SUBROGATION, SURETYSHIP, AND THE LAW OF RESTITUTION

By

MICHAEL IAN JACKSON

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Department of LAW

The University of British Columbia
1956 Main Mall
Vancouver, Canada
V6T 1Y3

Date 18 JULY 1988

ABSTRACT

Subrogation is well known to the common law legal system. It has existed in one form or other for at least three centuries, and quite possibly even longer. It was developed in the English courts of equity, and adapted for use in a variety of situations. Today, "rights" of subrogation lie at the heart of a number of commonplace legal relationships, including those of suretyship and insurance.

Yet, despite its antiquity, subrogation has never been well explained. Fundamental questions about its nature have never been fully resolved. Is it a "right"? Or a "remedy"? Or a "remedial technique"? Is it perhaps all of these? Or none? How exactly does it operate? And why? The answers forthcoming have varied almost from one case or piece of legal literature to the next. As a result, subrogation has remained something of a legal will-o-the-wisp - known to exist, experienced by many, but lacking theoretical substance.

Recently, however, the prospect of finally giving this theoretical substance to subrogation has improved. The catalyst for this has been the development and increasing acceptance in the common law world of a law of restitution premised upon a fundamental principle of unjust enrichment. For restitution writers have been quick to argue that subrogation, in its many guises, is fundamentally restitutionary in nature - that it is essentially a means of ensuring that one person in a tripartite relationship is not unjustly enriched at the expense of another in that relationship. This explanation, it is argued, more than any other in the past, offers the means of unifying subrogation in its various guises.

This paper is about this view of subrogation. Its general thesis is that subrogation is essentially restitutionary in nature. Subrogation can and should, it is submitted, be viewed as a remedial device or technique used to effect restitution in tripartite relationships when one party to that relationship would otherwise be unjustly enriched at the expense of another. As a necessary corollary, it is submitted that the existing "rights" of subrogation in our legal system can be satisfactorily explained and understood in these terms.

To test this general thesis and its corollary, this paper examines one in particular of the existing "rights" of subrogation, that of the surety. The surety's right of subrogation is one of the most established of the "rights" of subrogation. It many respects, it is the paradigm, or quintessential, tripartite case in which subrogation has been used. It should, therefore, fully reflect the restitutionary principles upon which subrogation is said to be premised. The question whether, and the extent to which, this is so is the central question that is explored in this paper.

Preliminary to that question, this paper explores and outlines the nature and content of the surety's "right" of subrogation itself, for this is an issue that is almost equally surrounded by uncertainty.

The general conclusion of this paper is that the surety's "right" of subrogation does fully reflect restitutionary principles, and can be satisfactorily explained in restitutionary terms, thus lending considerable support to this paper's general thesis. Further support for this conclusion is obtained by also considering the extent to which it holds true in relation to the closely related subrogation rights of parties to bills of exchange.

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INTRODUCTION

Chapter 1

INTRODUCTION

Subrogation is a remedial technique, or device, whereby one person, A, is "stood in the place (or shoes)" of another, B, in order to receive the benefit of B's pre-existing rights and remedies against a third person, C. Its use enables A, who is thought to deserve a remedy against C, to obtain that remedy, not directly, but indirectly through B. Its use is generally considered fair and just, since A is simply taking advantage of pre-existing rights and remedies against C, who thus seems no worse off. It is a relatively obvious and appealing method of effecting remedial justice in tripartite situations.

It is not surprising, therefore, to find that such a remedial technique has been recognised in Anglo-American law. Indeed, subrogation is of considerable antiquity in Anglo-American law.[1] Its use has been traced at least to the seventeenth century in England,[2] although its origins may well lie even earlier in English legal history.[3] Sureties, the quintessential "deserving party" in a tripartite situation, were apparently

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[1] See generally M.L. Marasinghe, "An Historical Introduction to the Doctrine of Subrogation: The Early History of the Doctrine - I & II", (1975) 10 Valp. U.L. Rev. 45, and 275.

[2] See eg. Sir R. Goff & G. Jones, THE LAW OF RESTITUTION (3rd ed., 1986)(hereafter "GOFF & JONES"), p. 524; G. Palmer, THE LAW OF RESTITUTION (1978), vol. I, p. 21.

[3] Marasinghe argues, loc. cit., I, p. 48, that the technique of subrogation in English law may have been first recognised and used by the courts of equity nearly a century earlier, in a contribution case: Anon. (circa 1557) 21 E.R. 1.

the first to benefit from its use, in Morgan v Seymour[4] in 1637. In that case, the Chancery ordered a creditor "to assign over" to co-sureties a bond previously given to the creditor by the principal debtor so that the co-sureties could "help themselves against the ...[debtor] for the said Debt."[5] A little over a century later, in 1749, the Chancellor, Lord Hardwicke, in Randal v Cockran,[6] held, without any reference to Morgan v Seymour or subsequent surety cases, that an insurer who had made full payment to an insured "had the plainest equity that could be"[7] and was entitled to the benefit of an insured's rights of recovery against third parties.

The recognition of these two uses of the remedial technique of subrogation was the principal development in the history of subrogation in Anglo-American common law. But they were not the only situations in which the use of subrogation was recognised. In the intervening century, for example, the Chancery had applied the technique of subrogation in at least one other context, that of loans of money to married women and infants to purchase "necessaries".[8] Similarly, in the years following its application in insurance cases, the courts found several other diverse uses for the technique.[9] Subrogation has, therefore, existed in English law, and subsequently in Canadian law, for well over two centuries.

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4 (1637) 1 Chan. Rep. 120, 21 E.R. 525.

5 Ibid., at 121, at 525.

6 (1748) 1 Ves. Sen. 98, 27 E.R. 916.

7 Ibid., at 98, at 916.

8 See infra, p. 23.

9 See infra, pp. 23-24.

Despite this considerable heritage, the topic of subrogation remains a source of considerable uncertainty and disagreement. The briefest examination of the various uses of subrogation only serves to bring to light and emphasise the numerous difficulties and inconsistencies that surround the subject. It has, for example, been variously described as a "doctrine", a "right", a "remedy", a "technique", and a "device". Its origins in English law have often been ascribed to Roman and civil law, but it has also been praised as an original development of the English common law legal system. Its development within the English legal system is generally ascribed to the courts of equity, but there are also occasional assertions, particularly in relation to subrogation in insurance law, that it was an original development of the common law courts.[10] It has been said to operate both as an "equitable assignment", and equally as "a transfer of rights from one person to another, without assignment or assent...".[11]

The attempt, therefore, to discern the essential characteristics of subrogation, with a view to proposing a conceptually integrated model of subrogation in all its contexts, faces considerable difficulties. It has recently been suggested that the task may even prove to be impossible:

> "['Subrogation'] embraces more than a single concept in English law. It is a convenient way of describing a transfer of rights from one

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10 The strongest advocate of this in recent years appears to be Lord Diplock. In Yorkshire Insurance Co. Ltd. v Nisbet Shipping Co. Ltd. [1962] 2 Q.B. 330, at 339-40, as Diplock J., he asserted that subrogation in insurance cases is an incident of the indemnity element lying at the heart of an insurance contract, and thus arises by virtue of an implied term in the contract. He re-asserted this in his judgments in Orakpo v Manson Investments Ltd. [1978] A.C. 95, at 104, and Hobbs v Marlowe [1978] A.C. 16, at 39. But this view has been considered in depth, and seriously doubted: see S.R. Derham, SUBROGATION IN INSURANCE LAW (1985), pp. 6-22.

11 Orakpo v Manson Investments Ltd. [1978] A.C. 95, at 104, per Lord Diplock.

> person to another, without assignment or assent of the person from whom the rights are transferred and which takes place by operation of law in a whole variety of widely different circumstances. Some rights by subrogation are contractual in origin ... . Others ... are in no way based on contract and appear to defeat classification except as an empirical remedy to prevent a particular kind of unjust enrichment. This makes particularly perilous any attempt to rely upon analogy to justify applying to one set of circumstances which would otherwise result in unjust enrichment a remedy of subrogation which has been held to be available for that purpose in another and different set of circumstances."[12]

Several reasons for these difficulties can be identified. First, and most simply, the term "subrogation" was a relative late-comer to English legal vocabulary, not apparently being introduced until the mid to late nineteenth century,[13] two centuries at least after the first use of the technique itself. Instead, the metaphor of "standing one person in the place (or shoes) of another" was generally used by the courts to describe

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[12] Idem. Goff & Jones, in the forward to their second, now outdated, edition of THE LAW OF RESTITUTION (2nd ed., 1978), refer to "what some say is the impossible, if not fruitless, task of formulating principles which unite all categories of subrogation. ... We consider that subrogation is one of the most important, if most intractable, subjects in the law of restitution."

[13] Marasinghe, loc. cit., II, p. 289, identifies Stringer v The English and Scottish Marine Insurance Co. Ltd. (1869) L.R. 4 Q.B. 676 as the first case in the English courts expressly to adopt the term. He does, however, identify an earlier case - a decision of the Privy Council on appeal from the Court of Appeals of the Province of Lower Canada, namely, Quebec Fire Insurance Co. v Augustin St. Louis and John Molson (1851) 7 Moo. P.C. 286, 13 E.R. 891 - where the term was used. This decision concerned "subrogation" under the civil law of Quebec and thus is not an authority on subrogation in English law. Nonetheless, it may have been the catalyst for the subsequent use of the term. As Marasinghe notes, loc. cit., II, pp. 287-8, "... the word 'subrogation' and the [English decisions] ... blended into a doctrine of subrogation applicable as such in English law ... . The succeeding English cases gave not the slightest indication that it was received from a foreign legal system where the word was used to connote a meaning different from what both equity and Lord Hardwicke envisaged".

the whys and wherefores of subrogation.[14] But even the use of this metaphor was not adopted in every case. The result is considerable difficulty in identifying accurately the various examples of subrogation in the case-law. This lack of a settled terminology, and the uncertainty thereby created, lies at the heart of many of the difficulties encountered with subrogation.

A second problem is that many of the subrogation cases contain no clear exposition of the reasons for its use. All that many of these cases say is that, according to the circumstances of the case, it was in some general sense "equitable" to grant relief by this means. Subrogation has, for example, been said to be a matter of the "plainest equity",[15] or of "natural justice".[16] "Explanations" along these lines, however, did little to advance understanding of the concept beyond the rudimentary. To a great extent, this theoretical weakness persists. Thus, even established equity texts give the subject of subrogation limited treatment, generally being merely descriptive of the various rights of subrogation, rather than analytical of their theoretical underpinings.[17]

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[14] The use of this metaphor has not always been welcomed. See, eg., GOFF & JONES, p. 525: "Metaphor has also contributed to the confusion." Birks, INTRODUCTION TO THE LAW OF RESTITUTION (1985), pp. 93-98, goes even further. He suggests, p. 93, that subrogation itself "is in the nature of a metaphor which can be done without."

[15] Randal v Cockran (1748) 1 Ves. Sen. 98, at 98, 27 E.R. 916, at 916, per Lord Eldon L.C.

[16] Craythorne v Swinburne (1807) 14 Ves. Jr. 160, at 162, 33 E.R. 482, at 483, per Sir Samuel Romilly, arguendo.

[17] This is not to say that there were no attempts at all to deal with this deficiency in earlier times, for there were. The most striking example is Sheldon's work on subrogation, H.N. Sheldon, THE LAW OF SUBROGATION, the first edition of which was published in 1882. See also D.G. Maclay, "Theory and Application of the Doctrine of Subrogation", (1885-86) 2 The Columbia Jurist 38. But more often than not, the entitlement to subrogation in any particular case was simply an historical

The third feature compounding the difficulties in this area is the almost automatic link that is drawn in many cases between subrogation and matters of security or priority. It is certainly true that subrogation is often highly relevant when questions of securities and priorities arise, as will be seen,[18] but there is no reason, it is submitted, why the two should necessarily be linked. Nonetheless, it is often assumed that they are. Given the theoretical shortcomings evident in the case-law, this is perhaps not surprising. But it has also been promoted by the simple fact that many of the early cases concerned with subrogation, particularly in the suretyship context, were primarily concerned with matters of security and priority. If subrogation could afford security or priority this to a surety, as it was held that it could, this gave a surety a tremendous advantage over mere unsecured creditors in the event of the principal debtor's insolvency. The assumption that this must always be the case is, however, the cause of some of the greatest difficulties in the development of subrogation. Most importantly, it can lead to the rejection of subrogation as a remedial technique because of the perception that subrogation, if permitted, would lead inevitably to the conferral of security and priority upon a party who did not merit that degree of beneficial treatment.[19]

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fact - equity had this remedial technique in its armoury, for whatever the reason, and it was used when and as necessary.

[18] Infra, p. 56 et seq..

[19] This was the approach adopted in Re Wrexham, Mold and Connah's Quay Ry. [1899] 1 Q.B. 440. Goff & Jones commented on this as follows: "[S]ome judges thought that to subrogate A to C must result in A succeeding to C's security. Consequently, subrogation was dismissed as irrelevant and A was given an independent, equitable right which put him in the same position as any other general creditor. In our view, this distinction was

Finally, there was no general perception of any necessary connection between the various rights of subrogation. Other than the fact that these rights were largely developed in the Chancery, and were explained in terms of "equity and good conscience", they remained substantially independent of each other. This was particularly true with regard to subrogation in the law of suretyship, and subrogation in the law of insurance, both of which have developed a considerable body of case-law on subrogation but without any special cross-referencing.

Overcoming these difficulties, it is submitted, only began to take place with the recognition and formulation of a substantive body of law known as the law of restitution premised on the principle of unjust enrichment. Development of this body of law occurred first in America, with the publication of the Restatement of the Law of Restitution[20] in 1937, and the formulation therein of the following general principle:[21]

> "A person who has been unjustly enriched at the expense of another is required to make restitution to the other."

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unnecessary and contrary to precedent; moreover, it would inevitably cause, and has caused, confusion as to the scope of equitable subrogation. Much of the confusion would never have arisen if the courts had accepted the full implications of the principle that subrogation is essentially a remedy, which is fashioned to the facts of the particular case and which is granted in order to prevent the defendant's unjust enrichment ... ", GOFF & JONES, p. 526.

[20] American Law Institute, RESTATEMENT OF THE LAW OF RESTITUTION-QUASI CONTRACTS AND CONSTRUCTIVE TRUSTS (1937).

[21] Ibid., p. 12, para. 1. In the tentative draft of the RESTATEMENT OF THE LAW OF RESTITUTION 2ND, this has been reformulated to read: "A person who receives a benefit by reason of an infringement of another person's interest, or of loss suffered by the other, owes restitution to him in the manner and amount necessary to prevent unjust enrichment"; noted in GOFF & JONES, p.13, note 64a.

English and Canadian law took longer to acknowledge this development and progress towards the formulation of a substantive law of restitution premised on the notion of unjust enrichment. In England, the first real impetus did not come until 1966 and the publication of the first edition of Goff and Jones's Law of Restitution.[22] Now in its third edition, this work formulated the principle of unjust enrichment in the following terms:[23]

> "[T]he principle of unjust enrichment is capable of elaboration and refinement. It presupposes three things: first, that the defendant has been enriched by the receipt of a benefit; secondly, that he has been so enriched at the plaintiff's expense; and thirdly, that it would be unjust to allow him to retain the benefit."

The English courts, however, have been slow to accept and adopt the notion of unjust enrichment as a general principle of restitutionary liability. This was recently emphasised by the House of Lords in Orakpo v Manson Investments Ltd.,[24] where Lord Diplock stated:[25]

> "My Lords, there is no general doctrine of unjust enrichment recognised in English law. What it does is to provide specific remedies in particular cases of what might be classified as unjust enrichment in a legal system that is based upon the civil law."

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[22] Goff & Jones, THE LAW OF RESTITUTION (1st ed., 1966). Several of the Law Lords had earlier made significant efforts in this regard. The most influential of these was probably Lord Wright. His best known judicial pronouncement in this regard is perhaps that in Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd. [1943] A.C. 32, where he stated, at 61-62: "It is clear that any civilised system of law is bound to provide remedies for cases of what had been called unjust enrichment or unjust benefit, that is to prevent a man from retaining the money of or some benefit derived from another which it is against conscience that he should keep. Such remedies in English law are generically different from remedies in contract or in tort, and are now recognized to fall within a third category of the common law which has been called quasi-contract or restitution."

[23] GOFF & JONES, p. 16.

[24] [1978] A.C. 95.

[25] Ibid., at 104.

The Canadian courts, on the other hand, have been more willing to embrace the notion of a substantive body of law - the law of restitution- based in large part on a principle of unjust enrichment. The turning point came in 1954 in Deglman v Guar. Trust Co. of Canada.[26] There, the Supreme Court of Canada adopted the view that a right to be paid the fair value of services rendered could be based not on contract, but "on an obligation imposed by law."[27] This adopted what had been earlier said by Lord Wright in Fibrosa Spolka Akcyjna v Fairbairn Lawson Combe Barbour Ltd.,[28] that:[29]

> "The law implies a debt or obligation ... . [T]he obligation is as efficacious as if it were upon a contract. The obligation is a creation of the law, just as much as an obligation in tort. The obligation belongs to a third class, distinct from either contract or tort though it resembles contract rather than tort."

The subsequent Canadian case-law, and the body of substantive principles that can be derived from the wealth of cases, have been recently brought together and considered in two Canadian works, one by Fridman and McLeod,[30] and the other by Klippert.[31]

In all these works, the authors scan far and wide into the case-law in building their law of restitution, and in amassing examples of the operation of its fundamental principle of unjust enrichment. In the

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26 [1954] S.C.R. 725, [1954] 3 D.L.R. 785.

27 Ibid., at 794, per Cartwright J.

28 [1943] A.C. 32.

29 Ibid., at 62.

30 G.H.L. Fridman & J.G. McLeod, RESTITUTION (1982) (hereafter "FRIDMAN & McLEOD").

31 G.B. Klippert, UNJUST ENRICHMENT (1983) (hereafter "KLIPPERT"). See also G.B. Klippert, "The Juridical Nature of Unjust Enrichment", (1980) U.T.L.J. 356.

process, a wide range of rights, remedies, techniques, and causes of action, some common law in origin and some equitable, have been said to be explicable in terms of unjust enrichment and deserving of inclusion in the burgeoning law of restitution.

Subrogation, traditionally based on notions of "equity and justice", is one remedial technique that has been said to be explicable in terms of "unjust enrichment", and thereby suitable for assimilation into the new law of restitution. This can be supported by the fact that, historically, many of the situations in which subrogation has been used have been the source of various other quasi-contractual rights and actions, which in turn have formed the bulk of the newly formulated law of restitution. Furthermore, within this context, subrogation has been seen to be explicable less in terms of a "right", than in terms of a general restitutionary remedial technique or device, whereby the unjust enrichment in situations involving at least three parties - tripartite, in other words - can be remedied. Subrogation's particular distinguishing feature, and that which limits it, is, of course, its application only in tripartite situations.

Subrogation thus found its way in 1937 into the American Restatement of the Law on Restitution.[32] There, under the general heading "Constructive Trusts and Analogous Equitable Remedies", the authors formulated a general principle dealing with subrogation:

> "Where property of one person is used in discharging an obligation owed by another or a lien upon the property of another, under such circumstances that the other would be unjustly enriched by the retention of the benefit thus conferred, the former is entitled to be subrogated to the position of the obligee or lien-holder."[33]

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[32] American Law Institute, op.cit..

[33] Ibid., p. 653, para. 162.

In time, other, increasingly sophisticated attempts to explain and understand subrogation as a restitutionary remedial technique were advanced. Dawson, for example, touched on the subject in his work on unjust enrichment in 1951;[34] Goff and Jones covered it more fully in 1966 in the first edition[35] of their seminal work on the English law of restitution, and developed it later in the second and now third editions thereof in 1978,[36] and 1986,[37] respectively; Palmer reconsidered it in the American context in 1978 in his four volume treatise on restitution;[38] and Fridman and Macleod,[39] and Klippert[40] have now considered it in the Canadian context.

This development has inevitably brought with it both an opportunity and a need to reconsider the established categories, or "rights", of subrogation to determine the extent to which they can be reformulated in terms of restitutionary principles, and the implications that such a reformulation has for them.

One of the foremost of these "rights" of subrogation recognised in Anglo-American law is the surety's right of subrogation. This, as has

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34 J.P. Dawson, UNJUST ENRICHMENT: A COMPARATIVE ANALYSIS (1951), pp. 36-37.

35 R. Goff & G. Jones, THE LAW OF RESTITUTION (1st ed., 1966).

36 R. Goff & G. Jones, THE LAW OF RESTITUTION (2nd. ed., 1978), chap. 27.

37 GOFF & JONES, chap. 27.

38 Op. cit., vol. I, pp. 20-24.

39 FRIDMAN & McLEOD, chap. 14.

40 KLIPPERT, pp. 205-15.

already been outlined,[41] was probably the original situation in English common law in which the technique of subrogation was used. Consequently, it is one of the most established of the "rights" of subrogation. It could even be said to be the paradigm, or quintessential, tripartite case in which subrogation has been used. As such, one would expect it fully to reflect the restitutionary principles - in particular, the principle of unjust enrichment - upon which subrogation is said to be premised. The question whether this is so - whether the surety's right of subrogation does reflect and is explicable in restitutionary terms - is the central question that will be explored in this paper. The thesis of this paper is that subrogation in general is restitutionary in nature, and that this is fully reflected in the surety's "right" of subrogation in particular.

In attempting to answer this question, an immediate difficulty arises. It might be assumed, given the considerable heritage of the surety's right of subrogation, that the nature and content of the "right" is settled and readily understood. But this is far from being so. There is, as will be seen, a great deal of uncertainty surrounding the right. Part of this paper, therefore, is concerned with outlining the surety's right of subrogation, its nature, and its content.

In all, this paper is divided into four parts. In the first, the origins and general development of subrogation in English common law will be outlined. In the second, the general nature and content of the surety's right of subrogation will be outlined. In the third, the extent to which this right reflects and can be explained in restitutionary terms will be explored. And in the fourth, the thesis of this paper - that subrogation in

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41 Supra, pp. 2-3.

general is restitutionary in nature, and that this is fully reflected in the surety's "right" of subrogation in particular - will be tested by considering the extent to which the subrogation rights of parties to bills of exchange, who are considered to be sureties and quasi-sureties in certain respects, conform to this thesis.

PART I

THE ORIGINS AND GENERAL DEVELOPMENT OF SUBROGATION

Chapter 2

ORIGINS[1]

Subrogation as it presently exists in Canadian common law[2] originated in and was received from the common law of England. Its earlier origins in the English legal system itself have never been authoritatively established, however, and, to quote Goff and Jones[3], remain "obscure".[4]

Commonly, they are said to lie in Roman private law, or in later doctrines of its civil law inheritants.[5] Reference in this regard is

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[1] For a full discussion, see M.L. Marasinghe, "An Historical Introduction to the Doctrine of Subrogation: The Early History of the Doctrine - I & II", (1975) 10 Valp. U.L. Rev. 45, and 275.

[2] As distinct from the civil law system adopted by Quebec. Subrogation existed in the civil law of property and civil rights, based on the pre-conquest law of France, that was adopted by the Province of Quebec in 1774 pursuant to the provisions of the Quebec Act of that year. In 1866, when Quebec (or Lower Canada) enacted a Civil Code of property and civil rights, following the example of the French Code Napoleon and the Civil Code of Louisiana, subrogation was specifically provided for in the Code. See infra, p. 18, note 12. Subrogation as practised in the civil law of Quebec is not considered in extenso in this paper.

[3] Sir R. Goff & G. Jones, THE LAW OF RESTITUTION (3rd ed., 1986), (hereafter "GOFF & JONES").

[4] GOFF & JONES, p. 523. See also J. O'Donovan & J.C. Phillips, THE MODERN LAW OF GUARANTEE (1985), p. 503: "Roman law recognised a right of subrogation but the history of its reception into English law is largely uncharted. While it is clear that it was originally a creature of equity and that it primarily developed out of the principal-surety relationship, little else is known of its early history in the English legal system."

