Wilberforce Lisbon Conference: Gamechangers

<u>Proprietary remedies *(Workshop session – problem)*</u>

Tiffany Scott QC and Daniel Petrides

Macbeth is a fraudster. He lives in the historic Glamis Castle (which in November 2020 had an estimated value of £1.25m) with his wife Lady Macbeth. The castle was purchased in 2010 by way of a mortgage and is registered in the sole name of Lady Macbeth, who denies knowing anything about her husband's fraudulent activities. There are two charges registered against the property:

- The Royal Bank of Scotland has, since 2019, had a legal charge registered against the property securing a re-mortgage of which £400,000 remains outstanding ("**the RBS Charge**");

- In 2020, Lady Macbeth consented to the execution of a charge in favour of Clydesdale Bank to secure Macbeth's indebtedness of £350,000 to Clydesdale (arising from a failed whisky venture) ("**the Clydesdale Charge**");

In early 2022, Macbeth committed the following frauds:

- In January 2022 Macbeth tricked his gullible friend, Duncan, into entering into a sale and leaseback of his home, Stirling Castle. Before the completion of the transaction, Macbeth mortgaged the property for £1m. The property was subsequently repossessed when Macbeth defaulted on the mortgage repayments.

- In February 2022, Macbeth persuaded another gullible friend, Banquo, to invest in his (fictitious) plans to establish a new golf resort in the Scottish Highlands. The resort was to consist of a golf course and luxury hotel constructed in Burnham Wood, the freehold title to which would be acquired by Burnham Wood Ltd, a company wholly owned and controlled by Macbeth. After much persuading by Macbeth:

    - Banquo personally transferred £400,000 to Macbeth for the purpose of the project;

    - Banquo's company, Ghost At The Feast Ltd, agreed to release a charge in its favour over a different property which Burnham Wood Ltd wished to sell in order to release funds for the purchase, in return for taking a registered charge over the land. Unbeknownst to Ghost At The Feast Ltd, Burnham Wood Ltd in fact only executed the charge over a small strip of the land.

- In March 2022, Macbeth accepted a £75,000 bribe to host a Proclaimers reunion gig at a historic property in Edinburgh which he holds on trust for another friend, Macduff. The event caused £50,000 in damage to the property.

Banquo, Duncan and Macduff issue (separate) proceedings against Macbeth in April 2022, and all obtain judgment against him.

Duncan

Duncan obtains judgment against Macbeth for deceit, coupled with a declaration that Macbeth holds the £1m on constructive trust.

At an examination about his assets under CPR 71, Macbeth reveals the following information about how he spent the £1m:

- £750,000 was paid into a bank account with Royal Bank of Scotland in Macbeth's sole name. Thereafter:
    - Macbeth transferred £65,000 to Lady Macbeth's account, which already contained £10,000. The balance of the account has since fallen to £50,000 after Macbeth and Lady Macbeth hosted a lavish Romeo and Juliet themed party for their 25th wedding anniversary.
    - £300,000 was paid into another account in Macbeth's sole name with RBS. Macbeth has continued to pay money in and out of the account – the balance is now £200,000, but at one time is dipped to £90,000.
    - Macbeth spent £210,000 on three bothies (each costing £70,000) near Inverness:
        - Macbeth immediately executed a conveyance purporting to transfer one of the bothies ("**the First Bothy**") to his nephew, Macbeth Jr. Macbeth Jr. immediately mortgages the First Bothy with Lloyd's Bank for £20,000. During his examination, Macbeth produces a letter from Macbeth Jr. which says "*of course, you still own the property and we just signed that document with all the legal jargon on it so that I could trick the bank into giving me that loan*".
        - Macbeth settled another of the bothies ("**the Second Bothy**") on a discretionary trust (to be administered by a firm of professional trustees). However, the trust instrument reserves extensive powers to Macbeth,

including a power of revocation, the trustees are accustomed to acting on his instructions.

- The final bothy ("**the Third Bothy**") is transferred to a newly incorporated company, Bothy Holdings Ltd, and used the property to store his large collection of antique ceremonial daggers.

- £100,000 was used to repay a firm of construction workers who had installed a moat and drawbridge at Glamis Castle in December 2021. A reputable surveyor has advised that this increased the value of the property to £1.5m (so an increase of £250,000).

- £50,000 was used to pay off the outstanding premiums on a life insurance policy with Scottish Widows (£100,000 already having been paid). The policy is worth £1.5m and Lady Macbeth is the sole named beneficiary; however, Macbeth has a contractual power to call for payment of the surrender value of the policy (which is £300,000) at any time.

- £200,000 was used to acquire a long leasehold interest in an office in Edinburgh. This was then sold – again, for £200,000 – to Macbeth's financial advisors, Weird Sisters LLP who were aware of (but not involved in) Macbeth's fraudulent schemes at the time. The £200,000 which Macbeth received for the sale has been dissipated, and the value of the lease has increased to £225,000.

Banquo

Banquo obtains judgment against Macbeth for (i) deceit and (ii) breach of trust. During the proceedings, it transpires that Macbeth spent the £400,000 which Banquo transferred to him in discharging the First RBS Charge against Glamis Castle.

Disclosure also reveals that after the sale of Burnham Wood Ltd's previous land, Macbeth took out a director's loan of £350,000 which he immediately used to pay off the Clydesdale Charge. It is also reveals that Burnham Wood Ltd has numerous other (unsecured) creditors.

Macduff

Macduff obtains judgment against Macbeth for breach of trust and an order for an account of profits coupled with ancillary relief. Following the taking of the account, Macduff obtains a declaration that the £75,000 is held on constructive trust and an order for equitable compensation in respect of £50,000 in damage to the trust property.

Macbeth revealed during cross-examination at the trial that the £75,000 was spent purchasing a property on the Isle of Bute where Macbeth's mistress, Hecate, now resides. The property was initially registered in Macbeth's sole name however, the day after Macduff served the proceedings on Macbeth, he transferred his entire interest to Hecate for £100.

Other events

Another friend, Malcolm, is intending to sue Macbeth for breach of contract and believes that he has a very strong claim. HMRC is also pursuing a bankruptcy petition against Macbeth in respect of £125,000 in unpaid taxes.

Questions

For the purpose of answering these questions, assume that Scottish law is identical to the law of England and Wales following the passage of the Scottish Law of Property Act 2022.

1. What is the size of Macbeth's (soon to be insolvent) estate? Specifically, what interest does he have in:
    a. Glamis Castle?
    b. The bothies?
    c. The Isle of Bute property?
2. Clearly, Banquo, Duncan and Macduff will all want to 'trace' the proceeds of the fraud – what are the rules of 'tracing'?
3. Can Duncan trace the sums that passed through the bank accounts? Specifically:
    a. The sums in Lady Macbeth's account?
    b. The sums in Macbeth's (second) account?
    c. The bothies?
    d. The increase in the value of Glamis Castle attributable to the building works?
4. How might Duncan be able to enforce against the life insurance policy? Would the answer be different if Macbeth had instead acquired an option over land?

5. Can Duncan trace into the property transferred to Weird Sisters LLP? Would the answer be different if Macbeth had purchased (and still retained) property situated in Ruritania (which does not recognise the concept of beneficial ownership)?

6. How should Banquo and Ghost At The Feast Ltd go about recovering the sums used to discharge:

    a. The First RBS Charge?

    b. The Clydesdale Charge?

7. Can Macduff take possession of the Isle of Bute property?

8. What enforcement steps should Macbeth's various creditors take?

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Proprietary remedies *(Workshop session – answer guide*)

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Introduction

While much of the hard work in litigation often focuses on proving/disproving the existence of a cause of action, the question which is frequently of most concern to clients is that of remedies. It is, after all, only at the remedial stage that it will be decided what (if anything) the parties to the litigation will be able to recover/be liable to hand over. At this stage, the existence (or otherwise) of a proprietary interest will often be of paramount importance.

