine of Subrogation: the Early History of the Doctrine II' (1976) 10(2) *Valparaiso University Law Review* 275.
[59] *Duncan, Fox & Co v North & South Wales Bank* (1880) 6 AC 1
[60] *Yonge v Reynell* (1852) 9 Hare 809, 818–819; *Duncan, Fox & Co v North & South Wales Bank* (1880) 6 AC 1, 12; *O'Day v Commercial Bank of Australia Ltd* (1933) 50 CLR 200, 223; *Friend v Brooker* (2009) 239 CLR 129, 153 [55].
[61] *Coshott v Parker* [2015] NSWSC 998.
[62] *Chief Executive, Department of Justice and Attorney General v Hambleton* [2013] QSC 356.
[63] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269.
[64] See *Warman International Ltd v Dwyer* (1995) 182 CLR 544, 559.
[65] *Drew v Lockett* (1863) 32 Beav 499; 55 ER 196.
[66] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269.

subrogation is bedevilled by problems of terminology and classification which are calculated to cause confusion'.[67]

Certainly what was achieved in this period was the acceptance that the doctrine was squarely within Institutional Equity, and not arising out of contract and therefore not to be regarded as part of the common law. Other theories posed in this period include that the principle was based upon the maxim that 'equality is equity'.[68]

The principle was also said to function by way of an assignment of rights: that is, by way of an assignment of the creditor's rights to the Plaintiff.[69] A substitution of rights was also said to function and the metaphor that the Plaintiff would 'stand in the place of the creditor' applied, and that where in rem rights were to apply and an interest in property formerly held by the creditor as security for the debt was satisfied by the Plaintiff, the Plaintiff was to be awarded a charge in Institutional Equity over the security formerly held by the creditor. This security was said to be kept alive to the extent that the Plaintiff would 'step into the shoes of the creditor'.[70] Another theory in quasi contract was also advanced.[71]

Such other theories were difficult to justify, and the best the law seemed to do was to say that such other theories operated by some sort of 'legal fiction',[72] which calls into doubt any explanation of doctrine that adopt the metaphors 'standing in the place of the creditor', 'standing in the shoes of the creditor' and 'keeping the security alive'.[73]

In the Australian context, the case of *Drew v Lockett*,[74] a surety case followed by the High Court of Australia in *Bofinger v Kingsway Group Ltd*, referred to the rights of the creditor in the past tense. The language adopted by the High Court was 'the right operates so as to confer on the surety who has paid the debt in full *the rights against the debtor formerly enjoyed by the creditor* or by imposing on the creditor the obligation to account to the surety for any recovery in excess of the full amount of his debt'[75] (emphasis added).

As has already been said, the law in the UK has taken a different approach to an explanation of doctrine than that in Australia. *Boscawen v Bajwa*, *Banque*, and *Appleyard* have been particularly influential in the development of the unjust enrichment theory.

The Position in the UK post-1999

Presently the doctrine appears well-settled in the UK with the firm statement that it is based in unjust enrichment,[76] with the acceptance of a set of rules as set out in *Appleyard*.[77]

Doctrinally, *Boscawen v Bajwa* is somewhat enigmatic and often quoted.[78] It makes a worthwhile contribution in some respects, but not in others. It recognises that causes of action

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[67] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 237 [D]–[E].
[68] *Craythorne v Swinburne* (1807) 14 Ves Jun 160, 162.
[69] *Burston Finance Ltd v Spierway Ltd* [1974] 1 WLR 1648; *Ex parte Crisp* (1744) 1 Atkyns 133; 26 ER 87, 88.
[70] *Re TH Knitwear (Wholesale) Ltd* [1987] 1 Ch 275.
[71] *Orakpo v Manson Investments Ltd* [1978] AC 95, 104.
[72] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 237.
[73] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 237; Robert Goff and Gareth Jones, *The Law of Restitution* (Sweet & Maxwell, 1998) .
[74] *Drew v Lockett* (1863) 32 Beav 499; 55 ER 196.
[75] *Liberty Mutual Insurance Co (UK) Ltd v HSBC Bank Plc* [2001] Lloyd's Rep Bank 224, 225 (Morritt VC).
[76] See *Anfield (UK) Ltd v Bank of Scotland Plc* [2011] 1 WLR 2414.
[77] *Cheltenham & Gloucester Plc v Appleyard* [2004] EWCA Civ 291, [32]–[44].
[78] See, eg, *Commonwealth Bank of Australia v Saleh* [2007] NSWSC 903.

function with respect to different authoritative principles in Institutional Equity[79] and warns about the dangers of the adoption of misleading language,[80] but then goes on to say, when referring to the Equitable Indemnity Principle, 'subrogation, therefore, is a remedy, not a cause of action'.[81] This statement is contradictory and confusing as it ignores the distinction between a cause of action as an essential element to a Plaintiff's claim[82] and the form of order available to the court once the Plaintiff succeeds in its action. The form of order is the remedy, not the authoritative legal principle relied upon by the Plaintiff in its cause of action.