[5] See eg.: J. Story, EQUITY JURISPRUDENCE (2nd ed., 1893), p. 419, para. 635; H.H. Sheldon, THE LAW OF SUBROGATION (2nd ed., 1893), p. 2. See also John Edwards & Co. v Motor Union Insurance Co. [1922] 2 K.B. 249, at 252, per McCardie J.; R v O'Bryan (1900) 7 Can. Exch. 19, at 25, per Burbidge J.; Grace v Kuebler (1918) 38 D.L.R. 149, at 152-53, [1918] 1 W.W.R. 182, at 186, per Beck J.; Freeburg v Farmers' Exchange Bankers [1922] 1 W.W.R. 845, at 847, per Turgeon J.A. (Sask. C.A.). Numerous American decisions assert this view: see eg. Enders v Brune 4 Rand (Va.) 438, Houston v Branch Bank 25 Ala. 404, Knighton v Curry 62 Ala. 404, Shinn

usually made to the Roman law doctrine of cessio actionum[6] which enured to the advantage of sureties, or fideiussores[7]. This entitled a surety:

> "before payment, or, in general, issue joined, [to] require the creditor to transfer to him, by way of procuratio in rem suam, all his rights and securities against the debtor or other sureties. This demand ... [had to] be accompanied by offer of full payment, and ... [had to] be made before payment."[8]

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v Budd 14 N.J. Eq. 234. See generally on the relevant Roman law doctrines: F. Schulz, CLASSICAL ROMAN LAW (1951), pp. 499-502; W.W. Buckland, A TEXTBOOK OF ROMAN LAW FROM AUGUSTUS TO JUSTINIAN (3rd ed., revised, 1963), pp. 449-50; R.W. Leage, ROMAN PRIVATE LAW (3rd ed., 1961), pp. 344-45.

[6] More fully, beneficium cedendarum actionum. The relevant passage in the Digest - Digest 46-1-17 - has been translated as follows: "He to whom a creditor makes over a debt is substituted to the right, and he acquires, together with the credit, the mortgage and privileges which are annexed to it, whether the assignment be made for a valuable consideration or gratis. For, although it be true that the payment extinguishes the debt, and that it seems, for that reason, that the creditor cannot transmit to another a right which is extinguished in his person by the payment, yet the assignment, which is made at hte same time, has the same effect as if the creditor had sold his right to him who pays him. And, as to the effect of the assignment, it is the same thing to him who pays for the debtor, whether it be the person who is bound jointly with him for the debt, or his surety, or a third person." The Civil Law (1 Domat, b.3, s.6, art.1). According to Marasinghe, this doctrine "... bore the closest resemblance to subrogation, as known in England, and ... had been regarded as the precursor of subrogation...", loc. cit., I, p. 50.

[7] Roman law also recognised other forms of suretyship, including adpromissio (where two or more persons jointly made a promise to pay or perform some other obligation) and mandatum qualificatum (whereby a man who requested another to lend money to a third person was held to promise repayment himself if the third person made default. This differed from fideiussio in several respects: most importantly, whereas the fideiussor was liable with the principal debtor for the same debt, the mandator was liable on a separate contract. Payment by the mandator did not therefore, as it did in fideiussio, automatically discharge the creditor's claims against the person to whom the money was lent; thus the mandator, even after payment, could still demand that the creditor's claims against the debtor should be transferred to him). See Buckland, op. cit., pp. 445-52; Leage, op. cit., p. 369.

[8] Buckland, op. cit., p. 449. Buckland also noted, op. cit., p. 449, that the demand "was never implied".

Leage explained the nature of this action in terms more closely approximating those associated with subrogation in English law:[9]

> "a surety called upon to pay the whole debt might ... require the creditor before payment to hand over to him all his remedies (including mortgages to secure the debt), and so, standing in the place of the creditor, sue the principal debtor for the amount paid, or the other sureties for their fair share".

The demand had to be made before payment was effected because, as Buckland explains,[10]

> "[t]here was in this system an obvious difficulty. If the creditor was paid, he had no longer any rights to cede, and though he ceded them before payment, the payment would destroy them. The difficulty was met by treating the surety who paid, not as discharging the debt, but as buying it."[11]

This mechanism for investing sureties with rights and remedies against both the principal debtor and also co-sureties eventually found its way into most civil law systems. It exists, for example, in the Civil Code of Quebec,[12] and in the Civil Code of Louisiana in America.[13] Neither code,

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9 Op. cit., p. 345.

10 Op. cit., p. 449.

11 See also Leage, op. cit., p. 345: "he was regarded, not as having paid the debt, but as having purchased the right of the creditor. The cession of actions against the principal debtor had to be made before the surety's payment because that payment would automatically have extinguished all the creditor's rights against the principal."

12 See generally Articles 1154-57 of the Civil Code, headed "Of payment with subrogation" (derived primarily from Articles 1249-52 of the earlier French Code Napoleon). These provide for "subrogation in the rights of a creditor" (Art. 1154). The Code divides subrogation into two types: "conventional" (essentially subrogation by agreement)(Art. 1155), and "legal" (essentially subrogation by operation of law without the consent of the creditor)(Art. 1156). The surety's rights of subrogation are expressly provided for in Art. 1155(1) and Art. 1156(3). Art. 1157 recognises that subrogation may take effect both against principal debtors and also other sureties (see also Art. 1118 re subrogation against sureties).

however, limits subrogation to suretyship cases; both extend subrogation more generally to a variety of situations. And, importantly, both recognise the mechanism by the name "subrogation".

These Roman and civil law doctrines are often said to be the intellectual origins of subrogation in English law. It is difficult completely to deny this connection; if nothing else, it seems probable that the term "subrogation" itself was derived from the civil law.[14] Beyond this, however, the view that English law owes an intellectual debt to Roman or civil law in respect of subrogation cannot be asserted with confidence. Not only is the textual evidence for this "slight", as Goff and Jones remark,[15] but, more significantly, there is arguably a fundamental difference between subrogation as it developed in English law and subrogation in Roman and civil law. This relates to the manner in which the conferral of rights and remedies inherent in subrogation is effected. As Marasinghe has pointed out,[16] although:

> "both doctrines impart a transfer of rights from one person to another ... [a]t common law, subrogation applies ipso jure without any

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13 See generally Articles 2159-62 of the Louisiana Civil Code. These articles, like those of the Quebec Civil Code, are virtually literal translations of the corresponding articles of the French Code Napoleon (Arts. 1249-52); they accordingly provide for conventional and legal subrogation. Subrogation in Louisiana is considered to be a substantive right created by the civil law; equitable subrogation does not exist in the state, see Fidelity-Phenix Fire Insurance Co. of New York v Forest Oil Corp. (1962) 141 So. 2d 841; Home Ins. Co. v Highway Ins. Underwriters (1953) 222 La. 540. See also J.T. Hood, Jr., "Subrogation", in ESSAYS ON THE CIVIL LAW OF OBLIGATIONS (ed. by J. Dainow), p. 174 et seq.

14 See supra, p. 5, note 13, for reference to a civil law case from the courts of Quebec which may have influenced the adoption of the term "subrogation" in English and Canadian law.

15 GOFF & JONES, p. 523.

16 Marasinghe, loc. cit., II, pp. 298-9.

> requirement of any express agreement to transfer rights. In contrast, ... in cessio actionum an express agreement to transfer rights must always precede the payment."

In his view, there is no clear or acceptable explanation "to show how the doctrine of subrogation [in English law] became capable of effecting an ipso jure succession to another's rights...",[17] without prior express demand and cession. "Legal" subrogation - in other words, subrogation by operation of law without any express agreement to transfer rights - is, however, known to the civil law.[18] This came about, it has been said,[19] when:

> "a merger of [the right of beneficium cedendarum actionum] occurred with the rights under negotiorum gestio of an outsider who paid the debt and those under mandate when the creditor (mandatory) had loaned money under a mandate from the surety (mandator). This resulted in the concept of the automatic legal subrogation of the surety to the creditor's rights under specified circumstances, a position adopted by modern civil codes."

This might provide the explanation sought by Marasinghe and other writers. Nonetheless, the uncertainty that exists in this regard has promoted the suggestion that subrogation in English law may well be a home-grown product of the English common law legal system, separate from, although similar in operation to, the doctrine adopted by European civil law legal systems.[20] Its evolution, on this view, is attributable more to

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17 Ibid., I, p. 54.

18 See supra, pp. 18-19, notes 12 & 13.

19 P.K. Jones, Jr., "Roman Law Bases of Suretyship in Some Modern Civil Codes", (1977) 52 Tul. L.R. 129, p. 135.

20 See eg., Marasinghe, loc. cit., Part I, p. 45; D.G. Maclay, "Theory and Application of the Doctrine of Subrogation", (1885-86) 2 The Columbia Jurist 38, p. 39. There are also a number of comments in early American decisions which refer to the parallel development of the doctrine in both the common and civil law legal systems: see eg. Cheeseborough v Millard (1815) 1 Johns. Ch. 409, at 413, per Chancellor Kent: "This

the fact that it is an obvious means of effecting an equitable result in tripartite situations, and presumably occurred to English judges in that light, than to a perception that it was a relevant doctrine of Roman or civil law to adopt into the English legal system for this purpose.

It is not intended to explore this issue further in this paper. What is more important, it is submitted, is that once the technique of subrogation gained a foothold in English law, its subsequent application and development was effected with only limited overt reference to possible ancestral roots in Roman or civil law.[21]

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doctrine of substitution, which is familiar to civil law ... and the law of those countries in which that system essentially prevails ... is equally well known in the English Chancery." See also Hayes v Ward (1819) 4 Johns. Ch. 123, at 130, per Chancellor Kent; and Stevens v Cooper (1815) 1 Johns. Ch. 425, at 431-32, per Chancellor Kent.

[21] Cf., the American courts where references to the doctrine of subrogation in the civil law were much more frequent. See the cases noted supra, pp. 16-17, note 5.

Chapter 3

THE GENERAL DEVELOPMENT OF SUBROGATION

STEPS AND OBSTACLES[1]

Subrogation is generally thought to have been first invoked in the English legal system by the Chancellor in aid of sureties around the beginning of the seventeenth century. At the time, sureties were undoubtedly favoured by the law. One commentator has noted:[2]

> "In former times the surety was in the typical instance a friend of the borrower, often more generous than discreet, who assumed gratuitously the collateral obligation and thereby subjected himself to possibility of financial loss. In his favour, therefore, all doubts of construction of the contract of suretyship were resolved. For his relief the chancellor imported from the civil law the remedy of subrogation."[3]

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[1] See generally Sir R. Goff & G. Jones, THE LAW OF RESTITUTION (3rd ed., 1986) (hereafter "GOFF & JONES"), p. 532 et seq; G.H.L. Fridman and J.G. McLeod, RESTITUTION (1982) (hereafter "FRIDMAN & McLEOD"), p. 391 et seq.

[2] "The Extent of the Subrogee's Remedy", Note in (1925-26) 35 Yale L.J. 484. See also Holland Can. Mge Co. v Hutchings [1936] S.C.R. 165, at 172, [1936] 2 D.L.R. 481, at 488.

[3] Ibid., p. 484. The reference to the civil law as the source of subrogation can be attributed to the fact that the commentator is American; as noted, supra, note 5, American law draws a much closer link between common law and civil law notions of subrogation. The commentator went on, pp. 484-5, to note an interesting change in the attitude of the courts towards sureties, in America at least: " With the rise of modern business methods, the prevailing notions of fairness have changed, and some of the rules relating to suretyship have been modified. The typical surety today in business transactions of any size is the surety company, organized for profit and, of course, allowed to exact it in the form of premiums. Inasmuch as the surety company is more like an insurer than an ancient surety, ... the rule of contract construction has been reversed as to it, all doubts being construed against the surety company". See also D.M. Kerly, AN HISTORICAL SKETCH OF THE EQUITABLE JURISDICTION OF THE COURT OF CHANCERY (1890), pp. 251-3.

Social and economic changes in England at the time also provided a powerful incentive for the judicial development of new rights and remedies. As another commentator has pointed out:[4]

> "A no less powerful reason for ... subrogation's slow development was the late rise of commercial activity; for undoubtedly, the doctrine received its greatest impetus in the necessity of a relief from the complexities and hardships arising from the various relations of guarantor, surety and creditor to each other, increased as they must have been by the inflexible rules of the early law."

In combination, these forces for change induced the Chancery in 1637, in Morgan v Seymour,[5] to confer on a surety an equitable right to the assignment of securities upon payment of the guaranteed debt. This particular right - to securities - is generally regarded as being at the centre of the surety's "right of subrogation".[6] Morgan v Seymour thus serves as a seminal case in the development of subrogation in English law.

Similar forces on later occasions led the Chancery, step-by-step, to apply the technique of subrogation in favour of persons other than sureties - first, in favour of persons who lent money to married women and infants to purchase necessaries,[7] then importantly in favour of insurers after

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4 D.G. Maclay, loc. cit., p. 39.

5 (1637) 1 Chan. Rep. 120, 21 E.R. 525.

6 See discussion infra, p. 56 et seq..

7 This use of subrogation was recognised in two chancery cases early in the eighteenth century, namely, Harris v Lee (1718) 1 P. Wms. 482, 24 E.R. 482; and Marlow v Pitfield (1719)1 P. Wms. 588, 24 E.R. 516. The common law courts had earlier denied recovery by way of assumpsit of a loan used to purchase necessaries; see Darby v Boucher (1693) 1 Salkeld 279, 91 E.R. 244; and Earle v Peale (1712) 1 Salkeld 386, 91 E.R. 336.

payment to the insured,[8] and eventually to several other categories of deserving plaintiff.[9]

In each case, the step-by-step extension of the use of subrogation was primarily undertaken by the Chancery employing broad notions of "natural justice" and "equity" as the justification for doing so. As a result, subrogation in English law is generally regarded as "equitable" in origin and nature.

Recording the course of development of subrogation in the English legal system is not, however, free from difficulties. First, as has already been suggested,[10] there was no great rush to develop the scope and use of the technique in the years immediately following its initial recognition. Instead, the early part of its development in the Chancery was relatively slow. It appears that it was only with the quickening of the pace of the industrial revolution in England[11] that the creative hand of the Chancellor became increasingly adept at using subrogation where it had not previously been used.

Secondly, the Chancery's expanding use of subrogation was not by any means a product of planning and foresight. Although a court occasionally applied one instance of subrogation, by analogy, to another similar

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8 See Randal v Cockran (1748) 1 Ves. Sen. 98, 27 E.R. 916. The common law courts recognised the use of subrogation in this context in Mason v Sainsbury (1782) 3 Doug. K.B. 61, 99 E.R. 538. See also London Ass. v Sainsbury (1783) 3 Doug. K.B. 245, 99 E.R. 636.

9 See infra, p. 27.

10 Supra, p. 3.

11 For a comprehensive, and illuminating, discussion of the effects of the industrial revolution on the English legal system - and, in particular, the law of contract - see P.S. Atiyah, THE RISE AND FALL OF FREEDOM OF CONTRACT (1979).

situation,[12] more commonly the technique was simply used, without overt recognition of that fact, as and when necessary to achieve an equitable result in the particular case before the court. Subrogation's development was, in this respect, more piece-meal than planned; as a result, it came to be applied in a host of diverse circumstances often bearing little apparant factual similarity to each other. As a further result, discussions of subrogation can nowadays be found in a wide range of contexts, including suretyship,[13] insurance,[14] trusts,[15] mortgages, and company law.

Thirdly, although subrogation was broadly "equitable" in nature, the haphazard nature of its development did not readily promote or facilitate either analysis of its theoretical underpinings, or unification of the various instances of subrogation.[16] Instead, subrogation is largely treated as simply an historical fact. Only relatively recently, it is submitted, with the recognition and development of a law of restitution, has this begun to change to any marked degree.

Fourthly, the course of subrogation's development was complicated by the fact that subrogation did not remain the sole preserve of the Chancery.

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12 Eg., early cases on the use of subrogation in favour of persons who had made ultra vires loans to a company which then used the loan to pay off other earlier intra vires loans reasoned by analogy to the cases allowing subrogation to a lender of money to purchasers of necessaries.

13 See texts referred to infra, p. 33, note 1.

14 See eg. S.R. Derham, SUBROGATION IN INSURANCE LAW (1985).

15 See eg. Meagher, Gummow, & Lehane, EQUITY - DOCTRINES AND REMEDIES (2nd ed., 1975).

16 One of the more comprehensive treatments of the subject amongst equity writers is to be found in Meagher, Gummow, & Lehane, op. cit., chap. 9, but even this merely highlights the difficulties attendant on subrogation. One early exception was the American writer, Sheldon, op. cit., who published the first edition of his work on subrogation in 1882.

Subrogation, or rights of similar effect, were eventually recognised and adopted by the common law courts in a number of cases. Accommodating subrogation within the strictures of common law thinking, however, posed problems for common law judges, given the avowedly equitable nature of the technique. The response of the common lawyers was to subject subrogation to a transformation of sorts. Instead of being a technique of relief whereby one party, A, for equitable reasons was "stood in the place (or shoes) of" another, B, so as to obtain the benefit of the latter's rights, remedies, and securities against a third party, C, against whom A may or may not have had concurrent rights in equity or common law, subrogation in the eyes of the common lawyers became a substantive right - a "right of subrogation". Furthermore, it was commonly said that the right arose by way of an "implied contract" between A and B, or A and C. In this sense, therefore, the common law courts went a considerable way towards transforming the equitable technique of subrogation into a quasi-contractual "right" of subrogation. This inevitably added to the uncertainty and theoretical confusion surrounding subrogation.

These difficulties still largely bedevil discussions of the theory and nature of subrogation. Subrogation is as a result still generally approached by way of the identification and elucidation of the general categories of case in which the technique of subrogation has been used to provide a deserving party with a remedy. Even restitution writers, in sifting through the various rights of subrogation with a view to constructing a "restitutionary" explanation of subrogation, have more often than not found themselves constrained to approach the subject in this way.

Goff and Jones, for example, identify four "established" categories of use, namely:

(i) sureties;

(ii) indorsers of bills of exchange;

(iii) insurers; and

(iv) creditors of a business carried on by a trustee or personal representative;[17]

and two further general categories, the second of which they concede is less clearly accepted as a category of use of subrogation:

(v) authorised borrowings: the discharge of the borrower's valid liabilities; and

(vi) unauthorised borrowings: the discharge of the borrower's valid liabilities.[18]

Fridman and McLeod, on the other hand, in the most detailed discussion to date of subrogation in the Canadian law of restitution,[19] adopt Goff and Jones's first four categories, but classify the fifth and sixth categories according to the two specific factual situations historically giving rise to them:

(v) loans to infants, lunatics, and married women to purchase necessaries; and

(vi) invalid loans to corporations used to discharge other valid liabilities of the corporation.[20]

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17 GOFF & JONES, p. 533 et seq.

18 Idem.

19 FRIDMAN & McLEOD, chap. 14.

20 Ibid., p. 391 et seq.

Other writers adopt other systems of classification, according to their particular view of subrogation.[21]

But even when the topic of subrogation is approached in this way, many of the difficulties already identified seem to persist. Is subrogation a "right"? Or a remedy? Does it necessarily entitle a party to securities and priority? And so on.

One of the principal reasons for these continuing difficulties, it is submitted, is the failure to recognise that the expression "subrogation", as used in the cases and legal literature, serves a number of purposes. In particular, it can be seen to refer variously to at least three aspects of the law regarding subrogation. First, it is used to refer to the remedial technique itself of "standing one person in the place (or shoes) of another" to endow the former with the rights and remedies of the latter (or some of them) against a third party. Secondly, it is used to refer to the entitlement to have the remedial technique of subrogation used or applied in one's favour. Here, it is appropriate to talk of a "right of

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[21] Birks, INTRODUCTION TO THE LAW OF RESTITUTION (1985), pp. 93-98, takes a different tack. He suggests that for the purposes of the law of restitution, it is not even legitimate to treat subrogation as a separate subject. In his view it is "in the nature of a metaphor which can be done without", op. cit., p. 93. He explains this further through the following illustration: "If I pay you £5000 and you use £2000 of it to pay off your overdraft, then a conclusion in the form and language of subrogation will be that I am subrogated to the claim which the bank had against you. I stand where the bank stood; and you, who are sitting on a surviving enrichment of £2000, in the form of a burden removed which would otherwise still impend, will thus be compelled to give up that enrichment. The metaphorical nature of this description is brought out by the fact that exactly the same conclusion can be expressed without speaking of any substitution. It could be said simply that I acquire a right having characteristics and content identical to that formerly enjoyed by the bank. The difference is between the language of substitution and the language of comparison: 'the bank's right' and 'a right like the bank's'. The notion of a substitution is vivid. But strictly speaking it is unnecessary", op. cit., pp. 94-94.

subrogation", or a " right to subrogation". And thirdly, it is used to refer to the actual body of rights and remedies made available through the use of the remedial technique of subrogation.

The second and third of these uses of the expression "subrogation" are themselves variable. Thus, the entitlement, or "right", to subrogation may be either contractual, or it may be essentially restitutionary in nature. That is to say, it may be either the product of agreement between the parties, whether express or implied, or it may be simply an expression of the existence of unjust enrichment in a particular tripartite situation. In this latter case, once the existence of unjust enrichment in a tripartite situation has been identified, it may be that restitution of the unjust enrichment can be effected simply through the conferral of direct rights or remedies on the party at whose expense the enrichment was obtained. But it may be that direct rights and remedies will be ineffective. In this case, since the situation is tripartite in character, the remedial technique of aubrogation may be applied as the best, or perhaps the only means of effecting restitution of the enrichment unjustly retained.

Equally, the actual body of rights and remedies available as a result of using the technique of subrogation may vary in each case. In particular, it may include only personal rights or remedies of the person whose shoes are filled by another; or it may also include rights of security or priority. The particular rights and remedies available in any particular case, it is submitted, will or at least should depend on and correlate to the facts of the particular case. If an agreement existed, then one should ask what was agreed regarding subrogation and the rights and remedies available by virtue of its application. If there was no agreement, then one

should ask questions such as "what was the nature of the benefit conferred?", "are there other interested parties?", and so on. The facts, in other words, will, it is submitted, be highly relevant in determining the actual body of rights and remedies available through use of the remedial technique of subrogation. Furthermore, there is no necessary distinction in this regard between subrogation as a contractual "right", and subrogation as an expression of unjust enrichment. Where, for example, it is agreed that one party, A, shall be "entitled to subrogation", this may mean that A is entitled to all the rights and remedies of the subrogee, no matter what their nature. In this case, the actual body of rights and remedies rendered available to A is not limited by the perceived extent of unjust enrichment in the circumstances. But where this is not clear, then, it is submitted, the actual body of rights and remedies available becomes largely a matter of common law; in other words, it becomes largely a matter of determining the body of rights and remedies that have over time come to be accepted as appropriate to remedy the injustice - the unjust enrichment - perceived to exist in the situation warranting subrogation. Thus, even where the entitlement to subrogation is contractual, it will often, it is submitted, be the underlying unjust enrichment in the situation under consideration that will dictate the rights and remedies available to the aggrieved party.

If these distinctions are drawn and kept in mind, then, it is submitted, many of the apparent difficulties surrounding subrogation become more readily explicable. And, equally importantly, the essential restitutionary nature of subrogation can be seen more clearly. In Parts III and IV of this paper, these propositions will be considered in relation to

the surety's "right" of subrogation.

PART II

SURETYSHIP AND SUBROGATION

Chapter 4

SURETYSHIP[1]

A. Introduction

When one person, A, promises to answer to another, C, for the due performance of an obligation of a third, B, in the event that B fails to perform that obligation as required, then A is in English[2] and Canadian[3] law a "surety", and the relationship between him or her and B and C is one of "suretyship".[4] Commonly, B and C are debtor and creditor respectively, and A's promise is accordingly to answer for B's debt. Promises of this type were held to be enforceable against A early on in English legal

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[1] See generally on the law of suretyship: K.P. McGuinness, THE LAW OF GUARANTEE (1986) (hereafter "McGUINNESS"); D.G.M. Marks & G.S. Moss, ROWLATT ON THE LAW OF PRINCIPAL AND SURETY (4th ed., 1982)(hereafter "ROWLATT"); T.D. Putnam, SURETYSHIP (1981); J. O'Donovan & J.C. Phillips, THE MODERN CONTRACT OF GUARANTEE (1985). An early English text is H.A. de Colyar, THE LAW OF GUARANTEES (3rd ed., 1897). American texts include H.W. Arant, HANDBOOK ON THE LAW OF SURETYSHIP AND GUARANTEE (1931); E.A. Arnold, OUTLINES OF SURETYSHIP AND GUARANTY (1927); and L.P. Simpson, HANDBOOK ON THE LAW OF SURETYSHIP (1950).

[2] See eg., ROWLATT, p. 1: "A surety may be defined as one who contracts with an actual or possible creditor of another to be responsible to him by way of security, additional to that other, for the whole or part of the debt."

[3] See McGUINNESS, p. 1: "In its simplest form, a guarantee is a promise by one person to answer for the due performance of the obligation of another person (whether imposed by law or contract) in the event that the other person fails to perform that obligation as required. In most, but by no means all, cases the guaranteed obligation will be a debt." Although McGuinness gives this as a definition of "guarantee", he uses the term "surety" to refer to the person undertaking the obligation to answer for another, McGUINNESS, p. 22.