This is particularly so where the wrongdoer has become insolvent. This is because, while the insolvent estate will be distributed amongst creditors on a *pari passu* basis (subject to a limited range of statutory priorities), it is a fundamental requirement that the assets being distributed in any insolvency are actually those of the debtor; under s.283(3)(a) of the Insolvency Act 1986 any "*property held by the bankrupt on trust for any other person*" is excluded from the estate.[1] As Maitland memorably put it, '*Courts of Equity…have thought a great deal of the cestui que trust, much less of creditors*'.[2]

Even in non-insolvency situations, there are further advantages of establishing the existence of a proprietary interest, including the fact that claims may be available against subsequent recipients of the property (thereby expanding the class of potential defendants, and the pool of assets for enforcement) and the possibility that a claimant may be able to take the benefit of any increase in the property's value. The authorities also suggest that certain interim remedies – such as a freezing injunction – may be more readily available and subject to stricter terms where a proprietary interest can be established.[3]

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[1] "A *question may arise as to whether a particular asset was or was not the beneficial property of the* [insolvent] *company...If it is established in a dispute that it is not an asset of the company then it never becomes subject to the statutory insolvency scheme...*": as per Mummery LJ in *Re Polly Peck International Plc (in liquidation) (No 2)* [1998] 3 All ER 812.

[2] Maitland, *Equity* (Cambridge, 1936), p. 221

[3] See e.g. *Republic of Haiti v Duvalier* [1990] 1 QB 202 at 213-214 as per Staughton LJ: "*It may be that the powers of the court are wider, and certainly discretion is more readily exercised, if a plaintiff's claim is what is called a tracing claim. For my part, I think that the true distinction lies between a proprietary claim on the one hand, and a claim which seeks only a money judgment on the other. A proprietary claim is one by which the plaintiff seeks the return of chattels or land which are his property, or claims that a specified debt is owed by a third party to him and not to the defendant. Thus far there is no difficulty. A plaintiff who seeks to enforce a claim of that kind will more readily be afforded interim remedies, in order to preserve the asset which he is seeking to recover, than one who merely seeks a judgment for debt or damages.*"

This problem seeks to unpack a complex web of fraud in which there will, inevitably, not be enough to go around. It seeks to explore different types of proprietary interests which may arise, the ways in which these may be acquired, and how they interact with one another.

Question 1

Before going any further, it is helpful to understand what the size of Macbeth's (soon to be insolvent) estate is likely to be. While some of the assets – such as the money held in the bank accounts – are clearly identifiable as his, the position is more complex in respect of some of the other assets.

Glamis Castle

The starting point is, of course, that Lady Macbeth is the sole registered proprietor of Glamis Castle. There is therefore a rebuttable presumption that she also owns 100% of the beneficial interest. Furthermore, if (as she claims) Lady Macbeth knew nothing of her husband's nefarious activities, her interest in the property ought to be immune to attack by Macbeth's victims: she would not be a dishonest assistant or knowing recipient.

As such, in order to enforce against Glamis Castle, Macbeth's creditors would need to be able to point to an interest which *he* owns in the property.

While he lacks any legal title, it may be arguable that Macbeth has a beneficial interest. The presumption that equity follows the law is rebuttable and, as is trite law, following the decisions of the Supreme Court and House of Lords in *Jones v Kernott* [2011] UKSC 53 and *Stack v Dowden* [2007] UKHL 17 the courts may infer that the parties' common intention was that the beneficial interest in the property was to be held in different shares to the legal title. Furthermore, this may be based not only on direct financial contributions to the purchase price (as had been the case since the decision of the House of Lords in *Lloyds Bank Plc v Rosset* [1991] 1 A.C. 107), but also the parties' "*entire course of conduct*".[4]

It has been suggested that the approach outlined in *Jones* and *Stack* will only apply in cases where the legal title is registered in the joint names of the parties, and that in cases where the legal title was registered in the sole name of one, only contributions to the purchase price can be taken into account: see for example *Culliford v Thorpe* [2018] EWHC 426 (Ch) at [50] (as per HHJ Paul Matthews). However, this argument was rejected by Nugee J in *Amin v Amin (Deceased)* [2020] EWHC 2675 (Ch).

[4] Cf. *Marr v Collie* [2017] UKPC 17 in which it was suggested that the *ratios* of *Jones* and *Stack* may apply equally in cases concerning commercial property.

Furthermore, in *O'Neill v Holland* [2020] EWCA Civ 1583 the Court of Appeal took wider considerations into account in finding that a co-habiting partner without legal title had a 50% beneficial interest in the property. We therefore prefer the view that in the present case the court could have regard to a wide range of both financial and non-financial factors.

The enquiry in any given case will, of course, always be highly fact-sensitive. In the present case what we can say is that it seems likely that Macbeth contributed to the repayment of the original mortgage as well as the upkeep of the property; there may also be other non-financial matters about their relationship which would come to light in evidence from which a post-*Stack* court would be prepared to infer an intention that Macbeth should have an interest. For simplicity's sake, we will assume that a court would find that he had a 50% beneficial interest in the property, worth (following the improvements) £750,000.

The Bothies

Macbeth has purported to divest himself of both the legal and beneficial title to the bothies.[5] *Prima facie*, they would therefore sit outside his estate.

However, in recent years, the courts have become increasingly circumspect about attempts to disguise the true ownership of property. As Toulson LJ pointed out in *R v Richards* [2008] EWCA Crim 1841 at [21]:

> "…*No self-respecting organised criminal would expect to be caught with high-value property in his own name readily identifiable…As a matter of standard practice he is likely to have taken steps to transfer high-value assets to nominee companies, offshore trusts or trusted associates who can be looked upon to harbour the assets until such time as he perceives that the danger has passed*."

As a result, Macbeth's creditors would be well-advised to seek to challenge the purported dispositions of the bothies.

The First Bothy

In respect of the First Bothy, the strongest argument would appear to be that the purported conveyance to Macbeth Jr was a sham.

[5] As a mere discretionary beneficiary of the trust, Macbeth has no proprietary interest in the trust assets: see e.g. *JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev* [2015] EWCA Civ 139 at [13].

The classic definition of a 'sham' transaction was provided by Lord Diplock in *Snook v London and West Riding Investments* [1967] 2QB 786 at 802:

> "*if it has any meaning in law, it means acts done or documents executed by the parties to the "sham" which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create. But one thing, I think, is clear in legal principle, morality and the authorities … that for acts or documents to be a "sham," with whatever legal consequences follow from this, all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating.*"

In *National Westminster Bank plc v Jones* [2001] 1 BCLC 98, Neuberger J considered the applicability of the principle in the context of a series of purported property transfers between the members of a farming family trying to defeat efforts by a bank to sell the property in question. It was emphasised that mere artificiality is not sufficient; instead

> "*the whole point of a sham provision or agreement is that the parties intend to give the impression that they are agreeing that which is stated in the provision or agreement, while in fact they have no intention of honouring their respective obligations, or enjoying their respective rights, under the provisions of the agreement*".[6]

Similarly, in *Shalson v Russo* [2005] Ch 281 Rimer J emphasised the requirement that the shamming intention be shared by both parties to the transaction:

> "*The settlor may have an unspoken intention that the assets are in fact to be treated as his own and that the trustee will accede to his every request or demand. But unless that intention is from the outset shared by the trustee (or later becomes so shared), I fail to see how a settlement can be regarded as a sham. Once the assets are vested in the trustee, they will be held on the declared trusts, and he is entitled to regard them as so held and to ignore any demands from the settlor as to how to deal with them. I cannot understand on what basis a third party could claim, merely by reference to the unilateral intentions of the settlor, that the settlement was a sham and that the assets in fact remained the settlor's property*".[7]

[6] [45].
[7] 342.