The words 'subrogation, therefore, is a remedy, not a cause of action' might have been better expressed as the Equitable Indemnity Principle provides to the successful Plaintiff a personal remedy in the form of equitable compensation, in an amount not greater than the value of the benefit bestowed upon the Defendant, and where the creditor held property as security for the Defendant's financial obligation owed to the creditor, the Plaintiff is entitled to an equitable charge against that property.[83]

The position in Australian jurisprudence is distinct from that in the UK post-1999, particularly under the guidance of the High Court in *Bofinger* where unconscionability was seen as the influential factor. The High Court has not renounced that view and it will continue to apply in Australia unless positively renounced by the High Court.

The Australian Position post-1999

The law in this period would naturally draw upon principles laid down in the pre-2000 years, however somewhat regrettably, much of the basis for doctrine adopted post-1999 is misguided and misleading. The major source of distraction here is the misconception that Institutional Equity has the capacity to keep alive extinguished common law rights. This misconception is found in the fundamental concept that a Plaintiff will have the benefit of the creditor's rights against the Defendant, notwithstanding that no claim may be brought by the Plaintiff against the Defendant whilst any of the financial obligations owed by the Defendant to the creditor remain unsatisfied.

Once the creditor has been wholly paid out, it is clear that the creditor's rights against the Debtor are satisfied and extinguished. From the perspective of the creditor, in normal circumstances, the creditor is left with certain obligations including the obligation to return any property the creditor held as security for the debt to the Debtor, and to account for any surplus of funds it may hold once the balance of the debt has been satisfied. Institutional Equity does not confer common law rights, nor does it have the capacity to reincarnate extinguished common law rights.[84]

Lord Hoffman in *Banque* alluded to this when he said that metaphors like 'stepping into the shoes of the creditor' and 'keeping the mortgage alive' must be treated with caution as being metaphorical and not amounting to principle.[85] Certainly by 2011 this misconception in English jurisprudence was clearly accepted,[86] but regrettably not always adopted as seen in

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[79] *Boscawen v Bajwa* [1996] 1 WLR 328, 334.
[80] *Boscawen v Bajwa* [1996] 1 WLR 328, 334.
[81] *Boscawen v Bajwa* [1996] 1 WLR 328, 335.
[82] *May v Chidley* [1894] 1 QB 451; *Roberts v Plant* [1895] 1 QB 597. See generally LexisNexis, *Ritchie's Supreme Court Procedure New South Wales*.
[83] Here lies another source of poor taxonomy where the equitable charge is also often referred to as an equitable lien. 'Lien' in common law arises only where a claimant has a right to possession of property, which is not the case in Institutional Equity. See *Hewett v Court* (1983) 149 CLR 639.
[84] H Bergs, 'Rights, Wrongs and Remedies' (2000) 20 *Oxford Journal of Legal Studies* 1, 16.
[85] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 236.
[86] Charles Mitchell, Paul Mitchell and Stephen Watterson, *Goff & Jones: the Law of Unjust Enrichment* (Sweet & Maxwell, 8th ed, 2011) 847 [39.28]. See also Charles Mitchell, Paul Mitchell

Anfield (UK) Ltd v Bank of Scotland Plc[87] where the court said 'a lender who has made advances which have been used to discharge a secured debt owed to another lender may be entitled to step into the shoes of the other lender as far as the security is concerned, thereby gaining priority over intermediate lenders also holding security over the same property'.

The confusion present in the pre-2000 English case of *Boscawen v Bajwa* has seen influence in Australian cases.[88] However, doctrine remains unsettled in Australia, notwithstanding statement to the contrary by the High Court in *Bofinger*,[89] with the influence of the UK position still weighing heavily upon Australian courts.