[4] "Guarantor" and "guarantee" may equally be used. For discussion of these various terms, see McGUINNESS, pp. 21-27.

history. Indeed, they were were among the earliest forms of contractual obligation recognised in English law.[5] At the same time, as has already been seen,[6] these promisors - "sureties" - were favoured by the law. Consequently, suretyship proved a fertile ground for the development of rights and remedies in English law.

The range of rights and remedies available to a surety is considerable. It includes rights and remedies before the surety is called upon to pay or perform, rights and remedies when called upon to pay or perform, and rights and remedies upon or after payment or performance. It includes rights and remedies against (a) the person whose obligation the surety has promised to answer for - known as the "principal"; (b) the person who is entitled to payment or performance by the surety - known as the "creditor"; and (c) other persons who have also promised, along with the surety, to answer for the principal - known as "co-sureties".

One right in particular is the "right of subrogation".[7] Broadly speaking, this entitles A, upon performing B's obligation to C, to "stand in C's place (or shoes)" and exercise for A's own benefit all the rights and remedies, including securities, possessed in law by C against B at the time A pays or performs the guaranteed duty. The essential purpose of this right is to assist A in obtaining restitution from B of the benefit conferred on B by A in performing B's obligation to C. This right is not, however, always expressed in these terms. Often, for example it is

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5 Holdsworth, HISTORY OF ENGLISH LAW (2nd ed.), p. 185 et seq. See also Loyd, "The Surety", (1917) 66 U. Pa. L. Rev. 40.

6 Supra, p. 22.

7 Subrogation is usually spoken of in this context as a "right" of the surety, rather than as a technique of rights conferral.

expressed as being one of the contractual rights arising expressly or impliedly from the contract of suretyship between the parties. It is also often linked with certain other rights possessed by the surety, especially those of indemnification or reimbursement, and contribution.

In this Part, this "right" of subrogation, its nature and its scope, will be examined. Before doing so, however, it is first necessary to consider briefly two related matters. The first concerns the meaning of the expressions "surety" and "suretyship"; the second concerns the other two basic rights of a surety upon payment or performance, namely reimbursement and contribution. These latter two rights, it is submitted, are closely linked at a juridical level to subrogation.

B. Meanings: "sureties" and "quasi-sureties"

Where A makes a promise along the lines of that outlined above, it gives rise to a relationship that is essentially contractual in nature. It arises in a contractual setting, and depends upon an express or implied agreement between three persons: (1) the promisor (the "surety"), (2) the person whose obligation he or she has agreed to answer for (the "principal debtor"), and (3) the person entitled to performance of that obligation (the "creditor"). The suretyship thereby arising and the various rights enjoyed by the parties to it derive in essence from that agreement, and may be considered terms of it, either express or implied.

Relatively early on, however, English lawyers recognised that there could be persons who, for various legal or factual reasons, become liable to perform the obligation of another even though they have not expressly

promised to do so. These persons, it was realised, are in a position analogous to that of a contractual surety strictly speaking, even though their liability is not a product of a tripartite suretyship agreement. It was also eventually realised that these persons - who can be termed "quasi-sureties" to distinguish them from true contractual sureties - are no less deserving of the assistance of the law than contractual sureties. Accordingly, English law came to confer the rights of a "contractual surety", or at least rights analogous thereto, upon these "quasi-sureties", not upon the basis of contract, but rather upon equitable principles, or, later in history, quasi-contractual notions (insofar as a fictional agreement between the parties could be "implied" based upon "request" for example).

Discussion of the "rights" of "sureties", including the right of subrogation, is not, therefore, limited to the rights of contractual sureties strictly speaking. It extends to and encompasses both sureties strictly speaking, and also these "quasi-sureties", to adopt that term. This has been clear since at least the late nineteenth century, and the judgment of the House of Lords in Duncan, Fox, & Co. v North & South Wales Bank.[8] In that case, Lord Selborne L.C., delivering the leading speech, outlined three general classes of undertaking giving rise to suretyship rights, including the right of subrogation:

> "(1.) Those in which there is an agreement to constitute, for a particular purpose, the relation of principal and surety, to which the creditor thereby secured is a party; (2) Those in which there is a similar agreement between the principal and surety only, to which the creditor is a stranger; and (3) Those in which, without any such contract of suretyship, there is a primary and a secondary liability of two persons for one and the same debt, the debt being, as between

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[8] (1880) 6 App. Cas. 1.

> the two, that of one of those persons only, and not equally of both, so that the other, if he should be compelled to pay it, would be entitled to reimbursement from the person by whom (as between the two) it ought to have been paid."[9]

The rights enjoyed by each class of surety, however, are not the same, as was emphasised by Lord Selborne L.C.[10] A surety in the first class enjoys the rights of a surety in full, for this class of suretyship is based upon a tripartite agreement and is clearly contractual in nature. The rights themselves can also be said to be contractual in nature, attaching as they do as express or implied terms of the suretyship agreement. This class of suretyship provides the paradigm case.

"Suretyships" of the second and third classes - or "quasi-suretyships" - do not necessarily enjoy the same body of rights.[11] Lord Selborne L.C. illustrated this by reference to the rights of the surety against the creditor, in particular in relation to the protection of securities.[12] Since the creditor is not a party to the agreement or circumstances giving rise to the second and third classes of suretyship, other than as the immediate recipient of payment or performance, the quasi-surety could not per se assert the same rights against the creditor, as attached by virtue of the agreement in the first class, particularly prior to payment or

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9 Ibid., at 11.

10 Ibid., at 11-12.

11 Ibid., at 11, per Lord Selborne L.C.: "It is, I conceive, to the first of these classes of case, and to that class only, that the doctrines laid down in such authorities as Owen v Homan [(1851) 3 Mac. & G. 378, 10 E.R. 752], Newton v Chorlton [(1853) 10 Hare 646, 68 E.R. 1087], and Pearl v Deacon [(1857) 24 Beav. 186, 1 De G. & J. 461, 53 E.R. 328] apply in their full extent."

12 This right is discussed more fully infra, p. 56 et seq..

performance.[13] Something more was necessary before subrogation and other rights comparable to those of the contractual surety arose in favour of these quasi-sureties. The additional requirement in the second class was seen by Lord Selborne L.C. to be the giving of notice to the creditor of the suretyship agreement between the surety and the debtor giving rise to the suretyship.[14] In the third class, it was rather seen to be something in the circumstances themselves that led to liability.

In neither the second nor the third classes of case do the rights derive directly from contract. This is clearly so in relation to the third class since it arises independent of any agreement. It is also true of the second class, even though there is an agreement, since the creditor is not a party to it. In both cases, in Lord Selborne L.C.'s view, the conferral of rights derives primarily from equitable considerations arising from the circumstances of the case.[15]

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[13] (1880) 6 App. Cas. 1, at 11, per Lord Selborne L.C.: "If, so far as the creditor is concerned, there is no contract for suretyship, if the person who has (in fact) made himself answerable for another man's debt is, towards the creditor, no surety, but a principal, then I think that the creditor would not be subject to those special obligations which were described by Lord Truro in Owen v Homan [ibid., at 396-97], and would not, generally, have his powers of dealing with securities circumscribed and restricted in the manner described by Vice-Chancellor Wood in Newton v Chorlton [ibid., at 651], and by Lord Romilly and the Lords Justices in Pearl v Deacon [ibid.]."

[14] Ibid., at 12: "It is, however, consistent with this that the person who, as between himself and another debtor, is in fact a surety (though the creditor is no party to that contract of suretyship), has, against that other debtor, the rights of a surety; and that the creditor, receiving notice of his claim to those rights, will not be at liberty to do anything to their prejudice, or to refuse (when all his own just claims are satisfied) to give effect to them."

[15] Idem: "In such cases the equity is direct in favour of the surety-debtor against the principal debtor; but it affects the creditor towards whom thay are both principals only as a man who has notice of the obligations of one of his own debtors towards the other. As between the two

More specifically, in the second class, although A and B may be principal and surety inter se, they are initially joint debtors from the creditor C's point of view. This changes, however, once A and B give notice of the agreement between them resting primary responsibility for payment of the debt or performance of the duty upon the former; the creditor upon notice is obliged to recognise that allocation of responsibilty. "[T]he equity", said Lord Selbourne L.C.,[16] "is direct in favour of the surety-debtor against the principal debtor; ... it affects the creditor ...". This takes effect only from the time of notice, and thus may entail the conferral of rights on the surety against the creditor even prior to payment or performance.[17]

The conferral of rights in the third class of suretyship clearly does not arise from an agreement, not even one between the principal debtor and surety. Indeed, the persons within this third class might bear only a limited resemblance to contractual sureties strictly speaking. Instead, the conferral of rights arises from the interplay of two factors: first, the fact that there is something in the circumstances of the case, other than an agreement, which legally compels the "quasi-surety" to pay the debt or perform the obligation of another; and, secondly, the fact that there is

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debtors, the 'established principles of a Court of Equity,' ... are fully applicable." Although notice of the creation of a suretyship must be given in relation to the second class, it need not necessarily be given prior to the agreement inter se: Rouse v Bradford Banking Co. [1894] A.C. 586.

16 Idem.

17 The same analysis can be applied to the first of Lord Selborne L.C.'s classes of suretyship. It is not the contract per se, in other words, that gives rise to the surety's rights against the various parties, but rather the fact of notice to them of the suretyship, this notice being a necessary consequence of the fact that all the parties parties to the contract of suretyship. See eg., ROWLATT, p. 3.

something in the circumstances - perhaps the same thing, but again something other than an agreement - which dictates that as between the two of them, the one who fails to perform or pay the debt was the one who bore the primary liability for it, while the other who is compelled to pay or perform bore only secondary responsibility. It is these two factors that give rise to the equity in favour of the "quasi-surety" of the third class entitling him or her to the rights of a surety against the "principal debtor" and the "creditor", or at least to rights analogous thereto. As Lord Selbourne L.C. stated:[18] "these principles of Equity [applicable to the second class] are not less applicable to cases of the third class...". Importantly, this third class of case requires payment or performance under "legal compulsion". Not until then does the "equity" arise as between the "quasi-surety" and the "principal debtor", and the creditor.[19] Thus, it is clear that the rights of this third class of surety do not include rights against the principal or creditor prior to conferral of the benefit on the principal.

It is thus the "equities" of the situation, and not contract, it is submitted, that dictates the extent to which quasi-sureties - those in the second and third of Lord Selborne L.C.'s classes - enjoy rights that are the same as or analogous to those of truely contractual sureties.

Thus, discussion of "suretyship" and the "rights" attaching to it, including the "right of subrogation", has a broad sweep to it. It includes

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[18] (1880) 6 App. Cas. 1, at 13.

[19] It can, of course, be said that there is no notice of the "suretyship", or "quasi-suretyship", to the creditor until the fact of payment or performance by someone other than the person against whom the creditor has the most direct or immediate right of payment or performance.

not only those rights which attend contractual relationships as an incident of the contract; but also rights attending non-contractual relationships- "quasi-suretyships" - as an incident of the "equities" of the case.

Furthermore, it is possible for there to be more than one surety or "quasi-surety" in a given situation. A simple example would be if two persons, A1 and A2, jointly and severally promise to answer to C for the due performance of the obligations of the principal, B. In this case, both A1 and A2 are sureties of B's obligation, and C may accordingly seek performance from either or both of them. Vis-à-vis each other, A1 and A2 are said to be "co-sureties", and their rights are consequently slightly different to those of a single surety or "quasi-surety". In particular, as is discussed below,[20] while A1 and A2 will each have the same rights against the principal, B, and the creditor, C, as sureties or "quasi-sureties" normally do, each will also have a right of contribution from the other in the event that one only of them is required by C to perform the obligation jointly and severally guaranteed by them.

It is also possible for there to be different levels of suretyship or "quasi-suretyship" - for someone to be a "surety to a surety". If, for example, A has promised to answer to C for the performance of B's obligation, and is thus a surety of B's obligation, and D then promises to answer to C in the event that A fails to perform, D is not considered to be a co-surety with A of B's obligation; rather, D is considered to be a surety of A's obligation as surety - a "surety for a surety". As between A and D, A is in other words considered to be D's principal, and D will

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[20] Infra, p. 46 et seq..

accordingly be entitled to the normal rights and remedies of a surety against his or her principal.

The possibility of there being "co-sureties" or "sureties for sureties" in a given situation, or indeed both at once, and the consequential effect on the rights and remedies of the various parties, is something that must additionally be taken into account in the discussion of "suretyship" and the "rights" attaching to it, and endows the discussion with an even greater sweep.

C. Reimbursement and Contribution

When a surety or quasi-surety is called upon or compelled by the creditor or the circumstances of the case to answer for the principal debtor, and does so[21] - usually by paying money to the creditor - he or she has three general rights. Subrogation is only one of them. The other two are, broadly, the rights of reimbursement and contribution. As there is a considerable degree of overlap both in operation and in theory between these rights of reimbursement, contribution, and subrogation, it will help the discussion of subrogation to outline the nature and theoretical underpinings of reimbursement and contribution before considering subrogation in some detail.

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[21] A surety also has related rights (a) even before being called upon to perform, and (b) after being called upon to perform but before actual performance of his undertaking. See generally: McGUINNESS, p. 193 et seq; ROWLATT, p. 131 et seq; Putnam, op. cit., p. 79 et seq; O'Donovan & Phillips, op. cit., p. 404 et seq.

(i) Reimbursement

The surety's right of "reimbursement", "indemnity", "indemnification", or "recoupment",[22] as it is variously known,[23] is the fundamental right of a surety upon payment or performance. It entitles the surety or quasi-surety to be compensated by the principal debtor to the extent of the payment made by the surety to the creditor on the principal debtor's behalf pursuant to the suretyship obligation. It is a direct right of recovery against the principal debtor. Consistent with the distinction between contractual and restitutionary suretyships, this right may be contractual or restitutionary in origin.[24] It is contractual when there is an actual

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[22] See McGUINNESS, p. 211 et seq; ROWLATT, p. 134 et seq; Putnam, op. cit., p. 61 et seq; O'Donovan & Phillips, op. cit., p. 445 et seq.

[23] See McGUINNESS, pp.301-356, for a detailed discussion of the general development and nature of rights of "indemnification".

[24] McGuinness points out that rights of "indemnification" may arise (a) by contract, as either an express or implied term of the contract, (b) by statute, or (c) by virtue of "legal and equitable considerations ... [giving] rise to a right of indemnity founded upon a right of restitution"; McGUINNESS, pp. 302-3. The second of these is not germane to the discussion. Goff & Jones contend that there is an important difference according to whether the right is contractual - which they say is properly termed a right of "indemnity" or "indemnification" - or restitutionary-which is a right of "reimbursement" or "recoupment". The difference, they assert, GOFF & JONES, pp.324-25, relates to the amount that can be recovered by the surety: "In ... [the case of indemnity], the plaintiff's right of recovery is not limited to the benefit, if any, conferred on the defendant by the plaintiff's payment. The plaintiff will be entitled to be indemnified against his expenditure, even though his payment may have conferred no benefit on the defendant, by discharging a liability or otherwise. Where, however, the plaintiff's claim is quasi-contractual, his right is not to indemnity but to reimbursement to the extent that his payment has conferred a benefit on the defendant." This distinction is not necessarily maintained in the case law or legal literature. It will, however, be adopted for the purposes of this paper to distinguish between rights of recovery over against the principal debtor which are contractual in origin, and those which are quasi-contractual or more properly restitutionary in origin and nature.

(rather than a fictional "implied" or "quasi-contract") contractual obligation of indemnity/indemnification, express or implied, between the principal and surety. This obligation may exist in a separate contract between the principal debtor and surety, or be an express or implied term of the contract of suretyship itself. The right is restitutionary, on the other hand, when the entitlement - to "reimbursement" or "recoupment"- rests instead upon the existence of a relationship of primary and secondary liability, and the equitable or quasi-contractual principles arising therefrom.[25] "Quasi-contractual" rights of reimbursement are more readily explained in modern legal thinking in restitutionary terms.

These rights of indemnity and reimbursement have long been recognised in English law. According to Barbour,[26] they were first recognised and enforced in the Chancery in the fifteenth century. Other writers, however, record Ford v Stobridge[27] in 1632, as the first case clearly recognising the surety's right of reimbursement in the Chancery. Contemporaneously, rights of indemnity were being recognised and enforced by way of indebitatus assumpsit in the common law courts,[28] but only if the surety could show an actual request by the principal debtor to the surety to

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25 See Re a Debtor [1937] 1 Ch. 156, at 163, per Greene L.J.; Anson v Anson [1953] 1 Q.B. 636, at 641-42, per Pearson J. See also Brooks Wharf & Bull Wharf Ltd. v Goodman Bros. [1937] 1 K.B.534, at 545, per Lord Wright M.R.

26 W.T. Barbour, "The History of Contract in Early English Equity", pp. 135-37, in 4 OXFORD STUDIES IN SOCIAL AND LEGAL HISTORY (1914, ed. P. Vinogradoff).

27 (1632) Nels. Ch. 24, 21 E.R. 780.

28 Rooke v Rooke (1610) Cro. Jac. 245, Yelv. 175, 79 E.R. 210.

become such, and a promise by the principal debtor to repay the surety.[29] In the terminology of restitution writers,[30] this was a contractual right of "indemnity" or "indemnification"; it thus differed from the Chancery's restitutionary right of recovery from the principal debtor, based upon equitable principles arising from the existence of primary and secondary liability. The recognition by the common law courts of this broader restitutionary right of reimbursement did not occur until over a century later, in Morrice v Redwyn in 1731.[31] Recovery in this case was also by way of indebitatus assumpsit - in particular by way of the count of "money paid at request"[32] - but the necessary "request" was essentially implied from the circumstances of the case in the fictional manner that underpined the law of quasi-contract for so long.

Today, these rights of indemnity and reimbursement are at the very heart of the surety's claims for recovery upon payment.

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[29] Idem. See also Moore v Moore (1611) 1 Bulst. 169, 80 E.R. 859; Bagge v Slade (1616) 3 Bulst. 162, 81 E.R. 137. The "promise" to support the indebitatus assumpsit could by this time be either express or implied. It was implied by virtue of an antecedent request to the surety to be a surety for the principal debtor.

[30] Supra, p. 43, note 24.

[31] (1731) 2 Barn. K.B. 26, 94 E.R. 333. Several cases had earlier denied the existence of any such general right: see Bosden v Thinne (1603) Yelv. 40, 80 E.R. 29; Scot v Stephenson (1662) 1 Lev. 71, 83 E.R. 302.

[32] In full, "money paid to the defendant's use at the defendant's request". For an account of the development of this count, see GOFF & JONES, pp. 52-4; S.J. Stoljar, THE LAW OF QUASI-CONTRACT (1964), pp. 127-31.

(ii) Contribution

The second right enjoyed by sureties and quasi-sureties upon payment or performance is contribution. Contribution broadly entitles a surety or quasi-surety to recover from any person equally liable with the surety for payment or performance of the guaranteed obligation - co-surety(s) or co-debtor(s) - a proportionate share of the amount paid by the former to the creditor.[33] The proportion payable is determined by the number of co-sureties and their relative liabilities to the creditor, and, in the case of equitable contribution, their solvency.[34]

Rights of contribution, like those of indemnity and reimbursement, were first recognised by the Chancery. This occurred perhaps as early as 1557,[35] but certainly by 1630 after two Chancery cases in 1629, namely Fleetwood v Charnock[36] and Peter v Rich.[37] The full report of the former reads:

> "The Plaintiff and Defendant were jointly bound for a third Person, who died leaving no Estate; the Plaintiff was sued and paid the Debt, and brought his Bill against the Defendant for Contribution, who was decreed to pay his proportionable Part."

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[33] If two sureties are not co-sureties, but stand instead in a relationship of principal and surety - ie. one of the two sureties is in fact a "surety for a surety" - then no right of contribution will arise between them. For a recent illustration, see Scholefield Goodman and Sons Ltd. v Zyngier [1986] A.C. 562 (P.C.), discussed infra, p. 154 et seq..

[34] See infra, p. 49, note 45.

[35] Marasinghe, loc. cit., I, p.54, identifies an anonymous case in 1557 involving the payment of rentcharges as the earliest reported illustration of contribution.

[36] (1629) Nels. 10, 21 E.R. 776.

[37] (1629) 1 Ch. Rep. 34, 21 E.R. 499.

Peter v Rich was factually more complicated. The plaintiff and defendant, together with a third person, Sheppard, had bound themselves for the payment of various debts of yet another person. Having been called upon to do so, Peter paid off what he thought was his proportion of the debts. He assumed that he was thereby freed from further liability on the bonds he and the others had earlier given, but this proved not to be so. Peter was subsequently compelled to pay a further £100 together with £5 interest thereon which remained outstanding. Peter alleged that this amount was due from Sheppard, and not him. Sheppard, however, had unfortunately become insolvent. The question before the court was whether Peter could recover any of the further £105 he had been compelled to pay from Rich. The court was of the opinion that:

> "the said £105 ... ought to be equally paid and born by the Plaintiff and Defendant Rich, and decreed accordingly."[38]

This case thus established the equitable rule that all solvent sureties should contribute proportionately according to their respective liabilities for the guaranteed debt(s).

Applications by sureties for contribution thereafter became well established. It was not, however, until later, in the leading case of Deering v Earl of Winchelsea[39] in 1787, that the theoretical foundations of this equitable right of contribution were considered in depth. There, in response to an argument that contribution between sureties rested on "the foundation of contract implied from their being parties in the same engagement..." and could not therefore be available to persons who though

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[38] (1629) 1 Chan. R. 34, at 35; 21 E.R. 499, at 500.

[39] (1787) 2 Bos. & P. 270, 126 E.R. 1276. Reported also as Dering v Earl of Winchelsea (1787) 1 Cox Eq. Cas. 318, 29 E.R. 1184.

bound for the same debt were strangers to each other, Lord Chief Baron Eyre in the Chancery affirmed:

> "If a view is taken of the cases, it will appear that the bottom of contribution is a fixed principle of justice, and is not founded in contract".[40]

The underlying justification, he went on, for contribution in the many cases both equitable and common law cited to the court was that the sureties:

> "are all in aequali juri, and as the law requires equality they shall equally bear the burden. This is considered as founded in equity; contract is not mentioned. The principle operates more clearly in a court of equity than at law."[41]

It was inequitable, in other words, that persons who were equally liable for the performance of an obligation should let performance fall upon one of them alone - all who could pay, should pay.[42]

Although, as mentioned by Baron Eyre, a right of contribution was also recognised by the common law courts, they had initially been much more resistant to the acceptance of such a right.[43] Certainly, they recognised a right of contribution where, as with the right of indemnity, an actual

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[40] Ibid., at 272, at 1277. For a recent re-affirmation of this view of contribution, see Scholefield Goodman and Sons Ltd. v Zyngier [1986] A.C. 562 (P.C.).

[41] Ibid., at 273, at 1278.

[42] The Chancery subsequently allowed a surety to sue his co-surety(s) for contribution even before the former had paid either the whole debt or his share, so long as the creditor had already obtained judgment against the surety; see Wolmershausen v Gullick [1883] 2 Ch. 514.

[43] In Offley & Johnson's case (1584) 2 Leon. 166; 74 E.R. 448, Johnson sought contribution in the King's Bench from his co-surety Offley. The court commented that although such a claim was enforceable by the custom of London, "upon this matter no action lieth by the course of the common law", ibid., at 167, at 448.

promise of contribution had been given to the surety,[44] but otherwise it was felt that to recognise a general right of contribution would be a "great cause of suits".[45] Nonetheless, a general right of contribution was subsequently recognised by the common law courts. For many years, however, it was seen to be available simply as a matter of equity and justice rather than contract or quasi-contract. This more or less remained so until the turn of the nineteenth century. In 1800, in Cowell v Edwards,[46] recovery from co-sureties was allowed by way of the quasi-contractual count of money paid "at request", the request being implied in the fashion of quasi-contractual actions generally. This placed the right of contribution upon a footing that was more acceptable to common law thinking of the time, although it was still generally considered "equitable" in nature.

Occasionally, the common law courts went further and attempted to explain this quasi-contractual right to contribution without reference to its equitable nature, on the basis that the right was an implied term in a

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[44] See eg., Bagge v Slade (1616) 3 Bulst. 162, 81 E.R. 137.

[45] Wormleighton v Hunter (1613) Godbolt 243, 78 E.R. 141. Contribution in the common law courts was also limited by the fact that the solvency or otherwise of the co-sureties was ignored in assessing the relative liability of each co-surety. Thus, a surety who was forced to pay the debt to the creditor and then sought contribution from co-sureties would recover only from those who were solvent. If, for example, A, B, and C were co-sureties in equal proportion for a debt of $300, and A paid the debt, B and C would be ordered to pay $100 each to A by way of contribution, being their one third share. If however B was insolvent, then although A would recover $100 from C, he would recover nothing from B. A would thus end up carrying two thirds of the debt. Equity would assess shares according to their solvency and order payment of aliquot shares. Thus, in the above example, there being only two solvent co-sureties, each would be ordered to contribute half of the debt. A would thus recover $150 from C and be bound to carry only $150 himself.