The letter from Macbeth Jr to Macbeth appears to be clear evidence of a shared 'shamming' intention – accordingly, it seems likely that the conveyance would be held to be a sham.

The next question is what the consequences of this are. In *Penn v Bristol and West Building Society* [1995] 2 F.L.R. 938 a conveyance was held to be a sham, with the outcome that it was void. Furthermore, as Morgan J explained *Victus Estates (2) Limited* v *Munroe* [2021] EWHC 2411 (Ch), the consequence of a conveyance being void is that s.63 of the LPA 1925 cannot take effect in respect of it.[8] As such, we would expect the same result to follow here.

This clearly has the potential to create injustice for Lloyd's Bank, which has advanced £20,000 to Macbeth Jr on the basis of having security over his interest in the property. Such a scenario was considered in *obiter* by Neuberger J in *National Westminster Bank v Jones* at [60]:

> "*If a tenancy agreement is a sham, and an innocent third party accepts it as security for a loan to the tenant, then it seems to me that the third party is entitled to treat the tenancy in existence as against the landlord and as against the tenant: it can scarcely lie in the mouth of either of them to contend that the tenancy agreement does not exist as against the mortgagee in such circumstances. However, difficulties could arise where the interest of one innocent party, who contends that the agreement is a sham, clash with the interests of another innocent party, who contends that it is genuine*".

The first part of this sounds very much like an estoppel: the lender in such a case would have acquired an proprietary interest by way of proprietary estoppel at the point of advancing the sums, having relied to its detriment on a sham document – so a charge could still have arisen in favour of Lloyd's against Macbeth's interest in the First Bothy. However, such an interest would arise later in time than the interest of a party seeking to trace into the First Bothy (e.g. Macduff), so rank behind it in terms of priorities.

The Second Bothy

The settlement of the Second Bothy on trust appears to be susceptible to an argument that the trust in question is an 'illusory trust'.[9] Although a developing doctrine, one helpful definition is provided by *JSC VTB Bank v Skurikhin* [2015] EWHC 2131 (Comm) at [39]:

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[8] [61].

[9] In *JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev* [2017] EWHC 2426 (Ch) Briss J expressed disquiet about the appropriateness of the term 'illusory trust', and in the subsequent decision of the Privy Council in *Webb v Webb* [2020] UKPC 22 the term was not used.

> "*property subject to trust…would be regarded in equity as assets of the judgment debtor if he has the legal right to call for those assets to be transferred to him or to his order, or if he has de facto control of the trust assets in circumstances where no genuine discretion is exercised by the trustee over those assets.*"[10]

In other words, a trust will be 'illusory' where, on its true construction, the trust instrument fails to manifest the necessary (objective) certainty of intention on the part of the settlor to divest themselves of beneficial ownership. One example is provided by the recent decision in *Webb v Webb* [2020] UKPC 22, where the Privy Council held that the powers reserved to the settlor were so extensive as to be "*tantamount to ownership*", with the result that there was no trust.

In the present case it seems likely, on the information available, that this threshold would be crossed: Macbeth has extensive powers, including a power of revocation, reserved to himself and seems in practice to be able to direct the trustees as to how the trust property is administered. As such, the trust fails and the property results back to Macbeth.

The Third Bothy

Turning finally to the Third Bothy, following *Prest v Petrodel* [2013] UKSC 34 it is well established that the courts will only pierce the corporate veil in very limited circumstances (essentially confined to the deliberate evasion of obligations by abusing the doctrine of corporate personality – this element of the claim in *Prest* itself failed).[11] Although an arguable case might be mounted that this is such a case on the basis of Macbeth's web of fraudulent conduct, it would be unsafe for his creditors to rely on this.

Instead, the outcome in *Prest* itself points towards a neater solution. In cases where property is advanced to a third party (absent certain specified relationships), there may be a weak presumption that the property is held on resulting trust.[12] Accordingly, in the absence of evidence to the contrary, a company may be found to hold the legal title on trust for the disponee. This was the outcome in *Prest* itself.

We say 'may' because a modicum of doubt is introduced by s.60(3) of the LPA 1925, which provides that "*in a voluntary conveyance, a resulting trust for the grantor shall not be implied merely by reason that the property is not expressed to be conveyed for the use or benefit of the grantee*"; s.60(3) was

[10] cf. [45].
[11] See [35].
[12] *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] AC 669 at 708.

not referred to in *Prest* (something which *Halsbury's* suggests was an oversight). Furthermore, in *Lohia v Lohia* [2001] EWCA Civ 1691 the Court of Appeal suggested in *obiter* that the presumption of resulting trust may have been abolished by s.60(3).

However, when the issue arose for decision in *National Crime Agency v Dong* [2017] EWHC 3116 (Ch), Chief Master Marsh held that the presumption of a resulting trust in favour of a grantor survived the enactment of the provision, relying on the view to this effect expressed in *Snell's Equity.*[13] We are inclined to agree. And in any event, the existence of a resulting trust could still be established by positive evidence – it is only the presumption which may have been displaced by the statutory provision.

As to whether Bothy Holdings Ltd holds the property on resulting trust for Macbeth, in *Prest* Lord Sumption cautioned that

> "*Whether assets legally vested in a company are beneficially owned by its controller is a highly fact-specific issue. It is not possible to give general guidance going beyond the ordinary principles and presumptions of equity, especially those relating to gifts and resulting trusts*."

However, some of the matters which may be relevant were identified in *Khazakstan Kagazy Plc v Zhunus* [2021] EWHC 3462 (Comm) at [283]:

> "*It is relevant to consider whether a company alleged to be a nominee:*
>
> *i)* *acts in a manner that is not consistent with its own best interests (e.g. if a company gives away assets/does not use them for business purposes – such as allowing a property to be used as a matrimonial home for no consideration);*
>
> *ii)* *deals with its assets informally, without requiring its affairs to be properly documented;*
>
> iii) *has any trading business; or*
>
> iv) *has been newly incorporated to hold the asset in question: see, e.g.* NRC Holding Ltd v Danilitskiy *[2017] EWHC 1431 (Ch) [39]*".

[13] [29] - [35].

On the information available, it seems well arguable that the Third Bothy is held on resulting trust for Macbeth: Bothy Holdings Ltd seems to have been recently incorporated for the sole purpose of holding the property and does not appear to make any commercial use of the property (or indeed have any business whatsoever). In any event, it may be tactically advantageous for Macbeth's creditors to raise this in the proceedings as it will throw the evidential burden on him to adduce evidence to the contrary; in *Prest* itself the decision in the Supreme Court that the property was held on resulting trust for the husband ultimately turned on his evasiveness whilst giving evidence, which prevented the presumption from being rebutted.

The Isle of Bute property

The transfer of the property on Bute to Hecate appears to have been effective. This does not mean, however, that it cannot be challenged. We will explore this further below.

Other assets

It is worth briefly noting the range of routes via which Macbeth's creditors and potential creditors may seek to obtain information about any other assets which he controls.

First, there are a range of interim remedies available to claimants prior to judgment: these include *Norwich Pharmacal*, *Bankers Trust* and *Anton Piller* orders, and the power to order a party to provide information about the location of property or assets which may be subject to a freezing injunction under r.25.1(g).

Secondly, following judgment Macbeth's judgment creditors would be able to use the procedures of Part 71 of the CPR to obtain information about his assets for the purpose of enforcement. Indeed, it appears that Duncan has already done so.

Finally, if Macbeth were to be made bankrupt (or any of his companies wound up by order of the court), the trustee in bankruptcy/liquidators would acquire extensive powers to investigate the affairs of the insolvent estate, including under s.236 and s.366 of the Insolvency Act 1986.

Question 2

As the starting point in establishing a proprietary claim is the ability of Macbeth's various victims to 'follow' or 'trace' the proceeds of his frauds, it is convenient to begin with a brief refresher on the rules governing tracing.