Even as late as 2006 Australian courts were uncertain as to the basis for the doctrine. In *Highland v Exception Holdings Pty Ltd (in liq)*[90] the court questioned whether the principle was based 'upon notions of restitution to prevent unjust enrichment, or on some broader basis such as the notion of unconscionable conduct or to avoid an inequitable discharge of liability or even on a basis as broad as that which reason and justice demand'.

The only High Court of Australia case on this topic appears to be *Bofinger v Kingsway Group Ltd* in 2009, so naturally any cases followed by *Bofinger* will be referred to, with a number of seminal statements of principle being made or adopted in *Bofinger* including 'the relevant principles of equity do not operate at large and in an idiosyncratic fashion',[91] 'the equity arises from the conduct of the parties on well settled principles and in defined circumstances which make it unconscionable for the defendant to deny the proprietary interest claimed by the plaintiff',[92] and 'the equitable personal remedies include equitable lien or charge or a liability to account'.[93]

Notwithstanding the position in the UK, the High Court of Australia in *Bofinger* confirmed that unjust enrichment does not amount to an authoritative legal principle. Certainly with respect to the Equitable Indemnity Principle, the court said[94] 'the appeal to this Court in *Friend v Brooker*, which concerned the equitable doctrine of contribution, was correctly conducted on the footing that the concept of unjust enrichment was not a principle supplying a sufficient premise for direct application in a particular case. The same is true of the equitable doctrine of subrogation.'

What the Payer asserts, in suing the Debtor, is a personal cause of action in Institutional Equity[95] and will only have merit if it is based on relevant facts and authoritative legal

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and Stephen Watterson, *Goff & Jones: the Law of Unjust Enrichment* (Sweet & Maxwell, 9th ed, 2016) 982 [39.37].

[87] *Anfield (UK) Ltd v Bank of Scotland Plc* [2011] 1 WLR 2414, 2417 [9].

[88] See, eg, *Lerinda Pty Ltd v Laertes Investments Pty Ltd* [2009] QSC 251, [7], followed by *Adams v Zen 28 Pty Ltd* [2010] QSC 36.

[89] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269, 304 [98].

[90] *Highland v Exception Holdings Pty Ltd (in liq)* [2006] NSWCA 318.

[91] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269, 301 [94].

[92] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269, 301 [94] citing *Boscawen v Bajwa* [1996] 1 WLR 328, 335.

[93] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269, 390 [48] citing *Jones v Southall & Bourke Pty Ltd* (2004) 3 ABC (NS) 1, 17.

[94] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269, 299 [85]–[86]. See also *Farah Constructions Pty Ltd v Say-Dee Pty Ltd* (2007) 230 CLR 89, 156 [151]; *Lumbers v Cook* (2008) 232 CLR 635, 664–665 [83]–[85] as referred to in *Hendersons Automotive Technologies Pty Ltd (in liq) v Flaton Management Pty Ltd* [2011] VSCA 167, [57]–[58], also referring to W M C Gummow, 'Moses v Macferlan: 250 years on' (2010) 84 *Australian Law Journal* 756, 759.

[95] As far back as 1882 the principle was seen as arising not 'in privity': H N Sheldon, *The Law of Subrogation* (Boston Book Co, 1st ed, 1882).

principle. Conceptual foundations[96] will not satisfy this requirement and in the context of the Equitable Indemnity Principle, a distinction needs to be drawn between a common law cause of action and a cause of action in Institutional Equity.

As a result of the absence of a clear statement of doctrine, other questions arise with respect to the Equitable Indemnity Principle: for example, whether it is to be more appropriately regarded as a process, like tracing, rather than as a standalone authoritative principle.

Is the Equitable Indemnity Principle a Process?

The short answer is that the Equitable Indemnity Principle is an authoritative legal principle where the Plaintiff asserts an independent cause of action in Institutional Equity and seeks a remedy. It is not a process, as is the case with respect to tracing,[97] which is an exercise in human endeavour.[98]

In *Heperu Pty Ltd v Belle*,[99] Allsop P said ‘tracing has been said to be neither a claim nor a remedy, rather the process by which a claimant demonstrates what has happened to its property, identifies its proceeds and the persons who have handled or received them; and the successful completion of a ‘tracing exercise’ may be a preliminary to the making of a personal or proprietary claim, to the extent such is available’.