[46] (1800) 2 Bos. & Pul. 268, 126 E.R. 1275. This development had been foreshadowed four years earlier in Turner v Davies (1796) 2 Esp. 478, 170 E.R. 425. See also Cole v Saxby (1800) 3 Esp. 159, 170 E.R. 572.

contract between the co-sureties, itself generally "implied". In Craythorne v Swinburne,[47] for example, the Lord Chancellor, Lord Eldon, commented that:[48]

> "It has been long settled, that, if there are co-sureties by the same instrument, and the creditor calls upon either of them to pay the principal debt, or any part of it, that surety has a right in this Court, either upon a principle of equity, or upon contract, to call upon his co-surety for contribution; and I think, that right is properly enough stated as depending rather upon a principal [sic] of equity than upon contract: unless in this sense: that, the principle of equity being in its operation established, a contract may be inferred upon the implied knowledge of that principle by all persons, and it must be upon such a ground, of implied assumpsit, that in modern times Courts of Law have assumed a jurisdiction upon this subject: a jurisdiction convenient enough in a case simple and uncomplicated; but attended with great difficulty, where the sureties are numerous; especially since it has been held ... that separate actions may be brought against the different sureties for their respective quotas and proportions. It is easy to foresee the multiplicity of suits to which that leads."[49]

Either way, whether treated as equitable or quasi-contractual in nature, the surety's right of contribution can be broadly described as restitutionary in nature, being based largely upon a notion of "equality" of treatment, rather than contractual. More particularly, using modern restitutionary theory, the "equity" upon which contribution is said to be based can be translated according to the principle of unjust enrichment upon which the law of restitution is based. Thus, it can be said that if one only of two or more persons who are equally liable is compelled to pay or perform the whole of their common obligation, he or she thereby confers a benefit upon the others (by releasing them from their proportionate share

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47 (1807) 14 Ves. Jun. 160, 33 E.R. 482.

48 Ibid., at 164, at 483-4.

49 See also Davies v Humphries (1840) 6 M. & W. 153, 151 E.R. 361. In Wright v Hunter (1801) 5 Ves. Jun. 792, 31 E.R. 861, the Chancery affirmed that the equitable right of contribution was still available.

of the common liability) which it would be unjust for them to retain at the expense of the one paying or performing. In this way, it is submitted, the appropriateness of contributory relief in a particular factual situation may be more readily assessed.

Chapter 5

THE SURETY'S RIGHT OF SUBROGATION

A. Introduction

The surety's "right of subrogation" is well established in the law of suretyship. Nonetheless, there is no clear consensus amongst commentators on the precise nature and scope of this "right". It has, for example, been said to be the right:

> "to take under, or to stand in the shoes of, the creditor in enforcing the principal obligation of the debtor as well as in asserting any securities, priorities and remedies which the creditor enjoyed prior to the performance of the principal obligation."[1]

This is a relatively broad definition of the surety's right of subrogation. It employs the traditional metaphorical language associated with subrogation - "in the shoes of" - yet it also refers to the more specific right commonly said to be enjoyed by a surety under the name of "subrogation", namely the right to enjoy "any securities, priorities and remedies" previously enjoyed by the creditor.

Other commentators, however, have adopted a more limited explanation of the surety's right of subrogation. Goff and Jones, for instance, define the right in the following terms:[2]

> "A surety, who pays off the debt owed by the principal debtor, is subrogated to any securities given by the debtor to the creditor as security for the debt."

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[1] J. O'Donovan and J.C. Phillips, THE MODERN CONTRACT OF GUARANTEE (1985), p. 502. See also Duncan, Fox, & Co. v North & South Wales Bank (1880) 6 App. Cas. 1.

[2] Sir R. Goff & G. Jones, THE LAW OF RESTITUTION (3rd ed., 1986) (hereafter "GOFF & JONES"), p. 533.

They effectively restrict subrogation in the suretyship context, therefore, to the specific right of the surety to have securities held by the creditor assigned to him or her (the surety).

Other writers see difficulties with both these definitions. McGuinness, for example, writes:[3]

> "A surety who is called upon to perform the principal's obligation is subrogated to the full rights to which the creditor is entitled against the debtor. For instance, a surety who pays a judgment in respect of the guaranteed debt is entitled to an assignment of the judgment and also any securities held in respect of the guaranteed obligation."

This bears considerable similarity to the definitions above - it is broad, referring to the "full rights" of the creditor, yet it also encompasses by way of illustration the specific right referred to by Goff and Jones. But McGuinness then asserts that this broad approach - one that places the above rights at the heart of the surety's "right of subrogation" - is misleading.[4] These rights against the principal, he asserts:[5]

> "are not truly subrogatory, as they are independent rights to which the surety is entitled. The surety is entitled to proceed against the principal in his own name when asserting these rights."

McGuinness does not deny the existence of these rights. He simply asserts that they operate strictly speaking without apparent recourse to the technique of subrogation. In his view, it is thus a misnomer to call them rights of "subrogation".

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[3] K.P. McGuiness, THE LAW OF GUARANTEE (1986) (hereafter "McGUINNESS"), p. 199.

[4] Idem.

[5] Idem.

Other rights of the surety, McGuinness would concede, do operate through subrogation:[6]

> "In contrast, where the surety pays the creditor in full and the creditor is entitled to claim against some person other than the debtor in respect of the breach by the principal (as, for instance, a right of claim based upon the negligence of a professional employed to monitor the performance of the principal), the surety is subrogated to that right of claim. This is a true right of subrogation, and thus any such claim must be brought in the name of the creditor."[7]

McGuinness thus looks to the operation of the various rights enjoyed by the surety to determine whether or not any particular right can properly be said to be subrogatory. The other writers cited, by way of contrast, look to and rely on traditional notions of the "surety's right of subrogation", even though the definitions thereby offered may, if McGuinness's argument is sound, be found to be flawed.

These differences, and the difficulties that consequently arise in any discussion of subrogation in the context of suretyship, are a product, it is submitted, of two factors. The first is simply that the expression "the surety's right of subrogation" is not, as McGuinness points out, used only to refer to rights which strictly speaking depend upon the use of the technique of subrogation. More commonly, that expression is used broadly to refer to a range of rights and remedies enjoyed by a surety that operate in similar ways and to similar effect, but without necessarily adopting the conventions of subrogation either as to language or as to operation. The difference between these two ways of talking about "subrogation" - between the narrow use of it to refer to rights which are dependent upon the

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6 Idem.

7 McGuinness cites the Canadian case of Prince Albert v Underwood, McLellan & Associates Ltd. [1969] S.C.R. 305, as authority for this latter point; McGUINNESS, p. 199, note 38.

technique of subrogation for their operation, and the broad use of it to refer to a range of related rights - is, broadly speaking, the difference between McGuinness and the other writers cited above. It is also both a major reason for, and, to a considerable extent, an explanation of, the difficulties associated with subrogation in this context.

The second, related factor is that the body of rights and remedies represented by the expression "the surety's right of subrogation", used in the broad sense, is not drawn uniformly from one source. Instead, it encompasses overlapping rights and remedies drawn both from equity and statute. Common law had little to add to this body of rights and remedies. At best, it recognised rights of subrogation as a matter of contract, express or implied, between the various parties to the suretyship, but it never really developed an independent means of pursing these rights and remedies in the common law courts, as it had by way of the quasi-contractual count of money paid at request in relation to the surety's rights of reimbursement and contribution. It only eventually managed this with statutory assistance in the mid-nineteenth century.[8]

B. The Content of the Surety's Right of Subrogation

Used accumulatively, the expression "the surety's right of subrogation" broadly encompasses two, perhaps three, rights (or remedies, depending upon how they are treated). They are: (1) the equitable right to have any securities given to the creditor by the debtor, or indeed by

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[8] See the Mercantile Law Amendment Act of 1856, 19 & 20 Vict., c. 97, s. 5. See infra, p. 71 et seq..

others, assigned to the surety to enforce in the surety's own name; (2) the equitable right to "stand in the place of the creditor" and exercise for the surety's own benefit any rights and remedies enjoyed by the creditor against the debtor, or indeed other persons; and (3) the statutory rights contained in the English Mercantile Law Amendment Act of 1856,[9] and its Canadian counterparts.[10] Each of these rights needs to be examined in some detail.

(i) Equitable right to securities

The first of the rights subsumed by the expression "the surety's right of subrogation" is the surety's equitable right to have any securities given to the creditor for the principal debt assigned to him (the surety) by the creditor.[11] This primarily relates to securities given to the creditor by the principal debtor, but may also extend to securities given by others such as co-sureties. In general, it does not matter when the securities were given to the creditor, or whether the surety had any knowledge of them.[12] Upon assignment, the surety is entitled to enforce the

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9 19 & 20 Vict., c. 97, s. 5.

10 Eg.: Mercantile Law Amendment Act, R.S.O. 1980, c.265, s.2(1)(2).

11 Morgan v Seymour (1637) 1 Chan. Rep. 120, 21 ER 525. In Wulff v Jay (1872) L.R. 7 Q.B. 756, Cockburn C.J. accepted that a creditor has a correlative duty, as soon as the surety has paid the debt, to make over to him all the securities held by the creditor in order that the surety may recoup himself.

12 Forbes v Jackson (1882) 19 Ch. D. 615, at 621. See also Mayhew v Crickett (1818) 2 Swanst. 185, at 191, 36 E.R. 585, at 587; Newton v Chorlton (1853) 10 Hare 646, at 651, 68 E.R. 1087, at 1089; Pearl v Deacon (1857) 24 Beav. 186, 53 E.R. 328; Goddard v Whyte (1860) 2 Giff. 449, 66 E.R. 188.

assigned securities against the debtor in the surety's own name, rather than that of the creditor.[13] If the creditor refuses to assign, the surety can bring an action in equity to compel him to do so.[14] If the creditor acts in relation to any of the securities held by him in such a way as to prejudice the surety's entitlement to have them assigned to him upon payment of the debt, then the surety may be discharged from liability to the creditor either in toto or in part.[15] This equitable right is, therefore, as McGuinness points out,[16] very much in the nature of an "independent right" enjoyed by the surety against the creditor, ostensibly existing without recourse to the technique of subrogation. The surety does not "stand in the place of" the creditor; rather he becomes a secured creditor in his own right by virtue of what is often explained as being in the nature of an "equitable assignment" of the securities.

Nonetheless, for many commentators, this equitable right to assignment stands at the centre of and typifies "the surety's right of subrogation". Goff and Jones's definition of the surety's right of subrogation along these lines[17] is illustrative of this fact. The reasons for this appear to be twofold. One is historical; the other is practical.

The historical reason rests simply on the fact that this right is generally thought to have been the earliest of the various rights and remedies subsumed within the expression "the surety's right of subrogation"

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13 McGUINNESS, pp. 204-5.

14 Goddard v Whyte (1860) 2 Giff. 449, 66 E.R. 188.

15 Pearl v Deacon (1857) 24 Beav. 186, 53 E.R. 328.

16 McGUINNESS, pp. 204-5.

17 GOFF & JONES, p. 533.

to have been recognised by the courts. This occurred, it is generally thought, in the Chancery case of Morgan v Seymour,[18] in 1637. The report of that case reads:

> "The Plaintiff with Sir Edward Seymour the Defendant being bound with Sir William St. Johns for the proper Debt of the said St. Johns, to the Defendant Rowland in a Bond of 200 for the payment of 100, and the said Rowland sued the Plaintiff only on the said Bond, the Plaintiff seeks to have the said Seymour contribute and pay his part of the said Debt and Damages, the said St. Johns being insolvent. This Court was of Opinion, that the said Seymour ought to contribute and pay one Moiety [half] to the said Rowland, and decreed Rowland to assign over the said Bond to the Plaintiff, and Seymour to help themselves against the said St. Johns for the said Debt."[19]

Morgan's claim, it must be observed, was for contribution from his co-surety, Seymour. That was duly ordered, presumably in accordance with the equitable principles shortly before affirmed by the Chancery.[20] Upon payment, Morgan and Seymour were entitled to reimbursement from Sir William; again, a right only shortly before affirmed in the Chancery.[21] But this right was of limited value, for it was in personam in nature, and Sir William was insolvent. Morgan and Seymour could not therefore claim any priority over other unsecured creditors of Sir William by virtue of their right of reimbursement. To remedy this, the court, for the first time it is thought in English law, ordered the creditor to assign over to the co-sureties the Bond given to him by the principal debtor, to be enforced by them. This changed things markedly, for it meant that Morgan and Seymour, upon assignment of the Bond, would also obtain any priority or preference

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18 (1637) 1 Chan. Rep. 120, 21 ER 525.

19 Idem. [Emphasis added]

20 Supra, p. 46 et seq..

21 Supra, p. 43 et seq..

it carried vis-á-vis other unsecured creditors in Sir William's bankruptcy. Needless to say, this order was a tremendous practical advantage over mere in personam rights of reimbursement and, for reasons which are self-evident, goes a considerable way towards explaining the association between the surety's right to the assignment of securities, and the "right of subrogation" as it has come to be popularly known.

Several further points concerning this seminal case bear emphasis. First, there is no reference in the case to "subrogation". Nor is there even terminology along the lines of "standing the surety in the place of the creditor", as was later to become the identifying metaphor for subrogation. It is difficult therefore to assert that the judges in this case saw themselves as relying specifically on a technique of subrogation to achieve the result that they did. More than likely, they would have seen themselves rather as resting their order on the notions and principles underlying equitable assignment.[22] Later cases certainly supported this latter view when they confirmed that the surety could enforce the assigned securities in his own name, and not that of the creditor as strictly speaking would be required if this right was thought or seen to rest upon the technique of subrogation.

Nonetheless, the conferral of remedies upon Morgan and Seymour, as sureties, was effected by giving them the benefit of rights possessed by another, the creditor, and this made it sufficiently similar in operation

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[22] The doctrines of equitable assignment were being developed at about the same time according to Ashburner, PRINCIPLES OF EQUITY (2nd ed., 1933), p. 236: "In equity, however, from the seventeenth century onward, an assignment of a debt for valuable consideration, even though by parol, was upheld against the assignor ... ". In support, Ashburner cites a case decided only two years before Morgan v Seymour, namely Earl of Suffolk v Greenvill (1631) Freem. Ch. 146, 22 E.R. 1119.

to the technique of subrogation strictly speaking to have led to the identification of this case as a "subrogation" case.

Secondly, the court did not offer any clear explanation of the basis upon which Morgan and Seymour were entitled to have the Bond assigned to them, other than that it was was "to help themselves against the said St. Johns for the said Debt." While this suggests some connection between the existence of a right of recovery against the principal debtor, and this new right to securities, this connection was not developed in the case. Equally, although the court presumably justified its order and the outcome of the case on some broad equitable basis, it made no express attempt to define the nature of that equity in this case. This task, however, was taken up later.

Broadly speaking, two explanations for the existence of this right presented themselves. One adopted the line that this right derives from and is a consequence of the debtor's undertaking, express or implied, to indemnify or reimburse the surety. Lord Selborne L.C. in Duncan, Fox, & Co. v North & South Wales Bank[23] provides an illustration of this view. There, it will be recalled, Lord Selborne L.C., in classifying the classes of surety, stated as his third class:[24]

> "Those in which, without any such contract of suretyship, there is a primary and a secondary liability of two persons for one and the same debt, the debt being, as between the two, that of one of those persons only, and not equally of both, so that the other, if he should be compelled to pay it, would be entitled to reimbursement from the person by whom (as between the two) it ought to have been paid." [25]

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23 (1880) 6 App. Cas. 1.

24 Ibid., at 11.

25 Emphasis added.

The surety's right of subrogation, on this view, is dependent upon the surety establishing a right of reimbursement.[26] This view has the advantage of simplicity. But this is also its main deficiency, for it assumes that the availability of a right of reimbursement is settled law. This is not so. As has been seen,[27] a right of indemnity or reimbursement may arise on contractual, quasi-contractual, or equitable grounds. Often it will be clear whether it arises or not. Sometimes, however, it will be necessary to examine the circumstances of the particular case to determine whether any such right of reimbursement exists. Those circumstances, it is submitted, will also ultimately justify the existence or absence of a right of subrogation, not the existence of the right of reimbursement per se. Both rights, in other words, arise from the same facts and, it is submitted, for similar restitutionary reasons. Thus, to relate the right of subrogation to the right of reimbursement is, it is submitted, to beg the question, for it fails to explain the circumstances that will justify a court in conferring rights, whether by way of reimbursement or subrogation, upon a surety. Ultimately, it is submitted, it is the identification of those circumstances and the "justice" in them, that explains the availability of the surety's equitable right to have securities assigned.

The second explanation for the right to have securities assigned recognises this fact, and consequently rests the right upon an "equity" arising from the facts of the relationship. This is the more common explanation of this right. It gained particular force under the

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[26] See also: Yonge v Reynell (1852) 9 Hare 809, at 819, 68 E.R. 744, at 748-49.

[27] Supra, p. 43 et seq..

Chancellorship of Lord Eldon in the early part of the nineteenth century. In Aldrich v Cooper,[28] for example, Lord Eldon L.C. stated that the surety's equity rested upon the same principles as those underlying the related doctrine of marshalling[29]:

> "[I]t is not by force of the contract; but that equity, upon which it is considered against conscience, that the holder of the securities should use them to the prejudice of the surety; and therefore there is nothing hard in the act of the Court, placing the surety exactly in the situation of the creditor."[30]

This view, while more enlightening in certain respects, still does not go far enough, however, for it fails to explain the nature of this "equity", or why the facts of the case give rise to it. What, in other words, is the underlying "inequity"? The answer to that question, it is submitted, rests in the law of restitution and its notions of unjust enrichment.

Thus, while Morgan v Seymour[31] is pivotal in the development of the surety's rights of subrogation, and undeniably established that the Chancery would aid a surety by ordering a creditor to assign any securities

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[28] (1803) 8 Ves. Jun. 382, 32 E.R. 402.

[29] The doctrine of marshalling ostensibly allows a surety to call upon a creditor who has two or more funds out of which he could satisfy his claim against the principal debtor, one or more of which would not be available to the surety, to resort first to the latter fund, so as to enable the surety to benefit from the others in the event of his making payment to the creditor.

[30] (1803) 8 Ves. Jun. 384, at 389, 32 E.R. 402, at 405. Four years later, in Craythorne v Swinburne (1807) 14 Ves. Jun. 160, 33 E.R. 482, he equated the equity underlying subrogation to that which underlay the doctrine of equitable contribution, at 165, at 484: "the principle of Equity operates ... upon the maxim, that equality is Equity: the creditor, who can call upon all, shall not be at liberty to fix one with payment of the whole debt; and upon the principle, requiring him to do justice, if he will not, the Court will do it for him."

[31] (1637) 1 Chan. Rep. 120, 21 E.R. 525.

held by him to the surety after payment of the debt, it offers only limited guidance on the theory of the right to securities recognised by it.

It also established from the very beginning the close connection between the surety's assertion of rights derived from the creditor, and the obtaining of priority against an insolvent principal debtor. This is of course the predominant advantage of this right over the other rights of indemnity or reimbursement enjoyed by the surety against the principal debtor.

Since this right to the assignment of securities operates to much the same effect as rights by subrogation strictly speaking,[32] it is hardly surprising, therefore, to find it discussed in the same breath as other similar rights by way of subrogation.

The advantages offered to the surety by this right to securities also meant that it was not long before it took hold and became an established action in the Chancery. Actions to enforce this right figure increasingly in the case law throughout the seventeenth and eighteenth centuries.[33] By the early nineteenth century, much of the law on this equitable right was well settled, although, as has been seen, the theory of the right was never really worked out in detail.

It was also clear by the early nineteenth century that the common law

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[32] The principal difference is, of course, in the entitlement to enforce the securities in the surety's own name, rather than that of the creditor.

[33] See eg., Parsons v Briddock (1708) 2 Vern. 608, 23 E.R. 997; Ex parte Crisp (1744) 1 Atk. 133, 26 E.R. 87; Greerside v Benson (1745) 3 Atk. 248, 26 E.R. 944; Wright v Morley (1805) 11 Ves. Jun. 12, 32 E.R. 992. See also the discussion infra, p. 74, in relation to the rule in Copis v Middleton (1823) 1 Turn. & R. 224, 37 E.R. 1083.

courts were unable to countenance the existence of a similar right at common law.[34]

(ii) Equitable right to "stand in the place of another"

The second of the three rights that can be subsumed within the expression "the surety's right of subrogation" is the equitable right of the surety to "stand in the place (or shoes) of" the creditor, as it is commonly expressed, and, using the creditor's name, exercise all the creditor's rights and remedies whether against the principal debtor, or others,[35] for his own (the surety's) benefit. Because the rights and remedies enjoyed by the surety pursuant to this "right" are derived from those of the creditor and must be exercised in the creditor's name, this right is quite clearly subrogative in nature, in the strict sense of that term. The surety's "right" is more accurately expressed as his or her entitlement to have the technique of subrogation used in his or her favour so as to endow him or her with rights and remedies whereby the principal debtor (or perhaps others such as co-sureties) can be prevented from taking unjust advantage of the surety's payment - to prevent the principal

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[34] It is clear from several cases in the first half of the nineteenth century, in particular Copis v Middleton (1823) 1 Turn. & R. 224, 37 E.R. 1083, and Hodgson v Shaw (1834) 3 My. & K. 183, 40 E.R. 70, that the common law courts considered payment by the surety to have the effect of discharging both the guaranteed debt and securities held for it, thus rendering it impossible for the surety to have the benefit of them either by way of assignment or otherwise. See also Batchellor v Lawrence (1861) 9 C.B.(N.S.) 543, 142 E.R. 214.

[35] Including co-sureties and even third parties liable to the creditor in respect of the principal debtor's performance of his obligation to the creditor: see Prince Albert v Underwood, McLellan & Associates Ltd. [1969] S.C.R. 305.

debtor's unjust enrichment, in other words. This injustice is remedied by making the extant rights and remedies of the creditor available to the surety to enforce for his or her own benefit. But because they are the rights and remedies of the creditor, and not separate rights and remedies enjoyed by the surety, they must be exercised in the name of the creditor.

There is considerable uncertainty surrounding this right in equity. In particular, it is unclear how far this right can be separated from the equitable right to the assignment of securities already discussed. There are a number of reasons for this uncertainty. In the first place, there is no express reference to an equitable right of the surety to "stand in the place of the creditor" until the turn of the nineteenth century.[36] Prior to that, the relevant cases generally spoke in terms of the right to "assign", clearly treating that as the essential basis upon which equity conferred rights upon sureties, and thus making this second right but one aspect of the established equitable right to have securities assigned. Secondly, even when the more familiar terminology began to be used, it was still generally intermixed with references to the right to have securities assigned. In Wright v Morley,[37] for instance, the Master of the Rolls, Sir W Grant, when asked by a surety who had been compelled to pay the guaranteed debt to "stand [the surety] in the place of the creditor [who had access to a fund out of which he could have satisfied the debt], and avail himself of the pledge to reimburse himself",[38] held that:

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[36] The terminology had been used in other contexts, in particular in the context of loans to married women, infants, and the insane, for the purchase of necessaries. See supra, p. 23.

[37] (1805) 11 Ves. Jun. 12, 32 E.R. 992.

[38] Ibid., at 19, at 994.

> "the surety has full as good an equity to the benefit of all the securities the principal gives to the creditor. ... [Parsons v Briddock[39] in 1708] established, that the surety had precisely the same right that the creditor had; and was to stand in his place. The surety had no direct contract or engagement, by which the bail were bound to him; but only a claim against them through the medium of the creditor; and was entitled only to all his rights."[40]

In Craythorne v Swinburne,[41] the Lord Chancellor, Lord Eldon, similarly approved the following outline of a surety's rights by Sir Samuel Romilly,[42] counsel in that case for the surety plaintiff seeking contribution:[43]

> "The contribution results from the maxim, that equality is equity: proceeding where the instruments are several, very much upon this; that a surety will be entitled to every remedy, which the creditor has against the principal debtor; to enforce every security and all means

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39 (1708) 2 Vern. 608, 23 E.R. 582.