In *Foskett v McKeown* [2001] 1 A.C. 102 at 127–128 Lord Millett provided the canonical exposition of tracing's role in the law of asset recovery:

> "*Tracing is…neither a claim nor a remedy. It is merely the process by which a claimant demonstrates what has happened to his property, identifies its proceeds and the persons who have handled or received them, and justifies his claim that the proceeds can properly be regarded as representing his property. Tracing is also distinct from claiming. It identifies the traceable proceeds of the claimant's property. It enables the claimant to substitute the traceable proceeds for the original asset as the subject matter of his claim. But it does not affect or establish his claim*. *The successful completion of a tracing exercise may be preliminary to a personal claim (as in* El Ajou v Dollar Land Holdings plc *[1993] 3 All ER 717) or a proprietary one, to the enforcement of a legal right (as in* Trustees of the Property of F C Jones & Sons v Jones *[1997] Ch 159) or an equitable one."*[14]

Accordingly, tracing is really best understood as a rule of evidence which may be a necessary prerequisite to obtaining either a personal or a proprietary remedy.

Following and tracing are technically distinct processes: following involves following a particular asset from hand to hand (e.g. a painting as it is sold and re-sold), while tracing involves identifying the substitutes for the original property in the hands of the same party (e.g. a claimant could trace into a car which a thief acquired using the proceeds from the sale of the painting). While it is common to speak of tracing 'into' an asset this is, strictly speaking, inaccurate; as Lord Millett explained in *Foskett*, it is really the value of the asset which is traced.

The prevailing orthodoxy remains that there are two separate species of tracing at common law and in equity, each of which is subject to subtly different rules.

The equitable rules (which are more generous) will apply in cases where the claimant only held the beneficial title to the property in question:

> "*The equitable remedies pre-suppose the continued existence of the money either as a separate fund or as part of a mixed fund or as latent in property acquired by means of such a*

[14] Cf. his judgment in *Boscawen v Bajwa* [1996] 1 W.L.R. 328 at 334. It is worth noting that, in a similar vein, the frequent tendency to refer to the 'remedy of an account' following a breach of trust is essentially meaningless, all beneficiaries of trusts being entitled as of right to an account of the trust's incomings and outgoings – it is only upon receipt of the account that the beneficiaries will be able to seek the court's assistance in remedying any misappropriation of trust property (for example, by calling for delivery up of missing property *in specie* or 'falsifying' the account such that the trustee will become liable to reconstitute the fund in the sum of any unauthorised disbursements).

> *fund. If, on the facts of any individual case, such continued existence is not established, equity is as helpless as the common law itself*."[15]

As Lord Browne-Wilkinson explained in *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] A.C. 669 at 706:

> "*A person solely entitled to the full beneficial ownership of money or property, both at law and in equity, does not enjoy an equitable interest in that property. The legal title carries with it all rights. Unless and until there is a separation of the legal and equitable estates, there is no separate equitable title. Therefore to talk about the bank "retaining" its equitable interest is meaningless. The only question is whether the circumstances under which the money was paid were such as, in equity, to impose a trust on the local authority. If so, an equitable interest arose for the first time under that trust*."

The first step in any tracing claim is, of course, for the claimant to show that they originally had title to the property in question. For tracing at common law, this simply requires them to have been the legal and beneficial owner of the property. At equity, the matter may be more complex if there is not an express trust; so, for example, in fraud claims the claimant will frequently have to show that the circumstances in which the defendant acquired the property were such as to require the imposition of a constructive trust at the point of its misappropriation. In general the courts have been prepared to adopt an expansive approach such that, in the majority of fraud cases, a court will find that misappropriated property became impressed with a constructive trust at the moment of misappropriation.[16] There are, however, enduring controversies about how readily the court should impose constructive trusts, which are beyond the scope of this paper.

Next, it is necessary that the original property – or its substitutes – remain clearly identifiable/can be identified across a connected series of unbroken transactions. In most cases this will simply be a question of factually reconstructing the transfers which took place, but we will explore the precise scope of this requirement in light of some of the recent case law as we move through the problem.

Finally, it is necessary for the claimant to show that their interest in the property has survived that process of transmissions. The common law, which requires both the legal and beneficial title to have survived, takes a restrictive approach which manifests itself in a number of limitations, including a prohibition on tracing through a mixed fund, and the availability of a broader range of defences (e.g.

[15] *Re Diplock* [1951] AC 251.

[16] Cf. Lord Browne-Wilkinson's famous example of thief becoming constructive trustee of a stolen bag of coins in *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] AC 669 at 715-716.

the defence of change of position).[17] Equity's approach is more expansive, only requiring that the beneficial interest survives. So if the ultimate recipient acquires an interest which equity will recognise as taking priority over that of the 'original' beneficial owner – for example, if the recipient is a *bona fide* purchaser for value without notice ('equity's darling') – the 'original' owner will be incapable of tracing the value into the recipient's hands, and may instead be left with a personal claim against the original wrongdoer.

If the claimant is able to establish that the defendant holds an asset which they are entitled to follow or trace, the claimant will be entitled to a remedy. As Millett LJ put it in *Boscawen v Bajwa* at 334, "*the remedy will be fashioned to the circumstances*", and may be either personal or proprietary.

There is a lively academic debate about the precise jurisprudential basis of tracing in equity, with scholars of restitution seeking to suggest that tracing (and the remedies which flow from it) are really best understood as responses to unjust enrichment. This debate is beyond the scope of this paper. Suffice to say that Chancery judges have firmly repeatedly and firmly rejected any suggestion that tracing is anything other than a vindication of proprietary rights.

Question 3a

Lady Macbeth seems to have been ignorant of Macbeth's schemes. There is therefore no obvious basis on which she could be rendered liable as a dishonest assistant or knowing recipient.

But that is not the end of enquiry. Lady Macbeth has not given value for the transfer. She is therefore a volunteer and Duncan's beneficial interest ought to survive the transfer to her account.

However, the fact that the balance of the account has dipped to £50,000 complicates matters. Where money to which the claimant is beneficially entitled is mixed with the property of another innocent party, the 'rule in *Clayton's Case'* will treat the sum first paid in as the sum first paid out.[18] The rule is controversial, and following the decision of the Court of Appeal in *Barlow Clowes v Vaughn* [1992] 4 All ER 22 is now treated as a displaceable presumption in cases where it would be unjust for the other innocent party to bear the entirety of the diminution in the balance. In the present case, given that Lady Macbeth has directly benefited from the expenditure in the account, we think that it is more

[17] This separation has been criticised at highest level: see *Foskett* at 128G where it was suggested in *obiter* that tracing at common law should become subject to the same rules as tracing in equity: "one set of tracing rules is enough".
[18] *Devaynes v Noble* (1816) 35 ER 781.

likely that the rule would be applied, such that Lady Macbeth's £10,000 would be exhausted first, and Duncan would be entitled to the full £50,000.

Question 3b

Where trust funds are mixed in a trustee's personal account, the rule *Re Hallett's Estate* (1880) 13 Ch D 696 presumes that any subsequent transactions deplete the trustee's own funds before those of the beneficiary; only once these are exhausted will the trust funds start to be depleted in any subsequent transactions. However, if the balance of the account falls below the sum to which the beneficiary is entitled, equity limits a beneficiary's proprietary claim to the lowest balance which the account reached between the date of the wrongful deposit and the date of the claim: see *Roscoe v Winder* [1915] 1 Ch 62. Accordingly, the value which Duncan will be entitled to trace into the account will be limited to £90,000. (None of this precludes Duncan from seeking to trace the funds paid out of the account).