It follows that the distinction needs to be drawn between a cause of action and the remedy. The cause of action is made up of the relevant facts and circumstances coupled with an authoritative legal principle, and the remedy being the form of order made by the court where the Plaintiff succeeds in asserting its cause of action. The common law and Institutional Equity are distinct and separate areas of law, and it follows that a common law cause of action and a cause of action in Institutional Equity are separate and distinct and one should not be confused with the other.

Another way to describe the difference might be to draw the distinction between substance and form, with the substance constituted by the cause of action relied upon by the Plaintiff, and the form constituted by the form of order made by the court. However, taxonomically, confusion has arisen where the distinction has not been clearly drawn between substance and form. A prime example of this is found in the words of the court in *Adams v Zen 28 Pty Ltd*[100] where the court said ‘subrogation is a remedy, not a cause of action’.

This assertion appears to be misguided. In simple terms, a remedy is not available in Institutional Equity until a Plaintiff has succeeded in establishing that it has a cause of action recognised at law and that it is entitled to succeed in its asserted cause of action. Only after these prerequisites are met may a court grant a remedy. On the basis that the court has no power to grant a remedy until the Plaintiff asserts a successful cause of action, the statement that ‘subrogation is a remedy, not a cause of action’ is prone to cause confusion as it suggests that all the Plaintiff is required to say is ‘I am entitled to a remedy but I do not need to establish a relevant set of facts nor an established legal principle’.

The position with a process is difference. With a process, the Plaintiff relies on a legal principle with the best example being the principle of tracing in Institutional Equity. Here the Plaintiff does not assert a cause of action, but is required to satisfy the court that the Defendant is a

[96] The maxims in Institutional Equity do not amount to authoritative legal principle.
[97] *Trustee of FC Jones & Son v Jones* [1997] Ch 159, 170 (Millett J).
[98] *Lipkin Gorman v Karpnale Ltd* [1991] 2 AC 548, 573.
[99] *Heperu Pty Ltd v Belle* (2009) 76 NSWLR 230, 252 [89].
[100] *Adams v Zen 28 Pty Ltd* [2010] QSC 36, [7].

fiduciary.[101] Once this threshold question has been answered in favour of the Plaintiff may the Plaintiff then embark on tracing property.

The mischief in the language was repeated in *Boscawen v Bajwa*[102] where the court said 'Equity lawyers speak of a right of subrogation, or of an equity of subrogation, but this merely reflects the fact that it is not a remedy which the court has a general discretion to impose whenever it thinks it just to do so'. The court then further said 'subrogation is a remedy, not a cause of action'.[103]

In making this statement, the court cited in support the fourth edition of *Goff & Jones*[104] which says, when referring to a right of subrogation as referred to by English lawyers, 'it is in essence a remedy, fashioned to the particular facts, and designed to ensure a transfer of rights from one person to another … by operation of law, in order to deprive B (*the Debtor*) of a benefit gained at A's (*the Payer*) expense' (emphasis in brackets added).

This was the position taken earlier in *Re TH Knitwear (Wholesale) Ltd*[105] where the court adopted the words in *Orakpo* in 1978 that subrogation was regarded, for convenience, as functioning by way of 'a transfer of rights from one person to another, without assignment or assent of the person from whom the rights are transferred and which takes place by operation of law'. However, the fourth edition of *Goff & Jones* did not say, as asserted in *Boscawen v Bajwa*, that 'subrogation' is not a cause of action – what it did say was that it is 'in essence a remedy'.

By 1996, Young J in *Re Trivan Pty Ltd*[106] in the Supreme Court of New South Wales said 'the next matter that should be noted about subrogation is that it is not a right, but a remedy, that is, it is a remedy which a court of equity will grant in order to prevent there being an unconscionable situation … Furthermore, it is an equitable remedy. That means that it will not be granted merely as a right, but will only be granted in circumstances where it is appropriate to do so.'[107]

The fifth, sixth, and seventh editions of *Goff & Jones* repeat that the principle is 'in essence a remedy' but go on further to adopt what was said in *Boscawen Bajwa* that the principle is a remedy, and not a cause of action. However, by the time of publication of the eighth edition of *Goff & Jones* in 2011, the authors had dropped the approach that no cause of action applied and acknowledged the requirement that the Plaintiff must establish a sustainable cause of action in Institutional Equity as a prerequisite to the granting of the remedy.[108]

Regrettably, some cases in Australia have not picked up on the distinction between the cause of action as it applies to the principle and the remedy. In *Dimella v Rudaks*,[109] the court repeated the statement in *Boscawen v Bajwa* that the principle is a remedy, not a cause of action.