40 (1805) 11 Ves. Jun. 12, at 22-23, 32 E.R. 992, at 995-96. Interestingly, in Parsons v Briddock (1708) 2 Vern. 608, 23 E.R. 582, referred to by Sir W Grant in Wright v Morley, the then Lord Chancellor, Lord Cowper, had used the teminology of "standing one person in the place of another", but in relation to a person who had agreed to give bail for another arrested for non-payment of his debts. When subsequently the principal failed to pay, judgment on the bail bond was obtained against the bail. Payment of the debts was, however, made by two sureties on the original bond, who now sought to have the judgment against the bail assigned to them to enforce. Lord Cowper held that "the bail stand in the place of the principal, and cannot be relieved on other terms than on payment of principal, interest, and costs", and thus ordered the judgment against the bail to be assigned to the sureties "in order to reimburse them what they had paid, with interest and costs." It was not, therefore, the sureties who were seen to stand in the place of another, although that in substance is the effect of the judgment - the sureties were allowed to stand in the place of the creditors who had obtained a judgment against the bail. The court treated this entitlement, however, as an aspect of the equitable right to have "securities" assigned.

41 (1807) 14 Ves. Jr. 160, 33 E.R. 482.

42 Sir Samuel Romilly has been described as "the greatest equity lawyer of his day", see Kerly, op.cit., 266. It is worth noting that Sir Samuel Romilly also appeared as counsel in Wright v Morley (1805) 11 Ves. Jun. 12, 32 E.R. 996., though not as counsel for the surety.

43 (1807) 14 Ves. Jun. 160, at 162, 33 E.R. 482, at 483.

> of payment; to stand in the place of the creditors; not only through the medium of contract, but even by means of securities, entered into without the knowledge of the surety; having a right to have those securities transferred to him; though there was no stipulation for that; and to avail himself of all those securities against the debtor."[44]

This submission was later relied upon by Lord Brougham, L.C., in Hodgson v Shaw,[45] in which he said that Sir Romilly's argument had "luminously expounded" the extent of the surety's right, but "placed [it] as high as it ever can be placed"[46]:

> "The rule here [in equity] is undoubted, and it is one founded on the plainest principles of natural reason and justice, that the surety paying off a debt shall stand in the place of a creditor, and have all the rights which he has, for the purpose of obtaining his reimbursement. It is hardly possible to put this right of substitution too high, and the right results more from equity than from contract or quasicontract; ... Thus the surety paying is entitled to every remedy which the creditor has."[47]

Here, then, is the first clear use in the suretyship context of the terminology now so closely associated with rights of subrogation.

It should be observed, though, that these cases, while using the terminology of "standing in the place of", nonetheless seem to assume the existence of a broad equitable right in the surety to enjoy the benefit of all the rights and remedies of the creditor, dating from earlier times. One instance of this is the reference in Wright v Morley[48] to Parsons v Briddock[49] in 1708. In the latter case, the Lord Chancellor ordered a

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44 Emphasis added.

45 (1834) 3 My. & K. 183, 40 E.R. 70.

46 Ibid., at 191, at 73.

47 Idem.

48 (1805) 11 Ves. Jun. 12, 32 E.R. 996.

49 (1708) 2 Vern. 608, 23 E.R. 997.

judgment obtained against a bail to be "assigned" to the plaintiff sureties who had been sued on their original bond and had paid, in order to reimburse themselves what they had paid. Although the case speaks in terms of the right to have securities assigned, the judgment was not as such a "security" for the original guaranteed debt. It related rather to the subsequent liability of the principal under enforcement proceedings. It was thus in the nature of a right or remedy available to the judgment creditors, but it was still made available to the sureties to enforce. They obtained that right, in substance, by standing in the place of the paid-off judgment creditor. This case thus provides an illustration of the apparent earlier recognition of this broader equitable right, even though still generally expressed in terms more closely representative of the right of assignment.

One writer[50] has taken this further and argued that the technique of standing the surety in the place of the creditor in order to confer the creditor's rights and remedies upon the surety was first recognised before even the right to assignment of securities, more than eighty years earlier in fact, in the context of the surety's right of contribution.[51] Contributory recovery against co-sureties was effected, this view asserts, not by means of a direct equitable right of contribution as was later established, but in substance by allowing the paying surety to "stand in the place of" the creditor and exercise the latter's contractual or other rights of recovery against any persons equally liable with the paying

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50 Marasinghe, loc. cit., I.

51 Ibid., pp. 54-56.

surety.[52] This, it is said, was the earliest manifestation of the technique of subrogation in favour of sureties in English law - indeed, it would be the earliest manifestation of subrogation in English law in any guise.

Alternatively, it might be said that this entitlement to the benefit of the creditor's rights and remedies was recognised at least implicitly in Morgan v Seymour,[53] insofar as the Chancery there displayed a willingness to enhance the surety's rights and remedies against the principal debtor by looking to the rights and remedies of the paid-off creditor. That the right subsequently failed to find clear recognition and elucidation as a separate right until much later may perhaps be a product of contemporaneous developments in the Chancery and the courts of common law. In particular, it may be that it was not until later, with the introduction of the terminology of "standing in the place of another" in the necessaries cases in the first quarter of the eighteenth century,[54] that the Chancery judges began to think of this right other than in terms of the right to the assignment of securities. But by then both the Chancery and the common law courts had recognised and were enforcing in favour of sureties direct equitable and quasi-contractual rights of reimbursement from the principal debtor[55] and contribution from co-sureties. These developments to an extent rendered an equitable right to stand in the creditor's place in order to recover against the principal debtor or co-sureties slightly superfluous, at least with respect to contractual sureties, for the surety could seek

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52 Idem.

53 (1637) 1 Chan. Rep. 120, 21 E.R. 525.

54 See supra, p. 23.

55 See supra, p. 43 et seq..

recovery directly from the debtor through these then newly recognised equitable and quasi-contractual actions. Where necessary the surety could also rely on the specific equitable right to the assignment of securities to enhance these rights of reimbursement and contribution. Thus there was at that time no need for the surety to ask the court to stand him in the place of the creditor so as to endow him or her with all the rights and remedies of the creditor. Later, however, when the rights and obligations of contractual suretyship were extended to quasi-suretyships, there was arguably a need for this right since, as has already been seen,[56] quasi-sureties were not automatically entitled to all, or the same, rights as those of a surety in the strict contractual sense. In particular, quasi-suretyships did not necessarily attract in full the equitable right to the assigment of securities.[57] That being so, the only way in which the quasi-surety could obtain the benefit of any securities held by the creditor and the priority they accorded, was if he or she was allowed to stand in the creditor's place and take the benefit of those securities. There was one difference, however: the surety had to exercise the rights in the creditor's name, rather than his own.

These uncertainties aside, it is clear that by the early part of the nineteenth century there was a general perception that a surety was entitled to a broader range of equitable rights than the equitable entitlement to have any securities held by the creditor assigned to him or her.

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56 Supra, p. 35 et seq..

57 Idem.

(iii) Statutory rights

The third of the surety's "rights of subrogation" comprises the statutory rights enjoyed by sureties pursuant to section 5 of the Mercantile Law Amendment Act of 1856.[58] This as enacted provided:

> "Every Person who, being surety for the Debt or Duty of another, or being liable with another for any Debt or Duty, shall pay such Debt or perform such Duty, shall be entitled to have assigned to him, or to a Trustee for him, every Judgment, Specialty, or other Security which shall be held by the Creditor in respect of such Debt or Duty, whether such Judgment, Specialty, or other Security shall or shall not be deemed at Law to have been satisfied by the Payment of the Debt or Performance of the Duty, and such Person shall be entitled to stand in the Place of the Creditor, and to use all the Remedies, and, if need be, and upon a proper Indemnity, to use the Name of the Creditor, in any Action, or other Proceeding, at Law or in Equity, in order to obtain from the principal Debtor, or any Co-Surety, Co-Contractor, or Co-Debtor, as the Case may be, Indemnification for the Advances made and Loss sustained by the Person who shall have so paid such Debt or performed such Duty, and such Payment or Performance so made by such Surety shall not be pleadable in bar of any such Action or other Proceeding by him : Provided always, that no Co-Surety, Co-Contractor, or Co-Debtor, shall be entitled to recover from any other Co-Surety, Co-Contractor, or Co-Debtor, by the Means aforesaid, more than the just Proportion to which, as between those Parties themselves, such last-mentioned Person shall be justly liable."

The effect of this provision was considered by Byles J. in Batchellor v Lawrence:[59]

> "In England, prior to the passing of this act, a surety or co-debtor who had been compelled to pay the debt for which he was liable, could not obtain the benefit of any securities held by the creditor without having recourse to a court of equity; and not always then. The section in question, I think, meant to afford the party at least the same remedy at law as he would have had in equity."

This provision thus conferred a statutory entitlement upon a surety both to "stand in the place of" the creditor and exercise for his own benefit - but in the creditor's name - all the latter's remedies, in the

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[58] 19 & 20 Vict., c. 97.

[59] (1861) 9 C.B. (N.S.) 543, at 555-6, 142 E.R. 214, at 218.

same general way that the courts of equity had apparently already allowed, and also to have all the latter's securities assigned to him to exercise for his own benefit in his own name, again as equity had already allowed. In substance, it codified the two equitable "rights" recognised by the Chancery, and made them equally available in the common law courts, where the availability of such rights had previously been denied.

Did this section confer any new rights or remedies upon the surety? This is not entirely clear. At first sight, it simply gives the established equitable rights a new and alternative statutory basis. On the other hand, certain features about the statutory rights might suggest that the draftsman intended them to operate more generously than had been the case in the Chancery. Thus, the section applies not only to sureties for "Debts", but also to persons who are surety "for the Duty of another", and also to persons who are "liable with another for any Debt or Duty". This, however, was arguably true of the equitable rights, for, as has been seen, they also were held to be available to persons who were not sureties strictly speaking, but only quasi-sureties, especially those whose rights were based upon the existence of a relationship of primary and secondary liability rather than any agreement. Co-sureties, co-debtors, those jointly liable for the performance of some duty other than the payment of a debt, and the like, could on this basis stake a claim for comparable equitable rights to those of the surety.

Equally, although the statutory rights and remedies are exerciseable not only against the principal debtor, but also against "any Co-Surety, Co-Contractor, or Co-Debtor", subject to the restriction that recovery be only for "the just Proportion to which, as between those Parties themselves,

such last-mentioned Person shall be justly liable", this again was probably so in equity. Co-sureties, co-debtors, and co-contractors who are equally[60] liable for payment of a debt or performance of a duty are essentially liable to each other for contribution. It is arguable that a surety's equitable entitlement to contribution from his co-sureties, and the like, exists not only directly in equity but also indirectly through the creditor's rights against the co-sureties.[61] Again, therefore, the section arguably did no more than record the status quo.

Thirdly, section 5 states that the persons entitled by the section to the assignment of securities are entitled not just to the assignment of any "securities" given by the debtor to the creditor, but more broadly to "every Judgment, Speciality, or other Security" given by him to the creditor. Furthermore, this entitlement accrues even though the judgment, specialty, or other security may have been "deemed at Law to have been satisfied by the Payment of the Debt or performance of the Duty". It is here that the statutory rights do appear to differ significantly from those available in equity. While the language of the chancery judges in explaining the scope of the equitable rights was certainly wide enough to cover more than "securities" strictly speaking, and in particular judgments and specialities, for a long time it was not clearly decided whether

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[60] If they are not equally liable, their rights inter se will be determined by their respective liabilities for payment of the debt or performance of the duty. If, as between themselves, either because of an agreement or some other relevant factor, one or more of them is or are only secondarily liable then that person(s) will be a surety or quasi-surety for the other(s) and be entitled accordingly to the rights of a surety or quasi-surety.

[61] As has been discussed, supra, p. 68, Marasinghe has argued that this was the first manifestation of the technique of subrogation in favour of sureties; loc. cit., I.

payment of the debt by the surety had the effect in equity, as it did at law,[62] of discharging both the debt and also any primary securities[63] given to the creditor by the debtor for the debt. This question was eventually considered by the Chancery in Copis v Middleton[64] in 1823. In that case, the Lord Chancellor, Lord Eldon, held that payment of the debt in equity discharged not only the debt but also primary securities. That meant that they were useless in the hands of the surety; this was so even if the creditor had previously purported to assign them to the surety in accordance with the surety's undoubted equitable right to assignment.

The case concerned a deceased debtor. Some of his creditors were speciality creditors,[65] entitled thereby according to the law of the time to rank in priority to ordinary creditors in the administration of the deceased's estate. A surety for the deceased, who had paid off some of those speciality debts prior to the deceased's death, and who was surety for further unpaid speciality debts, claimed not the right to be reimbursed out of the estate as an ordinary creditor,[66] but the right to rank in the place of the paid off speciality creditors as a speciality creditor himself. It was conceded that at law payment of the debt discharged not

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62 See Copis v Middleton (1823) 1 Turn. & Russ. 224, 37 E.R. 1083.

63 But not collateral securities such as a mortgage.

64 (1823) 1 Turn. & Russ. 224, 37 E.R. 1083.

65 A speciality was a contract under seal. A speciality debtor, therefore, was one whose debt was acknowledged by a contract under seal, and a speciality creditor was thus one to whom the debtor had acknowledged his liability under seal.

66 This right is in personam only and thus makes the surety an ordinary contract or quasi-contractual creditor, thus affording him or her no priority over other ordinary creditors.

only the debt but also the speciality bond which created the debt, thereby preventing the surety at law from taking advantage of the speciality.[67] Even an assignment of it prior to payment of the debt would have been to no avail since payment was still considered to have discharged it; only collateral securities could be kept alive in this manner for the benefit of the surety. But, argued the surety, that was not the position in equity. He was entitled, he argued, to rank as a speciality debtor:

> "because a Court of Equity would keep alive the bond for his benefit, and on the principle on which it interferes to prevent legal bars from being set up, would permit an action to be brought upon the bond, and restrain the principal from setting up the payment."[68]

This was not so, held Lord Eldon L.C. While there was:

> "a general rule that in equity a surety is entitled to the benefit of all the securities which the creditor has against the principal,"[69]

the nature of those securities had to be considered. When there was a bond merely, and no collateral security, then:

> "if an action was brought upon the bond, it would appear upon oyer of the bond that the debt was extinguished; the general rule therefore must be qualified, by considering it to apply to such securities as continue to exist, and do not get back upon payment to the person of the principal debtor ... ".[70]

Equity, in other words, would follow the law on this point.

The effect of this judgment, had it survived, would have been to devastate the equitable rights of subrogation previously afforded to a surety. Fortunately, it did not survive. One of the prime objectives of section 5 of the Mercantile Law Amendment Act of 1856 was to reverse this

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67 (1823) Turn. & R. 224, at 228, 37 E.R. 1083, at 1084.

68 Idem.

69 Ibid., at 229, at 1085.

70 Idem.

judgment. Thus, it became immaterial whether the "Judgment, Speciality, or other Security" was or was not deemed at law or in equity to be discharged by payment or performance. "Payment or Performance", provides section 5, "shall not be pleadable in bar of any such Action or other Proceeding" by the surety.

By way of contrast, the fourth potential difference between the equitable and the statutory rights is a product of case-law. In 1886, it was held that the statutory right of assignment entitled the surety to sue the principal debtor upon the securities held by the creditor in the surety's own name without necessarily taking an actual assignment from the creditor.[71] The section operated, it was held,[72] upon payment in full, on the basis of an "implied assignment". In this respect the statutory rights differed from the surety's existing equitable rights of subrogation, for equity required suit in the name of the creditor, or an actual assignment (although the Chancery would order the creditor to effect such an assignment).

As a result, section 5 could be said to go further than equity and not just "afford the party at least the same remedy at law as he would have had in equity", as Byles J. suggested in Batchellor v Lawrence.[73]

The enactment of section 5, together with the procedural changes in England consequential upon the subsequent fusion of the courts of common

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71 Re M'Myn, Lightbown v M'Myn (1886) 33 Ch. D. 575.

72 Idem.

73 (1861) 9 C.B. (N.S.) 543, at 555-6, 142 E.R. 214, at 218.

law and equity,[74] also had the practical effect that sureties generally had no need to continue to rely upon their former equitable rights in seeking recovery of monies expended on behalf of either the principal debtor or co-sureties. Instead they could simply rely upon the statutory rights afforded to them by section 5. To an extent, therefore, the equitable rights outlined above were rendered superfluous.

(iv) A composite of rights

Used broadly, therefore, the expression "the surety's right of subrogation" thus encompasses these three related rights. As already suggested, the most important from the surety's perspective, will generally be the right of assignment of securities, whether statutory or equitable, for only this will enable a surety to obtain priority over other ordinary creditors of an insolvent principal debtor. Indeed, unless the principal debtor is insolvent, then practically speaking, questions of the surety's rights of subrogation may never arise. Instead, the surety can simply rely on the broad, readily enforceable rights of indemnity or reimbursement outlined above (and similarly, his rights of contribution against co-sureties). This has the consequence that it is generally only when the debtor is insolvent that the surety needs to assert his rights of assignment, and thus also subrogation. The other rights subsumed within the expression "the surety's right of subrogation" - in particular the equitable and statutory rights to stand in the place of the creditor and

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[74] See the Judicature Acts of 1873 (36 & 37 Vict., c. 66) and 1875 (38 & 39 Vict., c. 77).

exercise the latter's rights and remedies - will generally be immaterial. Insofar as they confer in personam rights only against the debtor, they will be of limited value. Insofar as they carry with them the entitlement to the benefit of any securities in the hands of the creditor, and the priority they afford, they are superfluous, for the rights of assignment achieve the same result more satisfactorily from the surety's perspective since he can enforce the securities in his own name.

In practice, therefore, it is the equitable and statutory rights of assignment that are most closely associated with, indeed even treated as, the surety's "right of subrogation".

It can be seen, therefore, that the expression the "surety's right of subrogation" may refer in any given case to a panoply of overlapping, related rights, or only a selection of them. "Subrogation" in the suretyship context does not, therefore, necessarily refer simply to the technique of subrogation as a means of effecting restitution, but also to the "ends" achieved by its use - in other words, the accumulated effects of its use in equity, at common law, and by statute. The danger of this, from the theoretical viewpoint, is twofold: not only does it confuse subrogation as a means to an end with the end itself, and thus encourage the identification of subrogation with that specific end even though it may be achieved without the use of the technique of subrogation; but it also separates the various rights and remedies acquired by subrogation in suretyship cases from the jurisprudential or juridical considerations that underlie their availability. This in turn tends to create a schematised, rather black and white view of the "right" of subrogation: either subrogation with its panoply of related rights and the advantages of

priority they carry with them is available in full, or it is not available at all.

Nonetheless, this broadly speaking was the position which obtained by the second half of the nineteenth century. Thereafter, the process of development of "the surety's right of subrogation" became primarily a matter of fleshing out this skeleton of rights. This paper is not concerned with many of these details. What is rather of concern is the fundamental nature of the rights, and the extent to which these rights of subrogation can be said to be explicable in terms of restitutionary principles. These questions will be considered in the next Part.

PART III

THE SURETY'S RIGHT OF SUBROGATION AND THE LAW OF RESTITUTION

Chapter 6

THE RESTITUTIONARY NATURE OF THE SURETY'S RIGHT OF SUBROGATION

A. Introduction

The law of restitution, as has already been seen,[1] is generally premised upon the principle of unjust enrichment.[2] That is to say, it is the existence of unjust enrichment that gives rise in law to an obligation to make restitution. To effect restitution - to remedy that unjust enrichment - the law employs various remedies, or remedial techniques known to the law. These may be drawn from the common law, such as a simple money judgment; or from equity, such as imposing a constructive trust over property, or declaring property to be subject to an equitable lien, or subrogating one party to the place of a second in order to have a remedy against a third. Subrogation, in other words, is drawn into the law of restitution as an equitable remedy, or remedial technique, available to effect restitution. Its particular distinguishing feature is that it can only be used in tripartite situations.

When a remedy is granted, or a remedial technique such as subrogation is used, the nature of the remedy and the result of using the remedial

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1 Supra, pp. 8-11.

2 Not all recent writers in the field of restitution agree with the view that the law of restitution is premised or founded on a principle of unjust enrichment. One notable exception occurs in the Canadian literature, for Fridman & McLeod expressly reject "unjust enrichment" as the juridical foundation of the law of restitution. While accepting that the notion of "unjust enrichment" perhaps provides a jurisprudential basis for restitutionary principles, they see the notion of "restitution" itself as the best foundation for the law of restitution; G.H.L. Fridman & J.G. McLeod, RESTITUTION (1982) (hereafter "FRIDMAN & McLEOD"), pp. 55-57.

technique will be dictated in essence by (a) the nature of the enrichment, and (b) the circumstances rendering the retention of that enrichment unjust. Further factors, however, such as that the recipient of the benefit has subsequently changed his or her circumstances in a way he or she would not otherwise have done, may also have to be taken into account, insofar as they affect the question whether it would be "unjust" to allow the recipient of the benefit to retain the benefit.

"Unjust enrichment" thus plays a dominating role in the formulation and presentation of a restitutionary claim. Not only does it give rise to the obligation to make restitution, but it dictates the nature of the relief effected. The principle of "unjust enrichment", however, as has already been pointed out,[3] is not merely a vague expression of intuitive or "palmtree justice" as it is sometimes accused of being. As Goff and Jones state in their leading text:[4]

> "[T]he principle of unjust enrichment is capable of elaboration and refinement. It presupposes three things: first, that the defendant has been enriched by the receipt of a benefit; secondly, that he has been so enriched at the plaintiff's expense; and thirdly, that it would be unjust to allow him to retain the benefit."

Each of the three central concepts, namely "benefit", "at the plaintiff's expense", and "unjust", can then, they emphasise,[5] themselves be elaborated and refined. For example, Goff and Jones break down the third of these

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[3] Supra, p. 9.

[4] Sir R. Goff & G. Jones, THE LAW OF RESTITUTION (3rd ed., 1986) (hereafter "GOFF & JONES"), p. 16.

[5] Ibid., p. 16 et seq..

elements, that of "unjust retention", into six broad classes of reason for denying restitution:[6]

> "(1) the plaintiff conferred the benefit as a valid gift or in pursuance of a valid common law, equitable or statutory obligation which he owed to the defendant;
> (2) the plaintiff submitted to, or compromised, the defendant's honest claim;
> (3) the plaintiff conferred the benefit while performing an obligation which he owed to a third party or otherwise while acting voluntarily in his own self interest;
> (4) the plaintiff acted officiously in conferring the benefit;
> (5) the defendant cannot be restored to his original position or is a bona fide purchaser;
> (6) public policy precludes restitution."

Goff and Jones's expression of the principle of "unjust enrichment" is one which has received considerable favour from judges and legal commentators alike, both in Canada[7] and elsewhere, although other formulations of the principle have also been put forward. Klippert,[8] for example, has suggested that an examination of the Canadian case-law in the restitutionary field reveals a slightly different expression of the principle of unjust enrichment. According to Klippert, there are four elements, or "control devices" as he terms them, on a restitutionary claim in Canada:[9]

> "The control devices underlying the principle of unjust enrichment in Canadian law might be reformulated in the following fashion:
> (i) that the defendant received a benefit at the plaintiff's expense,
> (ii) evidence of volition in the receipt or retention of the benefit,
> (iii) that the benefit was not voluntarily conferred, and

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6 Ibid., pp. 29-30.

7 See eg., the recent decision of the Canadian Supreme Court in Pettkus v Becker [1980] 2 S.C.R. 834, 117 D.L.R. (3d) 257.

8 G.B. Klippert, UNJUST ENRICHMENT (1983) (hereafter "KLIPPERT").

9 KLIPPERT, pp. 37-38. See also G.B. Klippert, "The Juridical Nature of Unjust Enrichment", (1980) 30 U.T.L.J. 356.

(iv) that the benefit is unjustly retained by the defendant.
A claimant who establishes these elements makes a prima facie case of liability against a defendant."

Like Goff and Jones, Klippert emphasises that these control devices are themselves capable of elaboration and refinement. Klippert also emphasises that the law of restitution is not concerned only with liability, but also with questions of remedies and defences. Thus, he suggests:[10]

"The control devices in unjust enrichment cases can be classified under three headings of substantive rights, defences, and remedies."

In asserting, therefore, that subrogation in general, and the surety's right of subrogation in particular, are essentially restitutionary in nature, as restitutionary writers do, and has been submitted in this paper, the assertion is made that one can find in the law governing restitution claims all these elements, or control devices, in one form or another. The object of the discussion in this Part is to consider whether and to what extent this is so.

B. The Restitutionary Features of a Surety's Right of Subrogation

(i) Receipt of a benefit at the surety's expense

The first, and most obvious, restitutionary feature of the surety's right of subrogation - and the various rights and remedies subsumed within that notion - is the requirement of payment or performance before the right is enforceable. This feature is common to all the rights, both equitable

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10 KLIPPERT, p. 37.

and statutory, enjoyed by a surety in the name of subrogation. The requirement was implicit rather than explicit in the early decisions on subrogation, since payment had in fact been made by the surety in those cases before the claim for assignment or otherwise was brought. It was made more explicit later, particularly when cases in the third of the classes of suretyship subsequently outlined by Lord Selborne L.C. in Duncan, Fox, & Co. v North & South Wales Bank[11] began to be recognised. Lord Selborne L.C. himself, in discussing the equitable rights of this third class of sureties (quasi-sureties whose rights arose from the fact of their being only secondarily liable), stated that the rights arose when the debt "is paid by the person who is not primarily liable".[12]

On occasion it has been stated that actual payment is not required, that the rights of the surety arise not at the time of payment but at the time of creation of the suretyship. Dixon v Steel[13] provides a leading example of this view. There, Cozens-Hardy J. commented:[14]

> "It certainly is not the law that a surety has no rights until he pays the debt due from his principal."