A similar result would follow if the account had dipped into overdraft. In *Bishopsgate Investment Management v Homan* [1995] 1 ALL ER 347 the Court of Appeal held that where money is paid into an overdrawn bank account, the asset in question ceases to exist, and accordingly there can be no question of tracing the asset.[19] However, one possible exception to this arises where an individual has multiple accounts with the same bank. In *Cooper v PRG Powerhouse Ltd* [2008] EWHC 498 (Ch) at [32] it was accepted that in such a case, the courts could have regard to the claimant's overall credit with the bank, rather than confining itself to the balance of any particular account. It would therefore be worth investigating if Macbeth holds any other accounts with RBS which have not been disclosed.

Question 3c

The bothies are clearly 'substitute' assets for the sums misappropriated by Macbeth. Furthermore, as we have concluded that Macbeth's attempts to divest himself of the bothies probably failed, there is no third party able to assert a better equitable title than Duncan. As such, he ought to be able to trace into them.

Question 3d

This questions raises three issues.

[19] This was also the conclusion reached by the Court of Appeal in *Director of the Serious Fraud Office v Lexi Holdings* [2009] QB 376 – see [48] – [50].

The first is the ability of a party tracing in equity to take the benefit of any increase in the value of the misappropriated property. It is now firmly established that a claimant is entitled not only to the return of the original property, but also an appreciation in its value: see *Foskett* at 131A-B. Although this will result in a significant windfall for Duncan (and further deplete the assets which might have been available for other creditors), this is an inevitable consequence of the proprietary nature of the exercise. As Lord Millett explained in *Foskett* at 127:

> "*The transmission of a claimant's property rights from one asset to its traceable proceeds is part of our law of property, not of the law of unjust enrichment. There is no "unjust factor" to justify restitution (unless "want of title" be one, which makes the point). The claimant succeeds if at all by virtue of his own title, not to reverse unjust enrichment. Property rights are determined by fixed rules and settled principles. They are not discretionary. They do not depend upon ideas of what is "fair, just and reasonable". Such concepts, which in reality mask decisions of legal policy, have no place in the law of property*."

Or, as Lord Browne-Wilkinson put it,

> "*this windfall is enjoyed because of the rights which the purchasers enjoy under the law of property. A man under whose land oil is discovered enjoys a very valuable windfall but no one suggests that he, as owner of the property, is not entitled to the windfall which goes with his property right. We are not dealing with a claim in unjust enrichment*".[20]

The second, more controversial issue, is the ability of a claimant to trace into property which was 'acquired' *prior to* the alleged fraud perpetrated against them by the defendant. At first blush, this chafes against orthodox principles of tracing: if the source of the asset was not the claimant's property, what is there for the claimant to trace into?

Although long regarded as heretical, the realities of modern fraud have led to the appellate courts recently recognising the possibility of so-called 'backwards tracing'.

The first decision to recognise this possibility implicitly was the decision of the Court of Appeal in *Relfo Ltd (in liquidation) v Varsani* [2014] EWCA Civ 360, in which a dishonest director caused a payment to be made by the claimant company to a company called Mirren Ltd. Almost simultaneously, a payment for an almost identical amount was made by another company, Intertrade, to the defendant. The Court of Appeal inferred that Mirren Ltd had somehow transmitted the sum to Intertrade and/or that Intertrade had made the payment in anticipation of receiving the misappropriated sum from Mirren,

[20] 110G

and therefore held that the claimant could trace against Varsani (or, alternatively, that Varsani had been unjustly enriched at its expense). It was said at [63] that

> "*In my judgment, Mr Shaw is correct in his submission that* Agip *is authority for the proposition that monies held on trust can be traced into other assets even if those other assets are passed on before the trust monies are paid to the person transferring them, provided that that person acted on the basis that he would receive reimbursement for the monies he transferred out of the trust funds… What the court has to do is establish whether the likelihood is that monies could have been paid at any relevant point in the chain in exchange for such a promise*" (emphasis added).

In the ongoing *SAAD* litigation in the Cayman Islands, the Cayman Courts declined to extend the reasoning of *Relfo* to circumvent the need for a clear chain of transactions by holding that it was possible to trace into assets acquired in return for a debt. Properly considered, both *Relfo* concerned deliberate schemes designed to subvert the ability of creditors to trace, and it was this which justified the inference.

Shortly afterwards, the existence of backwards tracing was explicitly recognised for the first time by the Privy Council in *The Federal Republic of Brazil v Durant International Corporation* [2015] UKPC 35. The case concerned the misappropriation of funds by the former mayor of Sao Paulo in connection with a major public infrastructure project which had been passed through a series of overdrawn bank accounts. In permitting the claimant to trace into the hands of the defendant company, Lord Toulson at [38] held that (emphasis added)

> *"The development of increasingly sophisticated and elaborate methods of money laundering, often involving a web of credits and debits between intermediaries, makes it particularly important that a court should not allow a camouflage of interconnected transactions to obscure its vision of their true overall purpose and effect. If the court is satisfied that the various steps are part of a co-ordinated scheme, it should not matter that, either as a deliberate part of the choreography or possibly because of the incidents of the banking system, a debit appears in the bank account of an intermediary before a reciprocal credit entry… the availability of equitable remedies ought to depend on the substance of the transaction in question and not on the strict order in which associated events occur…"*

Lord Toulson continued at [40] that in order to trace backwards, a claimant "*has to establish a co-ordination between the depletion of the trust fund and the acquisition of the asset which is the subject of the tracing claim, looking at the whole transaction, such as to warrant the court attributing the*

value of the interest acquired to the misuse of the trust fund." So, the litmus test would appear to be whether the transaction into which the claimant seeks to trace was made in anticipation of the misapplication of the funds.

This is clearly a highly fact-sensitive question. But in the present case, it seems at least arguable that Macbeth's decision to commence the improvement works on the castle was made in anticipation of receiving the fraudulently acquired sums from Banquo (or his other victims).

Finally, there does not appear to be any English authority dealing with the question of whether it is possible to trace into the value of improvements to pre-acquired property. In the Jersey case of *Re Esteem Settlement* [2002] JLR 53 it was suggested that it should be possible to trace into any increase in the value of pre-owned misappropriated trust property expended on improvements to land already owned by an innocent donee. In light of this, the preferable view seems to be that, at the very least, the property would be subject to a charge in the claimant's favour as security for the sum stolen, and possibly that the claimant would be entitled to a pro rata share of any overall increase in value.[21]

Question 4

The Life Insurance Policy

As is well known, *Foskett* itself concerned a life insurance policy. In 1988, a number of purchasers had entrusted a total of £2.6m to a Mr Murphy for a property development scheme in Portugal on terms that within two years the developed plots would be conveyed to the purchasers or their money repaid with interest. The scheme was never carried out. Instead Mr Murphy, in breach of trust, used some £20,440 of the purchasers' money to pay two annual premiums for 1989 and 1990 on a whole life insurance policy effected in 1986 which paid out £1m to his children following his suicide in 1991. The litigation concerned whether the purchasers or the children should have the benefit of the payment. In the House of Lords, Lord Millett described the case as "a *textbook example of tracing through mixed substitutions*". It was held that Mr Murphy's victims were entitled to trace into a rateable proportion of the amount paid out under the policy. The same should be true here.

However, there is an added complication in the present case, arising from the fact that Macbeth is still very much alive. We will explore the ways in which Duncan may be able to access the value in the life insurance policy later on.

[21] Cf. *Boscawen* at 335 and Foskett at 109 and 113-114.

An option to purchase land

The outcome in *Foskett* was not confined to life insurance policies. As Lord Millett explained, the policy in question was a complex contractual instrument which created a bundle of rights in favour of the beneficiary of the policy. It was those bundle of rights – which represented the proceeds of the value misappropriated from the claimants – which the claimants were entitled to trace into.

Accordingly, we see no reason why a different form of contractual right – such as an option to purchase land – could not be amenable to the process of tracing.