Another comparison between the assertion of a separate cause of action for the purpose of obtaining a remedy and a process is seen functioning in the insurance law contract. Here the insurer is subrogated to the rights of the insured against a third party, but does not acquire an

[101] *Agip (Africa) Ltd v Jackson* [1991] Ch 547, 566.
[102] *Boscawen v Bajwa* [1996] 1 WLR 328, 335.
[103] *Boscawen v Bajwa* [1996] 1 WLR 328, 335.
[104] Gareth Jones, *Goff & Jones: The Law of Restitution* (Sweet & Maxwell, 4th ed, 1993) 389.
[105] *Re TH Knitwear (Wholesale) Ltd* [1988] 1 Ch 275.
[106] *Re Trivan Pty Ltd* (1996) 134 FLR 368, 372–373 (Young J).
[107] *Re Trivan Pty Ltd* (1996) 134 FLR 368, 372 (Young J).
[108] Charles Mitchell, Paul Mitchell and Stephen Watterson, *Goff & Jones: the Law of Unjust Enrichment* (Sweet & Maxwell, 8th ed, 2011) 840.
[109] *Dimella v Rudaks* (2008) 102 SASR 582, 589–590.

independent cause of action in his own right.[110] Here the insurer exercises its rights at common law, not in Institutional Equity, and subrogation is a process in order for the insurer to sue in the insured's name.

This is not to say that the process of tracing would not be a useful evidentiary tool in proving the source of the payment and the fact that payment reached the creditor to the benefit of the Debtor. Another question arising out of the lack of settled doctrine is what is the purpose of the principle, and why is it necessary?

Purpose

The purpose of the Equitable Indemnity Principle is to avoid the injustice of the Debtor benefitting from the satisfaction of its financial obligations owed to a creditor without being required to indemnify the Payer. The remedy is purely personal, in the form of a monetary award based in equitable compensation and may be proprietary where the remedy takes the form of an equitable charge over the property of the Debtor that was formerly held by the creditor as security for the debt.[111]

Whilst not precisely on point, it is convenient to refer to the assertion by Lord Salmon in *Orakpo* that, upon the relevant facts of each case being considered, the principle is entirely empirical, and that the courts should apply the principle based upon concepts of 'reason and justice'.[112] It follows that the principle is based in an authoritative legal principle, and in no way could be described as a process.

The purpose of the principle is to 'prevent double recovery'.[113] Here exists another example of poor taxonomy causing confusion about the basis for the doctrine. What is meant by these words is that it would be unconscionable for the Debtor to benefit twice, that is, to have the benefit of satisfaction of the Debtor's debt and the benefit of the return of the control of property formerly held as security by the creditor. Unfortunately, the term 'double recovery' appears to have been adopted from common law in the insurance law context.[114]

The principle does afford, where appropriate, not just a personal remedy but also a proprietary remedy in the form of an equitable charge against the proprietary interests in the assets of the Debtor formerly held by the creditor as security for the debt. Such an interest will only relate to proprietary interests over which the creditor held as security of the debt satisfied by the Payer.

The Proprietary Interest Remedy

The remedy available to the successful Plaintiff where the creditor had held security over the property of the Debtor is an equitable charge over the Debtor's interest in that property. The term is a charge, and not a lien or equitable lien. Deane J in *Hewett v Court*[115] described the equitable lien as:

> … a right against property which arises automatically by implication of equity to secure the discharge of an actual or potential indebtedness. Though called a lien, it is, in truth, a form of equitable charge over the subject property in that it does not depend upon possession and may, in general, be enforced in the same way as any

[110] *Sydney Turf Club v Crowley* [1971] 1 NSWLR 724, 734.
[111] *Dixon v Steel* [1901] 2 Ch 602, 607; *Themehelp Ltd v West* [1996] QB 84; [1995] 4 All ER 215; *Filby v Mortgage Express (No 2) Ltd* [2004] EWCA Civ 759.
[112] *Orakpo v Manson Investments Ltd* [1978] AC 95, 110 [D]–[E].
[113] *Ex parte Crisp* (1744) 1 Atkyns 133; 26 ER 87, 88.
[114] See, eg, *Yates v Whyte* (1838) 4 BNC 272; 132 ER 793.
[115] *Hewett v Court* (1983) 149 CLR 639.