Where, as in that case, there was a contractual suretyship, then, held Cozens-Hardy J., the particular right there under consideration, namely, the surety's right against the creditor to have securities preserved for

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11 (1880) 6 App. Cas. 1, at 11.

12 Ibid., at 13 [emphasis added]. See also Lord Blackburn, at 18: "Though the indorser is primarily liable as principal on the bill, and is not strictly a surety for the acceptor, he has this in common with a surety for the acceptor, that he is entitled to the benefit of all payments made by the acceptor, and is entitled, on paying the holder, to be put in a situation to have a right to sue the acceptor." [emphasis added]

13 [1901] 2 Ch. 602.

14 Ibid., at 607.

his benefit, arose, at least in an inchoate form, at the time the parties entered into the agreement forming the basis of the contractual suretyship.

This view was not without support in the case-law. In Duncan, Fox, & Co.,[15] for example, Lord Selborne L.C. had said[16] that the rights enjoyed by sureties against creditors arose in his first class of suretyship upon the making of the contract of suretyship; and in his second class, upon the principal and surety giving notice to the creditor of their agreement that the principal would be primarily, and the surety only secondarily, liable for performance of the existing obligation.[17]

Lord Selborne L.C.'s comments were not, however, directed at the surety's equitable rights in general. Rather, they were directed at the particular equitable right of the surety against the creditor obliging the creditor not to deal with securities held by the latter to the prejudice of the surety's equitable rights to them. This right against the creditor, as has already been pointed out,[18] is in the nature of an independent right

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15 (1880) 6 App. Cas. 1.

16 Ibid., at 11.

17 See also In re A Debtor [1937] Ch. 156, where the Court of Appeal held that the principal debtor's "obligation" to reimburse the surety was "incurred", at least for the purposes of s. 4 (1) of the Law Reform (Married Women and Tortfeasors) Act of 1935 (25 & 26 Geo. 5, c. 30), at the time that the surety agreed to guarantee the debtor and entered into a contract of guarantee. The court left open the question of when the "obligation" arose or was incurred "where a guarantee is given without any antecedent request on the part of the debtor" (at 166, per Greene L.J.). "That case", said Greene L.J., at 166, "is merely one example of a number of cases where the law raises an obligation to indemnify irrespective of any actual antecedent contractual relationship between the parties ... ", [such as existed in this case].

18 Supra, p. 57.

against the creditor, and as such does not depend upon the operation of the technique of subrogation for its existence.

In contrast, when the surety seeks to bring an action in equity against the debtor employing, by virtue of subrogation, the rights and remedies of the creditor, then at that point, it is submitted, actual payment is a pre-requisite of the surety's rights and remedies.

The comments of Cozens-Hardy J. in Dixon v Steel[19] do not necessarily conflict with this, for, as indicated, the particular right of the surety there under consideration was the surety's right against the creditor not to have the securities held by the latter dealt with to the prejudice of the former's rights to them. The securities themselves, it is submitted, would not have been enforceable by the surety in the exercise of her equitable rights of subrogation until she had paid the guaranteed debt.

Payment or performance, it is submitted, is therefore a necessary prerequisite of the rights of subrogation, in the sense that until payment or performance, the rights of subrogation cannot be enforced by the surety.

Payment or performance is also required before a surety or quasi-surety can enforce the statutory rights of subrogation. This follows from the wording of section 5 of the Mercantile Law Amendment Act of 1856:

"Every Person who ... shall pay such Debt or perform such Duty ...".[20] This, it has been held, requires actual payment or performance in full.[21] Until payment is made in full, or performance effected in full, then, it

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19 [1901] 2 Ch. 602.

20 19 & 20 Vict., c. 97. [Emphasis added]

21 Ferguson v Gibson (1872) L.R. 14 Eq. 379, at 386, per Wickers V.C.

has been held,[22] the various rights conferred by section 5 - in particular the right to the assignment of judgments, securities and so on - do not arise.

The rights subsumed within the expression "the surety's right of subrogation" can only be enforced, in other words, when the surety or quasi-surety actually confers a "benefit" upon another, whether by way of the satisfaction of some monetary liability of that other to a third person, or by way of the performance of some duty of that other to a third person. The idea that rights and remedies against another begin with or are only enforceable upon the conferral of a benefit upon that other, whether directly, or indirectly as in subrogation cases, is, of course, the cornerstone principle of current notions of restitution.

Furthermore, it is self-evident that the payment or performance must have been by the surety or quasi-surety, since payment or performance by the principal would have discharged the surety's obligation to answer for the principal. The benefit thus conferred on the principal by the surety's payment or performance is, therefore, by definition "at the expense of" the surety.

Payment or performance, or the "benefit" thereby conferred, also operates as a limitation upon the surety's rights of recovery from the principal debtor. In seeking reimbursement from the principal debtor, or

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[22] Re Howe; Ex parte Brett (1871) L.R. 6 Ch. App. 838, at 841, per Mellish L.J. See also Ewart v Latta (1865) 4 Macq. H.L. 983 (Scot.), where Lord Westbury L.C., in considering whether a surety could compel the creditor to resort to - or "discuss" - the principal before seeking satisfaction from the surety, stated: "It is quite a misapprehension to suppose that there is any equity entitling the surety to compel the creditor to discuss the principal - unquestionably the surety has no right unless he pays the whole debt."

from co-sureties, and in relying on subrogation as a means of obtaining the benefit of the rights, remedies, and securities of the creditor and thereby better securing reimbursement, the surety is limited by the amount actually paid by himself or herself, or by the value of his or her actual performance.[23] So, if the surety settles the creditor's claim for less than the full amount of the guaranteed debt, he or she cannot then recover the full amount of the debt from the debtor, either directly by way of reimbursement or indirectly through subrogation. The "benefit" conferred upon the debtor can be recovered, but no more. The surety is entitled to restitution only, and is not entitled to turn a profit on the transaction.[24]

"Payment" or "performance" must, however, be proved by the surety. In this regard, "payment" and "performance" mean payment or performance both in fact and in law. The latter requirement - payment or performance <u>in law</u> - can be a source of considerable difficulty. The reason for this is that the mere fact of payment will not of itself necessarily amount to "payment" in law. The fact of payment, in other words, in the suretyship context, will not necessarily operate in law as a discharge of the guaranteed debt. The payment may, for example, have been made in circumstances in which the legal effectiveness of the payment can be vitiated. This would be so, for example, if the payment were made under duress, or under undue influence. At law, the payment in these circumstances may be vitiated, in which event

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[23] Assessment of the value of performance - of services in other words - can be problematic. See generally GOFF & JONES, pp. 18-22.

[24] Exceptionally, where the claimant can establish a proprietary right, rather than just a personal claim against the principal debtor, the claimant may appear to recover more than he or she conferred upon the debtor. See generally, GOFF & JONES, chap. 2; FRIDMAN & McLEOD, chap. 20.

the payment will not be held to be legally effective to discharge the debt. The debt in respect of which the payment was in fact made will at law remain intact and enforceable by the creditor against the debtor. Since the debt is not thereby discharged, the payment in fact confers no benefit in law on the debtor - the principal - at the expense of the payor. The law will not, therefore, impose an obligation on the debtor to make restitution of the benefit to the payor.

The payor, however, will not necessarily be without any remedy. Since the creditor can still sue the debtor for the debt, it would be unjust for the creditor also to retain the payment made to him or her by the payor. To let the creditor do so would be to allow him or her unjustly to retain the benefit conferred upon the creditor - the payment - at the payor's expense. The principle of unjust enrichment would apply to impose an obligation on the creditor to effect restitution of the payment to the payor. This the law recognises, and a restitutionary claim may be brought by the payor against the creditor for a simple money judgment, based on the traditional quasi-contractual count of "money had and received".[25]

(ii) Voluntariness and volition

The question whether payment or performance by the surety of the guaranteed obligation has conferred a benefit upon the principal debtor so as to give rise to a restitutionary right of recovery from the principal debtor may arise in a slightly different form. For example, the payment may

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[25] See generally, GOFF & JONES, chaps. 3, 4, 9; FRIDMAN & McLEOD, chaps. 3, 4, 6.

have been made by someone who is not actually bound to pay it but chooses to do so, without however intending the payment to be a gift to the debtor,[26] or by someone who felt compelled by circumstances to pay it even though he or she may not have previously agreed to do so. The payor in these cases encounters a different problem in seeking recovery from the principal debtor. It is a cardinal principle of the law of creditor and debtor that a person who is a "stranger" to the debt of another cannot "voluntarily" or "officiously" pay off that debt, and thereby substitute himself as a creditor of that other in place of the original creditor, against the wishes of the debtor. If he or she purports to do so, he or she will in general be denied rights of recovery from the debtor in relation to the payment.[27]

Traditionally, the denial of rights of recovery in these circumstances has been justified on the basis that neither the common law nor equity will require persons who have had "benefits" "forced" upon them by others, against their wishes and without their request or acquiescence, to pay for those benefits. Such benefits, it is said, are conferred "voluntarily" or

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[26] Gifts, if effected in the manner required by law, cannot of course be recovered by the donor, whether on restitutionary principles or otherwise.

[27] The law does, however, allow the payor to ask the creditor to assign the debt to the payor in consideration of the payment. The debt will then be enforceable by the assignee payor against the debtor, provided that notice of the assignment is given to the debtor. The debtor's consent to the assignment is not necessary. See generally: Halsbury, LAWS OF ENGLAND, (4th ed., 1974), vol. 6, Choses in Action.

"officiously".[28] The essence of this is encapsulated in the oft-repeated comment of Pollock C.B. in Taylor v Laird:[29]

"One cleans another's shoes; what can the other do but put them on?"

This approach does not deny that a "benefit" - the discharge of the debt effected by the payment in the context of suretyship - was conferred upon the intended beneficiary of the payment. Rather, it expresses the perception that the beneficiary is not in any way "at fault" in the transaction; having had the benefit forced upon him or her, he or she should not therefore be required by the law to make restitution to the person who conferred the "unsolicited" benefit upon him or her. As between the two, using restitutionary terminology, it would be equally, if not more, "unjust" to require the recipient to make restitution as it would be to let the person who conferred the benefit thereby suffer a loss occasioned by his or her own "officious", "voluntary", or "unsolicited" conduct.

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[28] It has, however, been pointed out that terms such as "voluntarily", "officiously", and so on, are effectively just a "form of legal shorthand" used to express the fact that none of the numerous reasons that serve to negate "voluntariness" or "officiousness" exists in the particular case; see J.P. Dawson, UNJUST ENRICHMENT : A COMPARATIVE ANALYSIS (1951), pp. 127 et seq.; see also GOFF & JONES, pp. 42-44. Goff & Jones identify seven general grounds which they say will serve to negate a finding of "officiousness". They are: (i) if money had been paid under a mistake of fact; (ii) if land has been mistakenly improved with the defendant's acquiescence; (iii) if chattels have been mistakenly improved; (iv) if services have been mistakenly rendered; (v) if benefits have been conferred under duress, or undue influence, or compulsion of law; (vi) if benefits have been conferred under contracts void for want of authority, mistake or uncertainty; and (vii) if benefits have been conferred in anticipation of a transaction which does not materialise; GOFF & JONES, p. 43. Grounds (i), (v), (vi) and (vii) can be applied to payments of money.

[29] (1856) 25 L.J. Ex. 329, at 332.

This use of the notion of "voluntariness", or "officiousness", as a control device on recovery by the payor, is another reflection of the resitutionary nature of the surety's rights upon payment, including the right of subrogation. As has already been seen,[30] "voluntariness" or "officiousness" is one of the fundamental control devices built in to the principle of unjust enrichment.

Recently, however, it has been suggested[31] that there is another, perhaps more fundamental reason why the "officious surety" who purports to pay off the debt of another cannot recover from the debtor. The reason, it is said, goes back to the notion of "benefit" itself. The "voluntary" or "officious" payment, it is said, does not in law discharge the debt, contrary to the assumption made in the above view. The debt is only discharged, it is said, if the payment was either made with the debtor's "authority", or was "subsequently ratified" by the debtor.[32] In the absence of authority or ratification, the debt is not in general discharged at law, and no "benefit" is therefore conferred upon the debtor. Correlatively, there can be no question of restitutionary recovery of the payment by the surety or quasi-surety from the principal debtor.

To be entitled to restitutionary recovery of the payment from the debtor, according to this view, it is incumbent upon the payor to point to something in the circumstances surrounding the payment which shows that the

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30 Supra, p. 83.

31 For a detailed discussion of the authorities, see P. Birks & J. Beatson, "Unrequested Payment of Another's Debt", (1976) 92 L.Q.R. 188. See also W.R.C., "Intervenors and Unjust Enrichment", (1975) 38 Mod. L.R. 563; D. Friedmann, "Payment of Another's Debt", (1983) 99 L.Q.R. 534; GOFF & JONES, pp. 16-18 (esp. at n. 90), pp. 528-31.

32 GOFF & JONES, p. 17 (esp. at n. 90).

payment was not made "voluntarily", or that even if it was made voluntarily, the debtor nonetheless subsequently "assented to" or "ratified" the payment.[33] Only then, it is said, will the law hold that the debt has been effectively discharged; and only then can the payor claim indemnity or reimbursement from the debtor, and call in aid such further remedial techniques as subrogation.

In suretyship cases, the surety will generally point either to the prior agreement with the debtor whereby the surety undertook to pay the debt of the principal, or to a prior request, express or implied, from the latter to the former to pay the debt, to establish that a payment by the surety was not voluntary vis-å-vis the debtor. If an agreement or a request is established, this will lead to the conclusion that the payment was in a general sense "authorised" by the debtor, and that will in turn, according to this view, mean that the debt is considered discharged at law by the payment.

If the payor cannot point either to prior agreement, or to a prior request, then the payment will prima facie be "voluntary" in the eyes of the law, and thus, it is said, be ineffective at law. The payor may still be able to dispel this conclusion, however, by pointing instead to subsequent "assent", or "ratification" by the debtor;[34] something, in other words, which amounts to an adoption of the payment. If this is proved, it is said, it will equally lead to the legal conclusion that the payment was not "voluntary", that it was consequently legally effective to discharge

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[33] Idem. Birks & Beatson, loc. cit., use "assent to"; whereas Goff & Jones, using the analogy of agency, talk of subsequent "ratification", GOFF & JONES, p. 17, (esp. at note 90).

[34] Idem.

the debt, and that the principal debtor[35] should accordingly be prima facie liable to reimburse the payor.

This analysis of the payor's rights of recovery from the debtor thus places a premium upon the requirement of "payment" as a prerequisite of the surety's rights, including the rights of subrogation. If there is payment in fact, and some factor such as prior agreement or request, or subsequent assent or ratification, then, according to this view, two consequences follow: first, the payment is not "voluntary"; and secondly, and in consequence,the payment is legally effective, and a "benefit" is conferred on the debtor.[36]

The traditional approach, on the other hand, places less of a premium upon payment and "benefit" as the main control device on restitutionary recovery. Instead, it considers that a "benefit" has been conferred upon the debtor, but that because it was "forced" upon the debtor, "justice" dictates that the debtor should not be made liable to the payor.

Klippert's formulation of the principle of unjust enrichment[37] offers yet a third possible analysis of the payor's rights of recovery from the debtor. According to Klippert, Canadian law has placed some emphasis on the notion of "volition" in the receipt or retention of a benefit as a control device on a restitutionary claim. It is not enough, he suggests, that a

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35 The payor and the debtor may be equally liable, in which case the payor's primary right is to contribution, not reimbursement; see discussion supra, p. 46 et seq..

36 Goff J. (as he then was) adopted this "discharge or not?" approach in Barclay's Bank v Simms [1980] Q.B. 677, in holding that a bank which had mistakenly honoured a cheque in disregard of a stop instruction was entitled to recover that sum from the payee. But see Friedmann, loc. cit., pp. 546-47.

37 Supra, pp. 83-84.

benefit has been conferred, and that it was not conferred voluntarily; there must be evidence of volition on the part of the person on whom the benefit was conferred before a restitutionary right of recovery should be recognised. Applying this to the problem of the "voluntary" payment, one could therefore say that it is the existence of volition in the receipt or retention of the benefit that will ultimately dictate whether or not the principal debtor is liable to the surety. Payment by a "stranger" will prima facie be "voluntary", and will neither discharge the debt, nor confer a benefit upon the debtor, unless the debtor has, in other words, done something "volitional" to make that payment legally effective. What the debtor does, of course, that evidences and establishes this necessary element of "volition" is (1) to contract for or request the payment prior to payment, or (2) assent to or ratify it after the fact of payment. His "volition" transforms what would otherwise be an ineffective "voluntary" payment into a legally effective payment that discharges the debt and thereby confers a benefit on the debtor. The debtor's restitutionary liability to the surety who made the payment on the debtor's behalf thus rests in substance on the debtor's own actions or conduct. The injustice of letting the debtor retain the benefit is all the more heightened.

There is, however, a third general means of negating the suggestion that a payment was made "voluntarily" and thus can not be the basis of a restitutionary right of recovery. This is to show that there was some other factor in the circumstances of the case, besides agreement or request, that "legally compelled" the payor to make the payment in the first place.[38] One

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[38] Of course, the payor may also be said to have been "legally compelled" by virtue of the guarantee he or she gave pursuant to an agreement with the debtor (and perhaps also with the creditor).

such factor would be a statutory provision, as in Brook's Wharf & Bull Wharf Ltd. v Goodman Bros.,[39] where the plaintiffs were compelled by statute to pay customs duties which the defendants were primarily liable to pay. That legal compulsion meant that the plaintiffs' payment was not "voluntary" or "officious" in the eyes of the law, but was fully effective at law in discharging the defendants' liability to pay the customs duties. Since, under the statute, the defendants were primarily liable for payment of the duties, the plaintiffs were therefore entitled to recover the amount of the payment by way of duties from the defendants.[40] Furthermore, it would seem that the plaintiffs would be entitled, by virtue of their right of subrogation, to have the benefit of the rights and remedies of the Crown, as the paid-off creditor, against the defendants, as the principal debtor.[41]

In the absence, therefore, of agreement, request, subsequent ratification, or some other factor giving rise to legal compulsion, there is then little likelihood of recovery from the debtor on a restitutionary basis, whether this is so because there was no "benefit" conferred on the debtor by the payment, because any benefit that was conferred was

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39 [1937] 1 K.B. 534.

40 Ibid., at 546.

41 There is one important general constraint upon recovery where the payor says that he or she was "legally compelled" to pay the debt, whether by virtue of some "external" factor, or of a guarantee agreement with the creditor (without the debtor's agreement, request, or subsequent ratification). The payor must also show that he or she did not voluntarily or officiously create, or subject himself or herself to, the circumstances or factor subsequently giving rise to the legal compulsion to pay. The payor cannot, in other words, voluntarily assume liability and then purport to rely on payment pursuant to that legal liability in order to raise a right of recovery against the debtor. This was essentially what happened in Owen v Tate [1976] Q.B. 402; discussed infra, p. 98 et seq..

"voluntarily" or "officiously" "forced" upon the debtor, or because there was no volition on the part of the debtor in receiving or retaining any benefit. The payor consequently obtains neither rights of reimbursement against the debtor, nor, correlatively, rights of subrogation to assist in obtaining reimbursement.

Nevertheless, the payor should not be considered entirely without remedy. As in the case of a vitiated payment, he or she should in principle be entitled to recover from the creditor the money paid to the creditor, relying essentially on the quasi-contractual, or restitutionary, claim of money had and received based upon a total failure of consideration.[42]

Thus, it is theoretically possible to see concepts that lie at the heart of the law of restitution and form elements of the principle of unjust enrichment evidenced and reflected in the law governing sureties and their rights upon payment, including the right of subrogation. It has to be said, however, that the case-law in this regard has not always applied these concepts consistently. One particular case in this regard which has been the focus of a great deal of criticism is the relatively recent decision of the English Court of Appeal in Owen v Tate.[43]

(iii) Owen v Tate[44] - an illustrative case

Owen v Tate does not expressly relate to or consider subrogation. This, as will be seen, is one of the criticisms directed at the Court of

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42 Birks & Beatson, loc. cit., p. 205; GOFF & JONES, p. 17 (n. 90).

43 [1976] Q.B. 402.

44 Idem.

Appeal. Nonetheless, it is perhaps the leading recent case in English law upon the nature and effect of "voluntary" or "officious" payments by a surety, and therefore justifies consideration in some detail.

The facts were relatively simple. Mr and Mrs Tate obtained a loan from Lloyds Bank. It was secured by a charge by way of legal mortgage upon the property of a Miss Lightfoot. Owen, who was in no way connected with the transaction, but was a former employer of Miss Lightfoot, was subsequently approached by her for advice as to how to regain her deeds from the bank. To help her, but without consulting the Tates, Owen deposited £350 with Lloyds Bank and signed a form of guarantee by which he guaranteed payment of all money, limited to £350, due, owing, or incurred to Lloyds Bank by the Tates. The bank thereupon, apparently against the protest of the Tates, released Miss Lightfoot from her obligations to the bank and returned her deeds. Subsequently, the bank applied the £350 in repayment of the Tates' debt to the bank. Various letters written on behalf of the Tates prior to the bank applying the £350 to settle their debt appeared to invite the bank to clear the debt by recourse to the £350 deposited by Owen.[45]

Owen brought an action against the Tates claiming reimbursement of the sum of £350. He argued that he was a surety, that he had effected payment of the guaranteed debt pursuant to the guarantee given by him to the bank, and that he was thereby, on established principles, entitled to reimbursement from the Tates. Particular reliance was placed upon a passage of Greene L.J. in In re A Debtor.[46] Specifically, in considering the

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45 There was some dispute as to the facts on this point.

46 [1937] Ch. 156, at 166.

when rights of reimbursement were created in a contractual suretyship case, Greene L.J. commented:[47]

> "A question may arise as to the application of the sub-section [under consideration in that case] in a case where a guarantee is given without any antecedent request on the part of the debtor. That case is merely one example of a number of cases where the law raises an obligation to indemnify irrespective of any actual antecedent contractual relationship between the parties."[48]

This passage, argued Owen, applied to his payment. He had been "compelled by law", he argued, as a result of the guarantee he had entered into, and the Tates' actions, to "pay"[49] the debt in circumstances which should lead the law to impose an obligation of reimbursement upon the Tates.

The Tates resisted Owen's claim. His argument, they replied, was faulty. Owen, they said, had acted "voluntarily" or "officiously" in entering into the guarantee in the first place. How then, they asked, could he say that he had therefore been "compelled by law" to "pay" the debt? Owen had forced himself upon them, they argued, in circumstances such that they had had no choice but to accept the benefit of his payment. The law, they argued, would go too far were it to impose an obligation of reimbursement upon them on those facts.

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47 Ibid., at 166.

48 Emphasis added.

49 "Payment" on the facts of this case really referred to the application of the funds, previously deposited by Owen, by the bank in settlement of the Tates' debt to the bank. This the bank did pursuant to the guarantee Owen had given to the bank. Clearly, Owen was not "compelled by law" to enter that guarantee or deposit the funds with the bank. The "legal compulsion" occurred when the bank enforced that guarantee against him and applied the funds on deposit, pursuant to the Tates' invitation to do so. It was only at this point that there could be said to be "payment" of the debt.

The difficulty with this argument, countered Owen, was that the Tates had "requested" the bank to have recourse to the fund deposited by him with the bank, in order to discharge their debt. Without that, he argued, the bank would not have had recourse to Owen pursuant to the terms of the guarantee. Even if his initial actions were "voluntary" or "officious", as certainly it seems they were, this "request", he argued, evidenced the Tates' adoption of his payment to their advantage. That, he argued, justified the law in imposing an obligation of reimbursement upon them.