Question 5

The first step here is establishing that Weird Sisters LLP was a knowing recipient.

The requirements for such a claim were accurately summarised by Hoffman LJ in *El Ajou v Dollar Land Holdings plc* [1994] 2 All ER 685 at 700:

(i) There must be a disposal of assets in breach of fiduciary duty;
(ii) The defendant must be in receipt of those assets or their traceable proceeds;
(iii) The claimant must show that the assets are traceable to the original breach of duty.

All three of these elements appear to be present here.

However, any attempt by Duncan to trace into the leasehold interest in the property will be complicated by the fact that the asset in question is a registered interest in land.

Section 29 of the LRA has the consequence that a transferee for valuable consideration of land will take title free form the prior beneficial interest even if they had notice that the transfer was in breach of trust, unless the beneficiaries of the trust were in actual occupation at the time of the disposition. Furthermore, section 26 prevents the title of a transferee from being questioned on the basis of the validity of the disposition.

Two consequences flow from this. The first is that it would appear to be impossible for Duncan to assert a proprietary claim over the lease of the office; his beneficial interest has been statutorily 'postponed'.

The second, more controversial, consequence is that Duncan may also be precluded from bringing a personal claim in knowing receipt against Weird Sisters LLP. Two commentators – Matthew Conaglen and Amy Goymour – expressed the view in a 2010 article that "*in situations where trust property is*

registered land and the trustee transfers title to that land in breach of trust, if the disposition was made for valuable consideration so that the transferee can claim the benefit of section 29 of the Land Registration Act 2002 to avoid the beneficiaries' pre-existing equitable interest in the land, the transferee ought also to be immune from a personal claim for knowing receipt".[22] The apparent rationale for this was that 'proprietary base' necessary for a claim in knowing receipt (whether personal or proprietary) to be brought is destroyed by the operation of statutory provisions. The Court of Appeal declined to criticise this view in the recent case of *Byers v Saudi National Bank* [2022] EWCA Civ 43.

The Law Commission has taken a different view, suggesting in its report *Updating the Land Registration Act 2002* (2018) that s.26 and s.29 are only intended to prevent the validity of a disponee's title from being questioned, but not to prevent personal claims against the disponee. Furthermore, in *Haque v Raja* [2016] EWHC 1950 (Ch) Henderson J (albeit during an interim hearing) suggested in *obiter* that a disponee could not rely on the provisions to avoid being called on to account:

> "*if the requisite degree of knowledge on the part of [the transferee] is established, his liability as a constructive trustee arises as a matter of law and attaches to the Property while it remains in his ownership. It is a liability which affects his conscience directly, and is not dependent upon the survival of the claimant's original beneficial interest…This way of putting the claim is therefore unaffected by the technicalities of overreaching and land registration".*

This view also appears to gain indirect support from the judgment of Sir Terrence Etherton MR in *Arthur v AG of the Turks and Caicos Islands* [2012] UKPC 30. In that case, the question arose of whether a Torrens system of land registration (in that case in the Turks and Caicos Islands) precluded a claim that the registered proprietor of the land held it on constructive trust. The central allegation in the case was that Mr Arthur had received the freehold transfer of land in the knowledge that the transfer was being effected by the Minster for Natural Resources in breach of fiduciary duty. Mr Arthur contended that the operation of the Torrens system meant that he had taken good title, free from any pre-existing property interest vested in the Crown. The Privy Council dismissed this argument, holding that it would be "*strange*" if a quick sale by a wrongdoer could defeat the ability of a claimant to bring both a proprietary and a personal claim to recover their property.[23]

[22] In Mitchell, *Constructive and Resulting Trusts* (2010) .p.181; quoted by the Court of Appeal in *Byers v Saudi National Bank* at [64].
[23] [42].

We therefore prefer the view of the Law Commission and Henderson J, but given its recent airing by the Court of Appeal in *Byers* the matter may be ripe for consideration in a case which calls for it to be definitively determined.

In the present case, this means that Duncan be limited to a personal claim for equitable compensation against Weird Sisters LLP.

Ruritania

While the usual rule is that all rights in relation to immovable property are governed by the *lex situs*,[24] an exception exists in relation to constructive trusts.[25]

So, in In *Lightning v Lightning Electrical Contractors Ltd* (2009) 1 TLI 35 Peter Gibson LJ held that

> "*where a plaintiff invokes the in personam jurisdiction of the English court against a defendant amenable to the jurisdiction and there is an equity between the parties which the court can enforce, the English court will accept jurisdiction and apply English law as the applicable law, even though the suit relates to foreign land. In contrast if the equity which is asserted does not exist between the parties to the English litigation, for example where there has been a transfer of the property to a third party with notice of an equity but by the lex situs governing the transfer, the transfer extinguished the plaintiff's equity, the English court could not then given relief against the third party even though he is within the jurisdiction*".

Similarly, in *Akers v Samba* [2017] AC 424 Lord Mance accepted at [21] and [34] that a "common law trust" could exist in respect of property (in that case shares) registered in a country which did not recognise beneficial interests. Accordingly, subject to the rules of overreaching in the land registration system of Ruritania, there is no reason why Duncan could not trace at equity into the property (although enforcement may be more complex).

Question 6

This question is designed to explore the operation of equitable subrogation.

The doctrine was explained by Walton J in *Burston Finance v Speirway Ltd* [1974] 1 WLR 1648 at 1652 as arising "*where A's money is used to pay off the claim of B, who is a secured creditor, A is entitled to*

[24] See *Dicey,* Rule 132.
[25] See *Dicey*, Rule 172.

be regarded in equity as having had an assignment to him of B's rights as a secured creditor…". He continued:

> *"It finds one of its chief uses in the situation where one person advances money on the understanding that he is to have certain security for the money that he has advanced, and for one reason or another, he does not receive the promised security. In such a case he is nevertheless to be subrogated to the rights of any other person who at the relevant time had any security over the same property and whose debts have been discharged in whole or in part by the money so provided by him."*

But its operation is not limited to such a scenario. As Millett LJ explained in *Boscawen v Bajwa* [1996] 1 WLR 328

> "*It is available in a wide variety of different factual situations in which it is required in order to reverse the defendant's unjust enrichment. 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 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. A constructive trust arises in the same way. Once the equity is established the court satisfies it by declaring that the property in question is subject to a charge by way of subrogation in the one case or a constructive trust in the other.*"

Indeed, although most of the cases are about subrogation to existing forms of security, the principle can apply equally to personal rights: see *Cheltenham & Gloucester plc v Appleyard* [2004] EWCA Civ 291 at [36] and *Investment Trust Companies v Revenue and Customs Comrs* [2018] AC 275.

In light of the decision of the Supreme Court in *Menelaou v Bank of Cyprus Ltd* [2015] UKSC 66 (following *Banque Financiere de la Cite v Parc (Battersea) Ltd* [1998] UKHL 7) it now seems that the jurisprudential basis of subrogation is not the vindication of proprietary rights, but rather the reversal of unjust enrichment. However, Lord Carnwath was critical of this analysis, both because it was unnecessary to dispose of the case, and because it did violence to established principles. As Parker LJ noted in *Halifax v Omar,* the decision in *Banque Financiere* probably turned on the fact that the

appropriate remedy in that (unusual) case was personal rather than proprietary, which goes some way towards explaining the decidedly un-proprietary nature of Lord Hoffmann's reasoning.[26]

Later, in *Swynson Ltd v Lowick Rose LLP* [2017] UKSC 32, at [30] Lord Sumption suggested in reference to *Banque Financiere* and *Menelaou* that "*it would be unwise to draw too close any analogy with the role of mistake in other legal contexts or to try to fit the subrogation cases into any broader category of unjust enrichment. It is in many ways sui generis*". But he then went on to suggest another alternative analysis based on failure of basis: "*what this suggests is that the real basis of the rule is the defeat of an expectation of benefit which was the basis of the payer's consent to the payment of money for the relevant purpose*".