> other equitable charge, namely, by sale in pursuance of court order or, where the lien is over a fund, by an order for payment thereout. Equitable lien differs from traditional mortgage in that it does not transfer any title to the property and therefore cannot be enforced by foreclosure. While it arises by implication of some equitable doctrine applicable to the circumstances, its implication can be precluded or qualified by express or implied agreement of the parties. It can exist over land or personalty or both.
>
> Unlike its common law counterpart, the equitable lien does not depend on a transfer of possession to the creditor. Equally significantly, and also unlike the common law lien, the equitable lien confers on the lienee, via the intermediary of the court, the power to obtain an order for sale in the event of the debtor's default.

The knowledge by the Plaintiff of what property is held by the creditor as security, at the time the Plaintiff confers the benefit upon the Defendant, is not a requirement to the entitlement of the Plaintiff.[116]

Institutional Equity does not have the capacity to confer upon a Plaintiff common law rights that have been extinguished. In the context of the Equitable Indemnity Principle, the creditor's common law rights against the Debtor must be extinguished before the Plaintiff may sue.

The Great Misconception

The misconception that Institutional Equity has the capacity to and does reinstate extinguished common law rights by way of presumed intention of the parties has developed as an urban myth in Australian jurisprudence. Many lower courts have peddled the law as laid down in *Boscawen v Bajwa* where it was said, when dealing with a situation where monies had been paid in a conveyancing transaction, to a mortgagee 'Halifax', contrary to the interests of the principal 'Abbey National' to which the money belonged: 'their intention must be taken to have been to keep alive Halifax's charge for the benefit of Abbey National pending completion. In my judgement this is sufficient to bring the doctrine of subrogation into play.' With respect, the imputation of intention where no such intention was ever expressed is not permissible in Australian law.[117]

Whilst the writers in *Goff & Jones* did not point out the misconception until 2011, the law on the point was settled in the UK in 1999 in *Banque* where Lord Hoffman said 'it is a mistake to regard the availability of subrogation as a remedy to prevent unjust enrichment as turning entirely upon the question of intention, whether common or unilateral. Such an analysis has inevitably to be propped up by presumptions which can verge upon outright fictions'.[118]

It can be seen that the law on the topic in the UK, by the time of Lord Hoffman's speech in *Banque*, was that the principle was based in unjust enrichment and not upon any of the previous theories like 'presumed intention'. The law in the UK, as it was then and is now, is summarised in *Appleyard* as previously discussed earlier in this article. The acceptance in the UK of the unjust enrichment theory not only obviated the need to resort to the presumed intention theory, but has clearly stated that privity has no application. Lord Hoffman said, when referring to the doctrine underpinning the principle in *Banque*, that it was 'an equitable remedy to reverse or prevent unjust enrichment which is not based upon any agreement or common intention of the party enriched and the party deprived'.[119]

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[116] *Newton v Chorlton* (1853) 10 Hare 646.
[117] *Muschinski v Dodds* (1985) 160 CLR 583, 595 (Gibbs CJ); *Roxborough v Rothmans of Pall Mall Australia Ltd* (2001) 208 CLR 516, 576–577 [162]–[164].
[118] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 234.
[119] *Banque Financière De La Cité v Parc (Battersea) Ltd* [1999] 1 AC 221, 231.

The law in the UK no longer adopts presumptions with respect to the parties' intentions and the misconception that extinguished common la rights are kept alive for the benefit of the Payer, with *Banque* remaining good law in the UK.[120]

However, as mentioned earlier, the courts in Australia have not accepted unjust enrichment as a basis for doctrine,[121] although the misconception that common law rights are somehow kept alive for the benefit of the Payer remains. In this regard it would be easy to say 'but the High Court in *Bofinger* followed the surety case of *Drew v Lockett* which found that a surety who pays out a debt is entitled to the benefit of the creditor's rights against the Debtor', but the language in *Drew v Lockett* needs careful analysis. The court referred to the rights of the creditor in the past tense:[122] 'I am of opinion that a surety who pays off the debt for which he became surety must be entitled to all the equities which the creditor, whose debts he paid off, *could have enforced*, not merely against the principal debtor, but also as against all persons claiming under him' (emphasis added).

Contrary to the interests of coherence and the laying down of settled doctrine in Australia, the courts continue to languish in the old metaphors and in the misconception that somehow the rights of the creditor, although extinguished once the Debtor's financial obligation is satisfied in full, remain available to the Payer by way of assignment, substitution, or some form of transfer.