The Court of Appeal ruled against Owen. In the view of Scarman L.J., with whom both Stephenson and Ormrod L.JJ. broadly agreed,[50] there was a need for:

> "a broad approach ... to the question whether in circumstances such as these a right of indemnity arises, and that broad approach requires the court to look at all the circumstances of the case. ... [T]he fundamental question is whether in the circumstances it was reasonably necessary in the interests of the volunteer or the person for whom the payment was made, or both, that the payment should be made -whether in the circumstances it was 'just and reasonable' that a right of reimbursement should arise."[51]

On the other hand, Owen was clearly a "volunteer" at the time he purportedly assumed liability as the Tates' surety:

> "[Owen] assumed the obligation of a guarantor behind the back of the [Tates] ..., against their will, and despite their protest. ... [Owen] was as absolute a volunteer as one could conceivably imagine anyone to be when assuming an obligation for the debt of another."[52]

On those facts alone, Owen would clearly have no rights of recovery from Tates. The important question, therefore, was whether the later actions of

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[50] Both judges, however, added their own comments on the reasons for the failure of the plaintiff's claim.

[51] [1976] Q.B. 402, at 409-10.

[52] Ibid., at 410.

the Tates in apparently "requesting" the bank to have recourse to Owen's funds to pay off their debt altered the legal position?

> "[M]ust one read the subsequent letters to the bank ... as an adoption by the [Tates] ... of a benefit conferred upon them by the plaintiff?"[53]

Scarman L.J. went on:

> "[The Tates] never wished to lose the security of Miss Lightfoot's deeds. They lost it through circumstances outside their control and notwithstanding their protest. When the bank decided to call in the debt the defendants no longer had the security for the overdraft which was acceptable to them: they had to put up with a security which without their consent or authority had been substituted by [Owen] ... for that which was, or had been, acceptable to them and agreed by them. I do not criticise the [Tates] ..., nor do I think they can be reasonably criticised, for making the best of the situation in which they then found themselves, a situation which they did not desire, and one which I doubt ever appeared to them as beneficial."[54]

He concluded:

> "[Owen] ... has failed to make out a case that it would be just and reasonable in the circumstances to grant him a right to reimbursement."[55]

Scarman L.J. then formulated what he thought was "the true principle of the matter ... without reference to volunteers or to the compulsions of the law":[56]

> "If without an antecedent request a person assumes an obligation or makes a payment for the benefit of another, the law will, as a general rule, refuse him a right of indemnity. But if he can show that in the particular circumstances of the case there was some necessity for the obligation to be assumed, then the law will grant him a right of reimbursement if in all the circumstances it is just and reasonable to do so."[57]

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53 Ibid., at 411.

54 Idem.

55 Idem.

56 Idem.

57 Ibid., at 411-12.

Stephenson L.J., in agreeing,[58] commented that he could not see:

> "in the circumstances of loan and guarantee as far as they emerged at this trial any sufficient reason for imposing that obligation to indemnify on this debtor in favour of this guarantor. ... [Owen] was not under such constraint as may be one of the ways of creating a right which it is just and reasonable that a guarantor should have, as a general rule, to be indemnified by the debtor whose debt he has discharged."[59]

Ormrod L.J. also agreed,[60] but was more cautious in his general approach to the question confronting the court. He observed:[61]

> "This case demonstrates clearly ... the wisdom of the common law approach to the volunteer, which may be cautious, and perhaps unkind, if not cynical, because looked at superficially this case could be said to be one in which the [Tates] ... had acquired a considerable benefit from the acts of ... [Owen] and had given nothing in return. But a glance through the correspondence indicates that the transaction in this case is only a part of a much more complex series of transactions which have been going on between various people for some years. ... I find it quite impossible to sort out the rights and wrongs in this case, and certainly quite impossible to say whether or not the [Tates] ... in fact received a benefit by [Owen] ... undertaking an obligation of guarantor which had previously been undertaken by Miss Lightfoot. It seems to me possible that the [Tates'] ... position was worsened ... by the intrusion of [Owen] ... rather than helped ...".

The Court of Appeal thus dismissed Owen's claim for reimbursement from the Tates.

What, in the view of the recent writers, is wrong with the decision? Broadly speaking, two general criticisms have been levelled at the reasoning of the members of the Court of Appeal. The first is that the members of the Court of Appeal failed in substance to direct their minds to the question whether Owen's payment had effectively discharged the debt at

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58 Ibid., at 412.

59 Ibid., at 413. [Emphasis added]

60 Idem.

61 Idem.

law.[62] The conclusion the judges came to, it is said, is internally inconsistent. As Goff and Jones argue:[63]

> "in English Law a debt can only be discharged with the consent or subsequent ratification of the debtor. If the debt had been discharged by the surety's payment, it can only have been because the debtor has adopted that payment; the plaintiff should have been able to recover from the debtor. However, in Owen v Tate, the Court of Appeal found that the debtor had not adopted the payment, even though 'they invited the bank [the creditor] to clear their overdraft by recourse to the plaintiff.' It must follow that the debt was not discharged at law. In such circumstances, the plaintiff should normally be able to recover his payment from the creditor on the ground of total failure of consideration."

In other words, recovery from the Tates was denied because Owen's payment was not legally effective; yet recovery from the bank on the ground of total failure of consideration was also denied. This, it would seem, meant that the payment must have been legally effective, at least as between Owen and the bank. Goff and Jones suggest an explanation for this:[64]

> "In Owen v Tate, however, it would appear that the bank would have been able to retain its payment, for the bank had released another surety, at the plaintiff's request and in consideration of his guarantee."

The result, Goff and Jones argue, is that:

> "The bank would then be at law in a position to retain the plaintiff's payment and to recover the debt, which is a palpably indefensible result. Conversely, if the bank did not sue for the debt, the debtor would be incontrovertibly benefited."[65]

Birks and Beatson, in a detailed consideration of the law regarding

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62 Stephenson L.J. assumed it had, as is clear from the passage quoted at n. 59 above. Neither Scarman nor Ormrod L.JJ. expressly decided whether the payment discharged the debt in law.

63 GOFF & JONES, p. 530.

64 Idem.

65 Idem.

the payment of another's debt,[66] also criticise the decision in Owen v Tate on this score. They argue that Owen's claim could not be supported on the ground that Owen had been "legally compelled" to pay the debt when he was only secondarily liable for it, since there is:

> "no basis for adversely distinguishing the position of one who voluntarily assumes an obligation to pay and then pays from that of one who merely pays."[67]

In either case, the payor is simply a "volunteer". Owen's "strong quasi-contractual" claim, as they termed it,[68] based on "legal compulsion", was, therefore, correctly dismissed.

But, they argue, Owen could also raise what they termed a "weak quasi-contractual" claim, based upon the fact that the debtor had subsequently "approved" the payment. The general rule, where payment has been assented to, they submit, is:

> "the volunteer can recover from an assenting debtor, unless the assent is given in the belief that the intervener acted donandi animo or is not material to the perfection of the discharge."[69]

Since, on the facts, assent appeared to exist, and since there was no question of Owen acting donandi animo, prima facie recovery by the payor should have been permitted; yet recovery was denied. The explanation for this, they suggest, must be that the assent was "not material to the perfection of the discharge"; that:

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66 Birks & Beatson, loc. cit..

67 Ibid., p. 209.

68 The terms "strong quasi-contract" and "weak quasi-contract" were adopted by Birks and Beatson from an earlier article by Birks, "Restitution for Services", (1974) 27 C.L.P. 13, 13-14.

69 Birks & Beatson, loc. cit., p. 209.

> "contrary to the usual rule [regarding voluntary payments], this voluntary payment automatically discharged the debt."[70]

But, in their view, there was neither authority nor reason for drawing such a distinction between a payment by a person who had voluntarily assumed liability to pay and then paid pursuant to the "legal compulsion" of that liability, and a straightforward payment. Both cases were equally classifiable as "voluntary". If payment in the latter case does not automatically discharge the debt, there is no reason, they argue, why it should do so in the former case.[71] The restitutionary consequences for the payor if the debt was automatically discharged in the former case, they argued, would be "savage".[72] But if that was the law, then assent was material, indeed crucial, to the result of the case. If it existed, then the debt was discharged at law and recovery from the debtor was normally granted. If it did not, then the debt was not discharged and no recovery was possible:

> "if the payment did not automatically discharge the debt, the respondent's discharge lay in his own election and his assent satisfied the conditions for the weak quasi-contractual claim."[73]

This "weak quasi-contractual" claim, they observe, was not, in substance, considered by the Court of Appeal, which instead:

> "treated ... [Owen's] case as resting solely on strong quasi-contract and, in particular, on the question whether secondary liability, however incurred, was invariably sufficient to negative the voluntary character of the payment."[74]

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70 Idem.

71 Ibid., p. 209-10.

72 Ibid., p. 210.

73 Ibid., p. 209.

74 Ibid., p. 208.

Since that question, they agreed,[75] had to be answered against Owen, his claim for reimbursement was inevitably dismissed.

Both Goff and Jones, and Birks and Beatson, thus criticise the decision of the Court of Appeal in Owen v Tate for failing to consider or analyse coherently the legal effect of Owen's payment in relation to the debt.

Had the judges in the case done that analysis, both sets of writers suggest, the decision may have been different. In the first place, as just discussed, if the court had expressly held that the Tates had adopted or assented to the payment, then the payment could not be said to be "voluntary". Accordingly, the debt would have to be considered discharged, and this would in turn lead to a right of recovery from the beneficiary of the payment, ie. the Tates. In other words, if the court had applied the law regarding discharge of debts as these writers assert it to be, then the existence of assent ought to have led to recovery.

If, however, after analysis, the court concluded that the Tates had not "assented", and the debt was held not to have been discharged by Owen's payment, then the result would prima facie be that the Tates never received the "benefit" of Owen's payment, and recovery from them ought consequently to be denied, as indeed it was.

Prima facie, this analysis does not affect the question of the rights of recovery from the bank on the basis of total failure of consideration. Both sets of writers agree that if the debt was not legally discharged, a claim against the bank would still probably fail because, on the facts, the bank's agreement to discharge Miss Lightwood and accept Owen in her place

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[75] Ibid., p. 209.

as surety would constitute sufficient consideration to prevent Owen claiming total failure of consideration. The bank could, in other words, retain the payment as against Owen, even though as against the Tates the payment did not discharge their debt at law.

This would lead in theory to the anomalous result that, since the debt remains due, the creditor bank could enforce it against the Tates, thereby recovering twice. If it chose not to do so, then, say Goff and Jones, this would confer an "incontrovertible benefit" upon the Tates.[76] The result, they assert, would be "palpably indefensible".[77] This suggests to them that perhaps something was overlooked by the court in Owen v Tate. That something, they and other writers suggest, is subrogation.[78] Goff and Jones, for example, argue that:[79]

> "though the surety may have been officious vis-à-vis the debtor, he had not acted officiously vis-à-vis the creditor, the bank, which voluntarily and consciously accepted his suretyship and his payment. For that reason, and to prevent the possibility of the bank's unjust enrichment, the surety should in such circumstances be entitled to be subrogated to the bank."

Thus, even though Owen may not have been entitled to a direct right of reimbursement from the Tates, on the ground that his payment was "voluntary" or "officious", it is said that he should nonetheless on the

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76 GOFF & JONES, p. 530.

77 Idem.

78 Other methods also present themselves as a means of avoiding this result. Goff & Jones suggest that it might be considered a fraud on the payor were the creditor to seek recovery of the debt from the debtor (see Hirachand Punamchand v Temple [1911] 2 K.B. 330); or that there may in these circumstances be a defence in equity (see Porteous v Watney (1873) 3 Q.B.D. 534, at 540, per Thesinger L.J.); GOFF & JONES, p. 530 (at n. 57). Other methods which suggest themselves include perhaps estoppel by conduct, and constructive trust.

79 GOFF & JONES, pp. 530-31. [Emphasis added]

facts of the case have been subrogated to the rights of the bank against the Tates, including in particular - perhaps even limited to[80] - the bank's personal claim against the Tates on the debt. In this way, argue Goff and Jones, restitution could be done between Owen, the Tates, and the bank, where it would not otherwise be.[81] They are, accordingly, critical of the the Court of Appeal in Owen v Tate for not having considered subrogation in this way.

Birks and Beatson level the same criticism at the Court of Appeal in Owen v Tate. Owen, they assert, should have been entitled to subrogation on the facts of the case as a means of effecting recovery from the debtor:

> "If we are wrong to argue that the voluntary surety's payment does not automatically discharge the principal debt [ie. the payment does discharge the debt even though it is 'voluntary' in the sense that it was neither paid pursuant to a prior agreement or request nor given effect to by the assent of the debtor], we think that he ought nevertheless to be subrogated to the creditor's rights against the debtor in order to recoup his payment."[82]

Such a right, they concede, would:

> "conflict with a basic rule of restitution, namely that a volunteer cannot recover from his beneficiary unless the conditions of the weak

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[80] Goff & Jones suggest that it is a "distinct question whether a surety whose guarantee has been accepted by the creditor should succeed to the creditor's lien over securities deposited by the debtor"; GOFF & JONES, p. 530 (at n. 57a).

[81] It is not entirely clear, however, whether Goff & Jones see this argument for subrogation as applying only in the event that the payment did not discharge the debt at law, or also in the event that the payment does discharge the debt at law but still does not give rise to a right of reimbursement because the payor "thrust himself on the debtor", (GOFF & JONES, p. 530). Their earlier comments regarding adoption of the debt suggest the former, since they are unqualifed in asserting that a right of recovery from the debtor arises where the debt has been discharged at law.

[82] Birks & Beatson, loc. cit., p. 210.

> quasi-contractual claim are satisfied. It would therefore be an anomaly within the law of restitution ... ".[83]

The "justification" for conferring such a right, they continue,

> "would be that the denial of restitution is equally anomolous since, from the narrower perspective of the law relating to voluntary discharge, the unintended consequence of the rule decreeing automatic discharge is to render the position of the voluntary surety uniquely hard."[84]

Birks and Beatson thus advocate the conferral of a right of subrogation upon the "voluntary" or "officious" payor in the event that the debt is at law discharged by the payment; but not, it would seem, in the event that the debt is not discharged. In their view, the fact that the debt has been discharged means that the debtor has therefore been "benefited" by the payment. Subrogation, they argue, would relieve the debtor of the unjust enrichment he would thereby otherwise obtain at the payor's expense.

Though both Goff and Jones, and Birks and Beatson, thus advocate the use of subrogation as a means of remedying the "injustice" apparent, in their views, in Owen v Tate, and criticise the Court of Appeal for not having considered this, there are marked differences between their respective arguments. Most significantly, whereas Goff and Jones argue that subrogation should be used to confer on the payor rights of recovery against the debtor in order to prevent the creditor's unjust enrichment, even though the debt is not discharged and no benefit is necessarily conferred upon the debtor,[85] Birks and Beatson limit recovery from the

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83 Idem.

84 Idem.

85 Goff & Jones argue that if, on the facts of Owen v Tate, the payment cannot be recovered from the debtor because the debt was not discharged, but recovery of the payment from the creditor is also not possible because partial consideration for it passed to the payor, this

debtor by way of subrogation to the case where the debt is discharged in law by the payment, despite being "voluntary", thereby conferring a benefit upon the debtor. The writers, in other words, have quite a different sense of how subrogation could be used in this case, and why. Both sets of writers, however, essentially see subrogation as a means of conferring rights and remedies where no right of reimbursement can be granted.

It is not easy to reconcile these differences. Nor is it easy to agree with the writers in all respects. First, it is difficult to see why, if the debt is discharged by the payment and a "benefit" is thereby conferred upon the debtor, subrogation but not also reimbursement should be available. Either the circumstances surrounding the payment give rise to an entitlement to restitutionary relief in favour of the payor against the debtor, or they do not. Since rights of reimbursement[86] are in essence as much restitutionary in nature as rights of subrogation, it follows, it is submitted, that either both reimbursement and subrogation should be available in the circumstances of the particular case, or neither should be. It is difficult to see how any other result can be justified when the party ultimately liable, whether by way of reimbursement or by way of subrogation, is the same. If, according to the established tests, the payor

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leaves the creditor with the option of both keeping the payment and also suing on the debt. If he does not, they suggest, the debtor is "incontrovertibly benefited" by the payor's payment, thereby justifying recovery from the debtor; GOFF & JONES, p. 530. This however means that restitutionary recovery is granted against the debtor to prevent him from being unjustly enriched by the retention of that "incontrovertible benefit"; not to prevent the creditor from being unjustly enriched as Goff and Jones suggest. If the creditor chose to sue for the debt, and the debtor was held liable to pay it, it could not be said that the debtor received any benefit from the payment such as might give rise to a restitutionary right of recovery in the payor.

86 But not necessarily rights of indemnity, supra, p. 43, note 24.

has acted "voluntarily" or "officiously" in conferring the benefit on the debtor, then that should generally lead to the denial of all restitutionary rights or remedies.[87]

Secondly, by raising the prospect of subrogation as a means of preventing the creditor's unjust enrichment, Goff and Jones appear to treat subrogation as a right against the creditor. As has been seen, this is true in some respects. For example, the surety's right to have securities given to the creditor to secure the guaranteed debt not dealt with to the surety's prejudice can be treated effectively as an independent right against the creditor. But this is not true of subrogation as a remedial device. In that context, subrogation operates against the person who has obtained a benefit at the expense of another, by enabling that other to exercise rights and remedies against that beneficiary so as to strip him of the enrichment he or she would otherwise unjustly retain. In the suretyship

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[87] Putnam makes this point in his text on suretyship, SURETYSHIP (1981), p. 85: "The difficulty which the author sees in this academic argument [that the surety obtains rights of subrogation though not reimbursement] is that it would be a strange result if equity were to deny one remedy, ie indemnity against the debtor, but allow another, ie subrogation. There is authority for the proposition that the rights of indemnity and subrogation are based on the same equity: Yonge v Reynell (1852) 9 Hare 809 at 818; Nicholas v Ridley [1904] 1 Ch. 192." Putnam suggests, however, op. cit., p. 85, that a "surety" such as Owen "could successfully have argued that, irrespective of his rights in equity, by statute [ie. Mercantile Law Amendment Act 1856, s. 5] he was entitled to use all the remedies which the creditor bank had against the debtor." This right, he further suggests, op. cit., p. 85, is not subject to the condition that the debtor have "accepted" the payment by the "surety" before it can give rise to rights against the debtor: "So long as the surety, being liable with another for any debt or duty, shall pay such debt, the surety is entitled to rights of subrogation. It would be difficult to argue seriously that, where S, the officious surety, pays a bank £100, such payment being in respect of a debt of £100 owed by D, the debtor, to the bank, the terms of the guarantee being in the standard form 'I hereby agree to pay the bank ... all sums which shall ... remain due to the bank', S's payment was not a payment of D's debt."

context, the beneficiary is the debtor. But if the debt has not been discharged at law, then no "benefit" has been conferred upon the debtor, and there is no basis for a restitutionary claim against the debtor through subrogation or otherwise. If the creditor has been "unjustly enriched at the expense" of the payor, restitutionary rights and remedies should perhaps be conferred upon the surety against the creditor, but these would presumably operate directly by way of reimbursement. Indeed, this is exactly what the quasi-contractual action by way of money had and received on the grounds of total failure of consideration purports to do. If, on the facts of the case, that action fails, then it may be that no restitutionary relief ought to be available.

Thirdly, and most importantly, as has already been emphasised, restitutionary theory requires, in addition to proof that a benefit has been conferred, proof that it would be "unjust" for the recipient of the benefit to retain that benefit at the expense of the payor.[88] In the suretyship context, this means that it is not enough for the payor merely to establish that his or her "voluntary" or "officious" payment was legally effective. It must also be shown that it would be "unjust" to allow the debtor to "retain" the benefit of the payment. If the payor fails to establish this, then, discharge or not, his or her claim for restitutionary rights of recovery against the debtor should fail. This will also be the case if the debtor has some defence recognised by the law to the claim for recovery.

Neither Goff and Jones, nor Birks and Beatson, expressly advert to this in their discussions of the interaction between "voluntariness",

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[88] See generally GOFF & JONES, pp. 29-51.

discharge, and subrogation. Instead, they seem to have assumed that if the payment was legally effective, that of itself means that the debtor would be "unjustly" enriched if permitted to retain the benefit of the payment. This assumption, it is submitted, may be unfounded. "Voluntariness", or "officiousness", it is submitted, raises two distinct questions. The first is that which has been already been outlined in detail, namely, whether payment discharged the debt at law. The answer to this question, it has been seen, is essentially a matter of determining whether any one or more of the factors which will negate "voluntariness" exists on the particular facts of the case at hand. If no such factor(s) exists, then the debt will not be considered discharged at law, no benefit is conferred upon the debtor, and there is no basis for the conferral of restitutionary rights or remedies upon the payor against the debtor.[89]

If, on the other hand, the debt is discharged because of the presence of some relevant factor negating voluntariness, it is still necessary, it is submitted, to ask whether it would be "unjust" in all the circumstances of the case for the debtor who has thereby been benefited to retain that benefit at the expense of the payor. This, it is submitted, is a distinct question. In answering it, it is further submitted, factors which were not relevant to the first question - "discharge or not?" - may play an important role. In particular, it is submitted, broad equitable factors which may not have been pertinent to payment may figure prominently in answering this second question. Thus, the fact that the debtor "assented" to the creditor's application of the payment to settle the debt may mean

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[89] It is a distinct question in this case whether the payor should be able to recover the payment from the creditor on the grounds of total failure of consideration.

that the payment will be considered "non-voluntary" for the purposes of the first question; but it may not hold equal sway in answering the second. It does not, in other words, follow from the fact that the payment was "non-voluntary" that it is also "unjust" for the debtor to retain the benefit of that payment. Other factors may intrude. This, it is submitted, is an explanation of the decision of the Court of Appeal in Owen v Tate which does not appear to have been clearly considered by the above writers. Yet this seems to be precisely what Scarman L.J. was saying when he decided that "the plaintiff has failed to made out a case that it would be just and reasonable in the circumstances to grant him a right to reimbursement."[90] Thus, even if Owen's payment had discharged the debt and thereby conferred a benefit upon the Tates, that did not necessarily mean it was "just and reasonable" to grant him a restitutionary right of reimbursement. This view of the decision in Owen v Tate, it is submitted, equally accords with and is supported by the analysis of the other two judges, particularly Ormrod L.J. who, it will be recalled, expressly adverted to these broader issues:

> "the transaction in this case is only a part of a much more complex series of transactions which have been going on between various people for some years. ... I find it quite impossible to sort out the rights and wrongs in this case ...".[91]

In other words, the undeniably "voluntary" or "officious" nature of Owen's payment, in the context of a long history of transactions between the parties, "outweighed" the fact of assent, and militated against the conferral of a restitutionary right of reimbursement. Owen failed to prove

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90 Owen v Tate [1976] 1 Q.B. 402, at 411. [Emphasis added]

91 Ibid., at 413-14.

that it would be "unjust" for the Tates to retain the benefit of the payment he had "forced" upon them.

"Voluntariness", it is submitted, thus operates as a "form of legal shorthand" at two levels. First, it may signify that there is nothing in the facts of the case to overcome the primary rule that one person cannot "voluntarily" pay the debt of another and effectively disharge it at law. But secondly, it may indicate that even where there is something in the circumstances of the case to render the payment effective at law in discharging the debt, nonetheless, the overall character of the payor's conduct may be such that retention of the enrichment would not be "unjust". Owen, it is submitted, failed at that second level of inquiry, not at the first.

(iv) Unjust retention

Suretyship, as has been seen, is premised upon the existence of primary and secondary liability. It is self evident that it would in general be "unjust" to allow the party who is primarily liable - the principal - to retain the benefit of the payment by the party only secondarily liable - the surety. In general, therefore, this element of the principle of unjust enrichment can be readily identified in a suretyship situation. Difficulties in doing so may nonetheless occur, as has just been seen in the discussion of Owen v Tate,[92] primarily centred around questions of voluntariness.

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92 [1976] Q.B. 402.

Two other factors may also be relevant in assessing the injustice of the principal retaining the benefit of the surety's payment at the surety's expense, and the appropriateness of subrogation as a remedy to effect restitution of that enrichment. The first is the fact that although the surety's right of subrogation is not generally considered contractual in nature, it may nonetheless be modified or waived by contract.[93] This may be the result either of an express provision in the contract of suretyship,[94] or of a term implied into the suretyship relationship.[95] Insofar as restitutionary claims and rights are always subject to and affected by any express agreement of the parties regarding their respective rights and remedies, this also reflects the restitutionary underpinings of the surety's rights of subrogation.

The second additional factor that may be relevant to the justice or injustice of the principal retaining the benefit of the surety's payment and to the appropriateness of subrogation to effect restitution of that benefit is rights on the part of the principal debtor against the creditor. The surety's entitlement to enforce the rights, remedies, and securities of the creditor against the principal debtor, or any co-sureties, is subject to any rights or remedies which the principal debtor, or co-surety, may have against the creditor, whether by way of set-off or otherwise, and

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[93] This is equally true of the surety's equitable rights of reimbursement and contribution. See, eg., Swain v Wall (1641) 1 Chan. R. 149, 21 E.R. 534.