Banquo's position

On a conventional analysis, Banquo is able to straightforwardly trace into the RBS Charge. Strictly speaking, the RBS Charge has ceased to exist but Banquo's relations with Macbeth are regulated as if the benefit of the charge was assigned to him by RBS.

Ghost At The Feast

Tracing

The position of Ghost At The Feast Ltd is more complicated because it has not actually advanced any sum; instead, it is has simply released another charge in the expectation of receiving a new charge which has, in the event, failed to fully materialise.

It is an open question whether Ghost At The Feast Ltd has a sufficient proprietary interest in the proceeds of sale to be able to trace into the Clydesdale Charge. In *Buhr v Barclays Bank Plc* [2002] BPIR 25 Arden LJ suggested at [45] that where a mortgagor makes a disposition of mortgaged property in a manner which destroys the mortgagee's estate, the mortgagee will obtain a proprietary interest in the proceeds of sale. However, at [46] she went on to hold that if the property was sold with the consent of all the parties, the mortgagee cannot elect to have a charge over the proceeds of sale. This was fatal to an argument that the bank retained a proprietary interest at first instance in *Menelaou*, and both the Court of Appeal and majority in the Supreme Court disposed of the case on different grounds, preferring to leave the question open for another day. On these facts, we find the suggestion that Ghost At The Feast Ltd gave sufficient 'consent' to be debarred from asserting a proprietary interest difficult – its consent was conditional and the condition failed to materialise. A relevant

[26] Indeed, Neuberger LJ also seemed to recognise this in *Appleyard* at [32].

analogy may be a defective execution of a power which may give rise to a proprietary claim against the power holder if they are a trustee.

If Ghost At The Feast Ltd were able to trace into the Clydesdale Charge, Lady Macbeth would be able to take advantage of an equity of exoneration. This operates as follows:

> "*A person who has mortgaged his property to secure the debt of another is presumed in the absence of other evidence to be only a surety is and is entitled to be exonerated by the principal debtor. The same is true where jointly-owned property is mortgaged to secure money raised for the benefit of one joint owner*".[27]

In such a case, the surety may thus seek an order of the Court that any right to enforce against the property by the creditor be taken to be in extinction of the debtor's share in the asset before that of the surety. This could obviously have significant consequences for the ability of other, unsecured, creditors of Macbeth is the redemption of the Clydesdale Charge is (in effect) borne solely by his interest in the property.

Subrogation

But assuming that it cannot trace into the Clydesdale Charge, Ghost At The Feast will instead need to seek to perfect its charge over the land at Burnham Wood. This could be done in one of two ways.

First, Ghost At The Feast Ltd could seek to be subrogated to the vendor's lien which existed over the property between exchange of contracts and completion. This was the outcome in *Menelaou* where the bank had released a charge over property owned by the defendant's parents in the expectation of obtaining a charge over a property which they purchased for their daughter. This outcome is not obviated by the fact that Ghost At the Feast Ltd did obtain *some* security: see *Banque Financiere* at 241. In that case, the lender anticipated two forms of protection, one of which (a pledge of shares) was provided as agreed. Although this was "the principal security", it did not prevent the lender obtaining a subrogated right owing to the failure of the other form of protection.

The second is that an equitable charge has arisen in its favour by way of an estoppel. In *Kinane v Mackie-Conteh* [2005] EWCA Civ 45 a strong Court of Appeal accepted that an equitable charge could arise by way of estoppel. Indeed, this is what seems to have occurred in *Halifax Plc v Curry Popeck* [2008] EWHC 1692 (Ch). The facts of *Popeck* were remarkable. Two fraudsters, who were the registered freeholders of a bungalow with three garages at the bottom of its garden, perpetrated a

[27] *Day v Shaw* [2014] EWHC 36 (Ch) at [20].

mortgage fraud by which they obtained three mortgages from reputable lenders to be secured against the bungalow, but in fact granted each bank a charge registered against the title numbers of one of the three garages. Following the discovery of the fraud, one of the lenders obtained an order for sale at which point the question arose of how the proceeds of sale should be distributed. It was held that the first lender (Halifax) had acquired an equitable charge by way of estoppel at the time that it advanced the monies in reliance on the fraudsters' representations, and accordingly was 'first in time'. By parity of reasoning Ghost At The Feast Ltd would most likely have acquired an equitable charge over the entirety of the land.

Marshalling

The principle of marshalling operates in cases where two or more creditors are owed debts by the same debtor, one of whom can enforce his claim against more than one security. In such a case, the principle gives the second creditor a right in equity to require that the first creditor satisfy themselves so far as possible out of the fund against which the second creditor has no claim. See e.g. *Highbury Pension Fund Management Co v Zirfin Investments Ltd* [2014] Ch 359.

As such, if Ghost At The Feast Ltd were both to be subrogated to the Clydesdale Charge and to perfect its charge over the land at Burnham Wood, Macbeth's other creditors may be entitled to require it to look to the enforce against Burnham Wood.

Question 7

Tracing the bribe

This question raises two problems. The first is the status of the bribe paid to Macbeth – is this an asset into which Macduff is entitled to trace? After all, at first blush it is difficult to see how Macduff could have a beneficial interest in money which never belonged to him.

In *FHR Ventures LLP v Cedar Capital Partners LLC* [2014] UKSC 45 the Supreme Court held – with Lord Neuberger departing from his own previous decision in *Sinclair v Versailles* [2011] EWCA Civ 347 – that a secret commission such a bribe obtained by a fiduciary could be treated as the claimant's property such that it would be held on constructive trust. The 'proprietary base' is supplied by the fact that the defendant's opportunity to obtain the secret commission arose from the defendant's status as a fiduciary for the claimant. Similarly, it is well established that where a corporate opportunity is wrongfully exploited by a fiduciary, the resulting profit is held on trust for the principal: *Bhullar v Bhullar* [2003] 2 BCLC 241.

Has there been a valid disposition?

The second problem arises from the fact that, as set out above, there appears to be an argument that Hecate is 'equity's darling' – she has given (nominal) value for the property and knows nothing of Macbeth's fraudulent schemes.

There is legitimate doubt here: in *Nurdin & Peacock Plc v DB Ramsden & Co Ltd* [1999] 1 EGLR 119 Neuberger J suggested that a party who had paid £1 for a lease might not be a 'purchaser for value' in the eyes of equity. Hecate has paid £100, so it is perhaps an open question as to whether the same would be true here; in our view it is more likely than not that the same result would follow here. Macduff would therefore be able to trace into the property, notwithstanding the purported disposition to Hecate.

s.423

But assuming *contra* the above that the transfer to Hecate was effective, Macduff may be able to look to sections 423-425 of the Insolvency Act 1986 which contain a number of potentially far-reaching provisions for challenging transactions 'defrauding creditors'. In *Westbrook Dolphin Square Ltd v Friends Life (No 2)* [2014] EWHC 2433 (Ch) Mann J noted at [402] that "*a claim under s.423 is a claim for some appropriate form of restorative remedy, to restore property to the transferor for the benefit of creditors, who may then seek to execute against that property in respect of obligations owed by the transferor to them*".

The requirements for a claim under s.423 to be brought were summarised by Flaux J in *Fortress Value Recovery Fund I LLC v Blue Sky Special Opportunities Fund LP* [2013] EWHC 14 (Comm) at [104] as follows:

> "*(i) there must be a debtor*
>
> *(ii) who enters into a transaction*
>
> *(iii) at an undervalue*
>
> *(iv) with the purpose of putting assets beyond the reach of persons with an actual or potential claim*."