In 2006, the New South Wales Court of Appeal in *Highland v Exception Holdings Pty Ltd (in liq)*[123] regarded the basis for the doctrine as unsettled and was uncertain as to its doctrinal foundation, whether based in unjust enrichment or as a response to notions of unconscionability.

In 2010, the Federal Court of Australia in *Cook; re Italiano Family Fruit Company Pty Ltd (in liq)*[124] regarded that two intentions on the part of the Plaintiff must have been present; the first that the monies paid were paid with the intention to pay the creditor, and the second the intention to obtain the benefit of the security held by the creditor. These two elements are mutually exclusive, with the second having no application as a necessary element to the Plaintiff's cause of action.[125]

In the matter of *Re Dalma No 1 Pty Ltd (in liq),*[126] the court found it difficult to disregard the relevance of the 'presumed intention' of the Plaintiff, but only based on the fact that it had been 'mentioned' on 'many occasions' in the past. The court did not go so far as to reject it, so it remained as a necessary element.

The dominant modern theory is that the doctrine is based in unconscionability. It is not that the enrichment is unconscionable, but that it would be unconscionable for the Debtor to deny the entitlement of the Payer to recover from the Debtor the value of the benefit received by the Debtor.

The Reverse Application of Unconscionability

Traditionally, it has been unconscionable acts that Institutional Equity seeks to address and reverse, particularly where the Plaintiff had been under a special disability placing the Plaintiff

[120] *Cheltenham & Gloucester Plc v Appleyard* [2004] EWCA Civ 291; *Anfield (UK) Ltd v Bank of Scotland Plc* [2011] 1 WLR 2414.
[121] *Challenger Managed Investments Ltd v Direct Money Corp Pty Ltd* [2003] NSWSC 1072, [50].
[122] *Drew v Lockett* (1863) 32 Beav 499; 55 ER 196, 198.
[123] *Highland v Exception Holdings Pty Ltd (in liq)* [2006] NSWCA 318, [94], [111].
[124] *Cook; re Italiano Family Fruit Company Pty Ltd (in liq)* [2010] FCA 1355, [90].
[125] See *Coshott v Parker* [2015] NSWSC 998.
[126] *Re Dalma No 1 Pty Ltd (in liq)* [2013] NSWSC 1335, [32].

in the circumstances in a position of inequality, as opposed to the relative position of influence of the Defendant and the Defendant, having been aware of the relative position of inequality, has taken advantage of the Plaintiff to the Defendant's benefit.[127]

The doctrine in the Equitable Indemnity Principle does not operate in relation to the relative positions of strength of the Payer and the Debtor, but it does function on the basis that it would, in the circumstances, be unconscionable that the Debtor does not compensate the Payer. Here, 'compensate' is used in its ordinary and lay meaning. The remedy available to the Plaintiff is, once the Plaintiff has established a sustainable cause of action against the Defendant founded in its personal claim,[128] entitled to a monetary award as part of the law of equitable compensation.

Although time and space in an article of this size may only deal with the topic in a very introductory manner, it would be incomplete to not deal further with *Bofinger*, the only High Court case in Australia to deal specifically with the topic.

The proprietary remedy awarded in *Bofinger* was in the nature of an equitable charge over personal property, in the form of monies held in a solicitor's trust account. The money was held by the solicitors following the creation of surplus funds after a first mortgagee had exercised its power for sale that the first mortgagee held as security and was paid to the solicitors who were acting for the second mortgagee.

In short, the facts were that a private company, of which the Plaintiffs were the directors and shareholders, embarked on an endeavour to redevelop land in New South Wales as home units. The company sourced funding privately in the form of a number of non-institutional lenders, facilitated by a firm of solicitors.

So far as is relevant, a first and second mortgage were registered against the company's title to the land. The Plaintiffs, as sureties, executed guarantees to better secure the repayment of the debt by the company to the first and second registered mortgages. In the guarantee given in favour of the first mortgagee, the Plaintiff did not forgo an entitlement to make a claim in Institutional Equity, although they did do so in the guarantee given by t hem in favour of the second mortgagee.

During the course of the redevelopment, the company fell into arrears in its payment obligations to the first mortgagee and the first mortgagee called upon the guarantee by the Plaintiffs. The Plaintiffs sold the land given to better secure their obligations under the guarantee and from that satisfied the call made by the first mortgagee. However, as the project neared completion to the point where construction of the home units was complete and title had registered to the home units, the company again failed to meet its financial obligations to the first mortgagee and the first mortgagee exercised its power of sale with respect to at least some of the home units. A surplus of funds was generated after the debt to the first mortgagee was wholly satisfied.

The first mortgagee, relying on what it saw as its obligations under the priority of payment legislation, paid the surplus to the second mortgagee by paying the monies to the solicitors for the second mortgagee.

Applying the principles in *Drew v Lockett*[129] and *Charles v Jones*,[130] the High Court found that the first mortgagee was a constructive trustee with respect to the surplus funds and that it

[127] *Louth v Diprose* (1992) 175 CLR 621, 637.
[128] Whilst Institutional Equity acts in personam, such in personam rights may be assignable. See *Barber v De Prima* [2018] NSWSC 601.
[129] *Drew v Lockett* (1863) 32 Beav 499, 505–506; 55 ER 196, 198.
[130] *Charles v Jones* (1887) 35 Ch D 544, 544–550.

should compensate the Plaintiffs with respect to the funds paid to the second mortgagee. The nature of the Plaintiff's claim was found to be based in an indemnity owed to the Plaintiffs by the debtor company,[131] and the attendant functioning of 'the doctrine of equity associated with the term 'subrogation'' and consequently the first mortgagee was ultimately liable to the Plaintiffs.[132]

Conclusion

In the end, whether or not the principle applies in the UK or in Australia on different bases, the doctrine fundamentally rests upon a desire to effect a fair and just balance between the rights and interests of the parties concerned.[133] It is based on the positive obligation of the courts to fashion a remedy as suits the circumstances[134] and, provided the Plaintiff succeeds to a personal claim then Institutional Equity will, where the Plaintiff asks for it, grant a proprietary remedy in the form of an equitable charge over the proprietary interest formerly the subject of security taken by the creditor.

Real subrogation has no business being mixed up in an explanation of the doctrine that underpins the Equitable Indemnity Principle, as no actual substitution exists. The Equitable Indemnity Principle concerns purely a claim by P against D and the creditor is not relevant to that action. Perhaps the desire to effect a fair and just balance may be best achieved by applying the rest of what remedy will be, in the circumstances, just and equitable.[135]

In the end, the objective of a search for doctrine is to find and define the elements that constitute a legal principle that best applies to a particular set of facts or range of facts. Doctrine will always be in a state of flux as new sets of facts may arise over time, hence the words of the High Court of Australia in *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd*[136] that 'coherent legal principle should never be elevated to all-embracing legal theory'. The reverse is also true: all-embracing legal theory does not amount to authoritative legal principle.

The irony of Institutional Equity is that a cause of action may not be conceptually based but must be based in recognised legal principle: but authoritative legal principles in Institutional Equity are developed from concepts and sets of rules. The latter being the 'maxims' of Institutional Equity, and the former the concepts of equality, reason, justice and the law.[137]

Whilst over time a number of theories have been advanced as to the basis for the doctrine underpinning the Equitable Indemnity Principle, including those particularly based on fictions such as an assumption of presumed intention and that extinguished common law rights may somehow be assigned after being extinguished, the most persuasive theory is found in the test of the conscience of the debtor.

In the same way that Institutional Equity is not a tool available in the interpretation of legislation and does not have the capacity to vary a statute, it is not a tool available to the courts to modify agreed contractual terms or to reincarnate extinguished common law rights. It is

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[131] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269, 279.
[132] *Bofinger v Kingsway Group Ltd* (2009) 239 CLR 269, 280, [8].
[133] Robert Goff and Gareth Jones, *Goff & Jones: the Law of Restitution* (Sweet & Maxwell, 6th ed, 2002) [3.003].
[134] *Boscawen v Bajwa* [1996] 1 WLR 328, 334.
[135] 'Just and equitable' was seen as the basis for doctrine in the UK, certainly until the seventh edition of *Goff and Jones*.
[136] *Australian Financial Services and Leasing Pty Ltd v Hills Industries Ltd* (2014) 253 CLR 560, 618 [139].
[137] *Albion Insurance Co Ltd v Government Insurance Office (NSW)* (1969) 121, CLR 342, 351 (Kitto J).

time for a fresh look at the Equitable Indemnity Principle and to state a set of base rules, not according to any legal fiction, but based upon the fact that the Payer has a personal remedy against the Debtor when the Payer has paid out the Debtor's creditor, either at the request of the Debtor or by legal compulsion.

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REVIEW