The jurisdiction under s.423 was recently considered in *Akhmedova v Akhmedov* [2021] EWHC 545 (Fam), in which Knowles J ordered Liechtenstein trustees to return around £360m said to have been transferred to them for the purposes of frustrating an award made in matrimonial proceedings. It was

held that it is not a requirement under the fourth limb that the effect of the transaction in question was to leave the debtor with insufficient assets.[28]

If the requirements are made out, the court has a very broad discretion to unwind the fraudulent transaction, including making any of the (non-exhaustive) orders set out in s.425(1).

On our facts, the first three requirements are clearly made out. The fact that the transfer was made the day after Macduff served proceedings would seem to suggest that the fourth would be as well.

Question 8

Charging Orders

A charging order is, of course, a charge over the judgment debtor's property to secure the judgment debt. Under the Charging Orders Act 1979, it is open to any judgment creditor to apply to either the High Court or the County Court for such an order. It has the obvious benefit of creating an enforceable equitable security (which is also capable of being recorded at the Land Registry against the registered title, either by the entry of a notice or a restriction in Form K).

The court has a discretion as to whether or not to make a charging order, although it has been said that a judgment debtor is "entitled in expecting that such an order will be made in his favour" in most cases.[29] However, where an innocent co-owner behind a trust of land, who is unconnected to the judgment debt, is resident at the property, the court would be required to take into account the matters set out at s.15 of TOLATA before making an order for sale.[30]

There is no reason in principle why a creditor cannot seek a charging order against a debtor who is on the verge of bankruptcy – indeed, from the creditor's perspective it will frequently be desirable to do so. While the court may choose to take into account any possible prejudice to other creditors if the applicant is granted a charging order, it has been suggested that this alone is unlikely to prevent a charging order from being made.[31]

Receivership

[28] [93] – [104].
[29] *Roberts Petroleum Ltd v Bernard Kenny Ltd* [1982] 1 WLR 301 at 307.
[30] *Mortgage Corp v Shaire* [2001] Ch 743.
[31] *Roberts Petroleum*, ibid.

While not conferring any proprietary interest or allowing a creditor to obtain priority, the appointment of a receiver may still have significant advantages in assisting in the recovery of assets against which more traditional methods of enforcement may be inadequate.

Receivership operates *in personam* against the owner of the property by disabling them from dealing with their property, notwithstanding the fact that they hold legal title to it. Provided that the court has *in personam* jurisdiction, it is no bar to the appointment of a receiver that the assets are located outside the jurisdiction: *Derby & Co Ltd v Wheldon (Nos 3 &4)* [1990] 1 Ch 65 (CA).

The court's power to appoint a receiver arises under the inherent equitable jurisdiction and is confirmed by s.37 of the Senior Courts Act 1981 which permits a receiver to be appointed wherever it would be "*just and convenient*" to do so. This is, of course, the same test governing the court's power to grant an injunction and, following the Privy Council's decision in *Convoy Collateral Ltd v Broad Idea* [2021] UKPC 24 the jurisdiction is (at least as a matter of principle) therefore almost unlimited.

The recent authorities point towards a pragmatic approach. In *Cruz City 1 Mauritius Holdings v Unitech Ltd* [2014] EWHC 3131 (Comm) at [47] Males J referred to the leading cases of *Masri v Consolidated Contractors (UK) Ltd (No. 2)* [2009] QB 450 (as subsequently summarised by Lord Collins in *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch Bank and Trust Co (Cayman) Ltd* [2012] 1 WLR 1721 before summarising the approach to be adopted as follows:

> *"In the light of these and other statements cited, I would summarise the position so far as relevant to the present application as follows:*
>
> > *a) The overriding consideration in determining the scope of the court's jurisdiction is the demands of justice. Those demands include the promotion of the policy of English law that judgments of the English court and English arbitration awards should be complied with and, if necessary, enforced.*
> >
> > *b) Nevertheless the jurisdiction is not unfettered. It must be exercised in accordance with established principles, though it is capable of being developed incrementally. It is not limited to situations where equity would have appointed a receiver before the fusion of law and equity pursuant to the 1873 Judicature Acts. Specifically, in modern conditions where business is increasingly global in nature, the jurisdiction is 'unconstrained by rigid expressions of principle and responsive to the demands of justice in the contemporary context'.*

c) The jurisdiction will not be exercised unless there is some hindrance or difficulty in using the normal processes of execution, but there are no rigid rules as to the nature of the hindrance or difficulty required, which may be practical or legal, and it is necessary to take account of all the circumstances of the case. That is all that is meant by dicta which speak of the need for 'special circumstances': see in particular the decision of Tomlinson J in Masri … and also the decision of Arnold J in UCB Home Loans Corporation Ltd v Grace [2011] EWHC 851 (Ch) , holding that there were sufficient 'special circumstances' rendering it just and convenient to appoint a receiver by way of equitable jurisdiction when it would be 'difficult for the claimant to enforce its judgment by other means' and that the appointment of a receiver was the only realistic prospect available to the judgment creditor to enforce its judgment in the short term.

d) As the statutory source of the court's power to appoint a receiver speaks of what is 'just and convenient', it is impossible to say that convenience is not at least a relevant consideration (albeit not the only one).

e) A receiver will not be appointed if the court is satisfied that the appointment would be fruitless, for example because there is no property which can be reached either in law or equity. That is an aspect of the maxim that equity does not act in vain. However, a receiver may be appointed if there is a reasonable prospect that the appointment will assist in the enforcement of a judgment or award. It is unnecessary, and will generally be pointless, for the court to attempt to decide hypothetical questions as to the likely effectiveness of any order. That applies with even greater force where such questions involve disputed issues of foreign law. It is sufficient that there is a real prospect that the appointment of receivers will serve a useful purpose."

In general, if the Court is satisfied (i) that there are assets amenable to the receiver's reach (ii) that it is not practicable to enforce by other means (iii) that there is a real prospect that the court receivership will serve a useful purpose and (iv) that the remedy is not disproportionate, then the discretion should be exercised in favour of making the appointment: see *JSC VTB Bank v Skurikhin* [2015] EWHC 2131 (Comm) at [52] – [56].

The assets over which a receiver may be appointed are "*whatever may be considered in equity as the assets of the judgment debtor*" (*Shurikhin* at [38]). This obviously encompasses conventional forms of both personal and real property but, as the decision in *Blight* shows, the courts have increasingly taken

a broad view. To give two other examples, in *Tasarruf* a receiver was appointed over a power of revocation in a Cayman Islands trust where an unfettered power of revocation had been reserved to the settlor, while in *Shurikhin* a receiver was appointed over the powers of an LLP member to sell properties owned by the LLP. In *Masri* a receiver was appointed over the future receipts generated from a specific asset.

The procedures for appointing and controlling receivers are contained in Part 69 of the Civil Procedure Rules. An order appointing a receiver will frequently be coupled with ancillary orders necessary to ensure the efficacy of the appointment.

In the present case, one obvious candidate for the appointment of a receiver is the life insurance policy. In *Foskett* Lord Millett obliquely dealt with the possibility that the claimants could have accelerated the realisation of the interest in the policy had Mr Murphy been alive: "*Had they [the victims] discovered what had happened before Mr Murphy died, they would have intervened. They might or might not have elected to take an interest in the policy rather than enforce a lien for the return of the premiums paid with their money, but they would certainly have wanted immediate payment. This would have entailed the surrender of the policy*." However, as the issue was not necessary for determination of the case, he did not set out the precise mechanism for effecting such a surrender.

One possible mechanism is indicated by the facts of *Blight v Brewster* [2012] EWHC 165 (Ch) in which a receiver was appointed over a right to drawn down 25% of pension as a tax-free sum. We can see no reason why the same could not be done here.

The subrogated charges

Finally, the subrogated chargees will have at their disposal the full range of remedies open to the mortgagee in whose shoes they stand. These may include any contractual or statutory rights to seek possession, obtain an order for sale or even foreclose.