[94] See eg., Re Fernandes, ex parte Hope (1844) 3 Mont. D. & De. G. 720; Earle v Oliver (1848) 2 Exch. 71, 154 E.R. 410; Midland Banking Corporation v Chambers (1869) L.R. 4 Ch. App. 398. See also Morris v Ford Motor Co. Ltd. [1973] Q.B. 792.

[95] See Allen v De Lisle (1857) 5 W.R. 158; Brandon v Brandon (1859) 3 De G. & J. 524, 44 E.R. 1371.

which could have been used by him or her in diminution of the creditor's claim. This limitation on the surety's subrogative rights follows naturally from the fact that the rights and remedies which the surety is entitled to enjoy through the operation of subrogation are neither direct rights of recovery against the debtor, nor original in nature. They are derived from the rights and remedies of the creditor, and operate indirectly against the debtor through the medium of the creditor. The surety "stands in the place (or shoes) of" the creditor and has to make do with them, even if they do not fit perfectly or are not exactly to his preferred design; he does not obtain a brand-new pair of custom-made shoes. They are as good as, but not better than, those of the creditor. Were the law otherwise, the surety would be able, by payment or performance, to deprive the debtor or co-surety of any legitimate claims he or she may otherwise have against the creditor. Such a result would be inequitable and unjust, and contrary to the essentially equitable nature of the surety's rights of subrogation.

C. Conclusion

This examination of the nature of the surety's right of subrogation reveals, it is submitted, a number of basic features which support the view that both the surety's right of subrogation in particular, and subrogation in general, are essentially restitutionary in nature and operation. The use of subrogation is based upon the conferral of a benefit on the principal debtor. The extent of recovery by the surety is limited to the amount of that benefit - the extent of the principal's enrichment, in other words. Recovery will be denied if the surety acted voluntarily or officiously,

either in becoming a surety, or simply in making payment. Recovery will also be denied if it would be unjust to require the principal debtor to make restitution of the enrichment because, for example, the principal debtor has rights against the creditor. Subrogation in the suretyship context is also closely linked to the surety's rights of reimbursement and contribution, which are equally said to be essentially restitutionary in nature. Certainly, it is submitted, there is little which could be pointed to as an overt challenge to the assertion that the surety's right of subrogation illustrates and highlights the essentially restitutionary nature of subrogation.

PART IV

SUBROGATION AND BILLS OF EXCHANGE

SUBROGATION AND BILLS OF EXCHANGE[1]

A. Introduction

A second class of case in which the use of subrogation has been recognised by the law is that of bills of exchange. The use of subrogation in this context has flowed in part from a recognition that the relationship of certain types of party to a bill of exchange - in particular, accommodation parties - can generally be categorised as one of suretyship. As such, the use of subrogation in favour of an accommodation party is generally regarded as simply a specific illustration of subrogation in the suretyship context, and not as a distinct category of subrogation.[2]

The same view is not, however, taken of the use of subrogation in favour of certain other parties to bills of exchange - in particular, indorsers and drawers for value. These parties are not generally considered to be sureties in the strict sense,[3] so that their rights, including that

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[1] See generally re England: Bills of Exchange Act 1882, 45 & 46 Vict., c. 61; M. Megrah & F.R. Ryder, BYLES ON BILLS OF EXCHANGE (25th ed., 1983)(hereafter "BYLES"). Re Canada, see Bills of Exchange Act, R.S.C. 1970, c. B-5; Crawford & Falconbridge, BANKING AND BILLS OF EXCHANGE (11th ed., 1986); Falconbridge, THE LAWS OF NEGOTIABLE INSTRUMENTS IN CANADA (1967).

[2] See eg. Sir R. Goff & G. Jones, THE LAW OF RESTITUTION (3rd ed., 1986) (hereafter "GOFF & JONES"), p. 417.

[3] See generally Duncan, Fox, & Co. v North & South Wales Bank (1880) 6 App. Cas. 1. See also Re Conley [1938] 2 All E.R. 127, at 131, where Sir Wilfrid Greene M.R. commented: "... in the case of a bill accepted for value, the relationship between drawer and indorsers, on the one hand, and the acceptor, on the other, is referred to as one of

of subrogation, cannot simply be seen as an illustration of the surety's right of subrogation. Such parties are, however, seen to be in an analogous position in certain respects to sureties in the strict sense, and entitled thereby to some at least of the rights of such sureties, including the right to securities which, as has been seen, lies at the heart of the surety's right of subrogation. This was clearly recognised by the House of Lords in Duncan, Fox, & Co. v North & South Wales Bank,[4] where it was considered that cases such as that of parties to bills of exchange could be treated as a third class of "suretyship" based not on agreement and notice, but simply on the existence of primary and secondary liability.[5]

Because of this difference, restitutionary writers commonly categorise subrogation in the context of bills of exchange, other than in relation to accommodation parties, as a distinct right to that possessed in the ordinary way by a surety in the normal, or "strict" sense.[6] Furthermore, this distinct right is seen to be clearly restitutionary in nature, based as it is generally accepted to be simply on notions of primary and secondary liability and the conferral of a benefit (payment or performance) by the party only secondarily liable upon the party primarily liable.[7]

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suretyship by Cockburn, C.J., and Lush and Quain, JJ., in Rouquette v Overmann [(1875) L.R. 10 Q.B. 525]. We have the authority of the House of Lords [in Duncan, Fox, & Co.] for saying that this relationship is not one of suretyship, although it is analogous thereto."

4 (1880) 6 App. Cas. 1.

5 See discussion supra, p. 39 et seq..

6 See eg. GOFF & JONES, p. 417; G.H.L. Fridman & J.G. McLeod, RESTITUTION (1982) (hereafter "FRIDMAN & McLEOD"), p. 401.

7 See discussion supra, p. 39 et seq..

If, however, the thesis of this paper holds true - that subrogation, both in the suretyship context and generally, is essentially restitutionary in nature, whether the origin of the "suretyship" is an agreement, or just the existence of primary and secondary liability between two of the parties to a tripartite relationship[8] - then the distinction drawn between the use of subrogation in favour of accommodation parties to bills of exchange, and in favour of other parties for value to bills of exchange,[9] should in large part prove to be illusory. Instead, the principles guiding the availability and use of subrogation in favour of each should to a large extent coincide. This distinction and the supposed difference it reflects in the nature of the parties respective rights of subrogation according to whether they are sureties in the normal sense or only "quasi-sureties", and the support or otherwise that it gives to the thesis of this paper, is the focus of this part of this paper.

B. Subrogation and Accommodation Parties to Bills of Exchange[10]

An "accommodation party" to a bill of exchange, according to the relevant bills of exchange legislation,[11] is:

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8 Ie., Lord Selborne L.C.'s third class of case, and the one that applies to parties other than accommodation parties to bills of exchange.

9 And, it should be added, other rights of the parties to a bill of exchange after payment, such as reimbursement and contribution.

10 See generally D. Partlett, "The Right of Subrogation in Accommodation Bills of Exchange", (1979) 53 Aust. L.J. 694.

11 See the Bills of Exchange Act 1882, 45 & 46 Vict., c. 61 (U.K.); Bills of Exchange Act, 1970 R.S.C., c. B-5 (Can.). The Canadian Bills of Exchange Act contains similar provisions generally to those of the English Act. For ease of discussion, only the provisions of the English Act will be

"... a person who has signed a bill as drawer, acceptor, or indorser, without receiving value therefor, and for the purpose of lending his name to some other person."[12]

By signing a bill, an accommodation party becomes liable on the bill to the holder for value, in the same way as do all other parties to the bill.[13] Since this increases the likelihood of the holder being paid on the bill, the value and negotiability of the bill in the hands of the "other person" - the party accommodated - is thus enhanced.[14]

The creation of liability to the holder for value arises upon signature by the accommodation party and is not affected by whether or not the holder knew, when he or she took the bill, that the person was an accommodation party.[15]

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specifically referred to.

[12] Bills of Exchange Act 1882, s. 28(1). The Act also refers to "accommodation bills"; see s. 59(3). "Accommodation bill" is not however specifically defined in the legislation. In a loose sense, any bill to which there is an accommodation party could be called an "accommodation bill", but this is not strictly speaking correct. An "accommodation bill" is more correctly a bill where the accommodation party is the acceptor; see Scott v Lifford (1808) 1 Camp. 246, 170 E.R. 945.

[13] Ibid., s. 28(2).

[14] One commentator gives the following example: "Suppose A being pressed for money, arranges with his wealthy friend B that A shall draw a 3 months bill on B and that B shall accept the bill. B, in accepting, becomes liable for payment in 3 months' time although A has given him no value. As the party primarily liable for payment is the wealthy B the bill is first-class security and A can raise money on it (ie. 'discount' it) immediately. A hopes that, in 3 months' time when B will be called on to pay, his financial stringency will have disappeared and that he will be able to provide B with funds to pay the bill. B has signed the bill as acceptor to oblige or accommodate A. Consequently B is an accommodation party"; D. Richardson, GUIDE TO NEGOTIABLE INSTRUMENTS AND THE BILLS OF EXCHANGE ACTS (7th ed., 1983), p. 80.

[15] Ibid., s. 28(2). The accommodation party's liability to the holder for value may however be subsequently discharged. One important circumstance where this may occur arises from the fact that an accommodation party is considered to be a surety vis-á-vis the party

The fact that a party to a bill only signed the bill in order to accommodate another party to it does, however, affect the rights and liabilities of the accommodation party vis-å-vis the party accommodated. In the first place, since the party accommodated has not given the accommodation party any value or consideration for signing the bill and thereby undertaking liability on it, the accommodation party is not liable to the party accommodated on the bill. This is so regardless of the particular capacity in which the accommodation party signed the bill.[16] The ordinary rules regarding the respective liability of the parties to a bill of exchange, in other words, insofar as they would make the accommodation party liable to the party accommodated, do not apply as between the accommodation party and the party accommodated.[17]

Where the real nature of the transaction, as proved, is that one party to a bill signed it to accommodate another party to it, then this means that the party who has been accommodated will be held liable to the accommodation party. This will be so even though the ordinary rules regarding liability on a bill would not lead to this result, or indeed, would actually dictate that the former was not liable to the latter. For example, according to the ordinary rules applying to bills of exchange as stated in Batson v King,[18] the acceptor is considered to be the party

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accommodated. This is discussed more fully below; infra, p. 126.

16 Ie., it does not matter whether the accommodation party signed the bill as drawer, acceptor, or indorser.

17 Batson v King (1859) 4 H. & N. 739, 157 E.R. 1032.

18 Idem.

primarily liable on the bill.[19] As a result, the acceptor must normally indemnify an indorser of the bill who has been compelled to pay the bill.[20] If, however, it is proved that the acceptor only accepted the bill in order to accommodate the indorser in question, the acceptor - an accommodation acceptor - will not be liable to the indorser - the party accommodated - in the event that the latter is compelled to pay the bill. The rights and liabilities of the accommodation party and the party accommodated inter se have thus been varied.

The explanation for this, as has already been outlined, is that the law views the relationship between the party accommodated and the accommodation party as one of suretyship. The party accommodated and the accommodation party are considered to be principal and surety respectively. Thus, in Jones v Broadhurst[21] it was said that:

> "... in the case of an accommodation bill,[22] ... the acceptor is a mere surety, as between him and the drawer, and entitled to recover against the drawer whatever he may be compelled to pay in discharge of his suretyship."[23]

Similarly, in the leading authority of Liquidators of Overend, Gurney, &

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19 This is the effect of the Bills of Exchange Act 1882, 45 & 46 Vict., c. 61, s. 54. And see eg. Jones v Broadhurst (1850) 9 C.B. 173, at 181, 137 E.R. 858, at 861: "The acceptor is primarily and absolutely liable to pay the bill, according to its tenor. The drawers are liable only upon the contingencies of the acceptor's or drawee's making default, and of the holder's performing certain conditions precedent ...".

20 See Bills of Exchange Act 1882, s. 57.

21 (1850) 9 C.B. 173, 137 E.R. 858.

22 "Accommodation bill" is here used to refer to a bill of exchange in respect of which the acceptor is the accommodation party; see supra, p. 124, note 12.

23 (1850) 9 C.B. 173, at 181, 137 E.R. 858, at 862.

Co. v Liquidators of Oriental Financial Corp.,[24] the House of Lords held that an accommodation acceptor was to be considered a surety only vis-á-vis the party accommodated. The Lord Chancellor, Lord Cairns, stated:[25]

> "The giving of these bills of exchange, the drawing of them, and the acceptance of them [by Oriental Financial Corporation], were for the benefit of McHenry and his principals. McHenry was bound to provide the funds for the payment of the bills as between himself and the acceptors; and the relationship of principal and surety plainly existed between the parties."

This relationship is generally considered to be suretyship in the strict sense. That is, the source of the suretyship is seen to be an agreement - a contract - by the parties to the suretyship, to constitute themselves principal and surety inter se. However, since the party to the bill entitled to enforce payment by the accommodation party - the holder- will not generally have been a party to the agreement or transaction giving rise to the suretyship, the accommodation party's rights, as surety, against the holder, rather than the party accommodated, will only arise if notice of the suretyship has been given to the holder. Thus, although it is essentially the product of agreement, the suretyship will generally fall within the second of Lord Selborne L.C.'s three classes of suretyship in Duncan, Fox & Co. v North & South Wales Bank.[26]

There is, however, a problem with this approach. According to Lord Selborne L.C.'s classification, the circumstance giving rise to suretyships

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[24] (1874) L.R. 7 H.L. 348.

[25] Ibid., at 354-55. See also the decision of the Court of Appeal in this case: Oriental Financial Corp. v Overend, Gurney, & Co. (1871) 7 Ch. App. 142.

[26] (1880) 6 App. Cas. 1, at 11. This was the case in Liquidators of Overend, Gurney, & Co. v Liquidators of Oriental Financial Corp. (1874) L.R. 7 H.L. 348.

of the second class will generally be a contract. But logically, this cannot be so in relation to accommodation parties. For, although there may be an agreement between the accommodation party and the party accommodated, by which the former agrees to sign the bill "to accommodate" the latter, there is by definition no value or consideration given to the former for adding his signature to the bill. In the absence of value or consideration,[27] the agreement under which the accommodation party signs and assumes liability on the bill cannot, therefore, be said to be contractual, at least not in the normal sense.

This problem can, perhaps, be overcome if the "contract" is said to be an "implied contract" in the quasi-contractual sense. That is, for the purpose of conferring rights and remedies upon the accommodation party at common law, a "fictional contract" could be implied between the parties. This fictional contract would be implied from the request of the party accommodated to the accommodation party to sign the bill for the benefit of the former, and the consideration would be the agreement on the part of the party accommodated to indemnify the accommodation party. The appropriate form of action at common law by which the accommodation party would enforce his rights arising under this implied contract - such as the right of indemnity or re-imbursement - would be by way of the indebitatus assumpsit count of money paid at request.

This view of the nature of the "contractual" relationship between accommodation parties can be seen in the case-law. For example, in Asprey v

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[27] "Value" has an extended meaning under the Bills of Exchange Act 1882, s.27.

Levy,[28] in 1847, the plaintiff accepted a bill of exchange for £25 for the accommodation of a person named Faucher, who owed £7 to the defendant. The intention of the plaintiff and Faucher was that Faucher would discount the bill with the defendant who would accept it in satisfaction of Faucher's debt to him. Any balance would be given to the plaintiff. The defendant indorsed the bill and, wrongfully it was alleged, kept the whole proceeds. The holder of the bill subsequently sued the plaintiff who duly paid the bill. The plaintiff then commenced assumpsit proceedings against the defendant, claiming that the payment he had been compelled to make to the holder had been "paid to the defendant's use". The court held that the plaintiff's remedy in the circumstances was not against the defendant, but against Faucher. Parke B. stated:[29]

> "If a man gives his acceptance to another for the accommodation of that other, and the bill is disposed of according to the original intention of the parties, and the acceptor afterwards pays it accordingly, he cannot call on the indorsers, but his remedy is on the original contract against the drawer. Here the plaintiff's remedy is against Faucher, for the breach of his contract to indemnify the plaintiff against the consequences of accepting the bill for his accommodation. ... The plaintiff's remedy is against Faucher, to whom he lent his acceptance on his implied contract of indemnity."

This notion of a fictional, implied contract based upon a request has, however, been discarded in modern legal thinking, and replaced according to restitutionary theory with restitutionary rights and remedies based upon the principle of unjust enrichment.

Thus, the premise from which the law regarding the rights and remedies of accommodation parties to bills of exchange is derived, namely that their relationship is based upon a contract (which dictates their rights inter

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[28] (1847) 16 M. & W. 851, 153 E.R. 1436.

[29] Ibid., at 859, at 1439-40. [Emphasis added]

se, though notice of it will be necessary before rights arise against the holder of the bill), can be said to be flawed. In truth, it is submitted, it is the circumstance that the party accommodated has requested the accommodation party to sign the bill for the former's benefit on the understanding that the former will meet the bill when due, and is in that sense the party primarily liable as between the two, that gives rise to the accommodation party's rights and remedies against the party accommodated when the accommodation party is compelled to pay the bill. For it would be unjust in these circumstances to allow the party accommodated to retain the benefit of the accommodation party's payment on his behalf. The accommodation party's rights and remedies, in other words, are, it is submitted, essentially restitutionary in nature.

Nonetheless, upon the view that the accommodation party stands in a relationship of suretyship in the strict sense, it would follow that the accommodation party's rights include not only rights after payment by him or her, but also additional rights, already outlined,[30] prior to payment against both the party accommodated and, after notice, the "creditor". In the context of bills of exchange, the "creditor" will be the party presently entitled to seek payment of the bill. In the normal case, this will be the holder for value. Thus, in Liquidators of Overend, Gurney, & Co. v Liquidators of Oriental Financial Corp.,[31] the House of Lords held that the accommodation party - the surety - was discharged from liability to the holder on the bill as a result of the conduct of the holder in

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30 Supra, p. 34 et seq..

31 (1874) L.R. 7 H.L. 348.

granting time to the party accommodated - the principal.[32] This, as has already been seen,[33] is one of the "rights" of a true surety prior to payment of the debt or performance of the obligation in respect of which he or she is surety. This right, as has also been seen,[34] would not be available to the accommodation party were the relationship not considered to be a suretyship in the first or second of Lord Selborne L.C.'s classes, but rather a suretyship in the third class.[35]

Equally, if the party accommodated and the accommodation party are principal and surety, then it should follow that payment of the bill by the party accommodated - the principal - will effectively discharge the accommodation party - the surety - from liability on the bill, in accordance with the normal suretyship rules.[36] This is expressly provided

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32 See also Pooley v Harradine (1857) 7 E. & B. 431, 119 E.R. 1307; Greenough v McClelland (1860) 2 E. & E. 429, 121 E.R. 162; Rouse v Bradford Banking Co. [1894] A.C. 586.

33 Supra, p. 57.

34 Idem.

35 Nor would it apply if the creditor had reserved his rights against the accommodation party in giving time to the party accommodated-the principal; see eg. Re Renton, ex p. Glendinning (1819) Buck. 517; Owen & Gutch v Homan (1853) 4 H.L. Cas. 997, 10 E.R. 752.

36 Supra, p. 33 et seq..

for by statute, at least in relation to "accommodation bills",[37] for the Act[38] stipulates that:

> "Where an accommodation bill is paid in due course by the party accommodated the bill is discharged."[39]

Payment of the bill by the accommodation party, on the other hand, should not discharge the party accommodated - the principal - from liability, at least to the surety. Instead, the accommodation party in this case should have all the usual rights of a surety after payment.

Thus, the accommodation party should have the normal right of indemnity or re-imbursement against the principal. It is clear law that this is so. The obligation to indemnify the surety was recognised, for example, in Jones v Broadhurst,[40] when it was said that the accommodation party, the acceptor in that case, was:

> "entitled to recover against the drawer [the party accommodated] whatever he may be compelled to pay in discharge of his suretyship."[41]

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[37] Ie., bills in respect of which the accommodation party is the acceptor. As one commentator has pointed out: "['Accommodation bill'] should be used only to describe a bill where the accommodation party is the acceptor. The reason for this can be found in section 59(3) which states that an accommodation bill is discharged on payment by the party accommodated. A moment's thought will show that this must be the case only where the acceptor is the accommodation party. If any other party, say an indorser, was the accommodation party, then, if the party accommodated paid the bill the latter, though unable to sue the accommodation party, could nevertheless sue the acceptor and the bill would not be discharged whilst the acceptor remains liable on it"; D. Richardson, op. cit., p. 81.

[38] Bills of Exchange Act 1882.

[39] Ibid., s. 59(3).

[40] (1850) 9 C.B. 173, 137 E.R. 858. See also Reynolds v Doyle (1840) 1 Man. & G. 753, 133 E.R. 536.

[41] Ibid., at 181, at 862. [Emphasis added] See also, generally: Duncan, Fox, & Co. v North & South Wales Bank (1880) 6 App. Cas. 1.

This may also be the effect of the relevant bills of exchange legislation.[42]

Secondly, the accommodation party should be entitled to seek contribution from any other party to the bill who is equally liable with the accommodation party; any other party to the bill who is, in other words, a co-surety. This also is clear law.[43]

Thirdly, the accomodation party should be entitled to be subrogated to the holder's rights and remedies against the party accommodated, including in particular the right to have the benefit of any securities given by the party accommodated to the holder. The decision of the House of Lords in Duncan, Fox, & Co.[44] is authority for this. There, the Lords, in concluding that a party falling within the third of Lord Selborne L.C.'s classes of

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[42] For example, if the accommodation party is an indorser, he is entitled upon payment of the bill to recover the amount paid, together with interest and expenses, from either the acceptor or the drawer or any prior indorser; see Bills of Exchange Act 1882, s. 57(1). Similarly, if the accommodation party is the drawer, he may recover the same sums from the acceptor; s. 57(1).

[43] See eg. Reynolds v Wheeler (1861) 10 C.B. (N.S.) 561, 142 E.R. 572. There Erle C.J. held, at 565, at 573: "The machinery adopted here was, the drawing of a bill by Cheeseman [party accommodated] upon Reynolds [accommodation acceptor], and the indorsement of it by Wheeler [accommodation indorser]. As between these three parties and the holders, the acceptor would be primarily liable, and, on his failure to pay, recourse would be had to the drawer and the indorser. But their relation to the holder has no bearing on their relation to one another. Reynolds and Wheeler each became a surety for the same debt or liability of their principal, Cheeseman. Reynolds, therefore, [who had been compelled to pay the bill] clearly had a right to call upon Wheeler for contribution." This right arose, according to Williams J., upon the principle of equity recognised by Lord Eldon in Craythorne v Swinburne (1807) 14 Ves. Jun. 160, 33 E.R. 402. See also BYLES, pp. 420-21. A right of contribution would not, however, arise if the two sureties inter se are not co-sureties, but rather principal and surety; see eg., Scholefield Goodman and Sons Ltd. v Zyngier [1986] A.C. 562 (P.C.), discussed infra, p. 154 et seq..

[44] (1880) 6 App. Cas. 1.

suretyship was entitled to some at least of the rights of a full surety, including the right to receive the benefit of securities in the hands of the creditor, clearly accepted that the same was true of sureties in the second of Lord Selborne L.C.'s class. Lord Selborne L.C. stated:[45]

> "It is, however, consistent ... that the person who, as between himself and another debtor, is in fact a surety (though the creditor is no party to that contract of suretyship), has, against that other debtor, the rights of a surety; and that the creditor, receiving notice of his claim to those rights, will not be at liberty to do anything to their prejudice, or to refuse (when all his own just claims are satisfied) to give effect to them. ... [T]he equity is direct in favour of the surety-debtor against the principal debtor; but it affects the creditor towards whom they are both principals only as a man who has notice of the obligations of one of his own debtors towards the other."

In support of this, Lord Selborne L.C. cited, inter alia, the decision of the House of Lords in Liquidators of Overend, Gurney, & Co. v Liquidators of Oriental Financial Corp.,[46] which serves as authority that an accommodation party on a bill of exchange is only a surety for the party accommodated.[47] Clearly, therefore, accommodation parties, as sureties, are entitled to be subrogated to the position of the holder paid off by the accommodation party, and take the benefit of all the rights and remedies of the holder, including any securities held by him in relation to the party accommodated, in order to enable the accommodation party to obtain re-imbursement from the party accommodated, the principal.

Further support for this can be found in several cases dealing with the rights of accommodation parties to promissory notes, which are

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45 Ibid., at 12.

46 (1874) L.R. 7 H.L. 348.

47 Supra, pp. 126-27.

essentially the same as those under bills of exchange.[48] Thus, in Pearl v Deacon[49] it was held that a party who had joined a promissory note as surety was entitled to have the value of certain securities held by the holder of the note brought into account in assessing the liability of the surety to the holder. Similarly, in Aga Ahmed Ispahany v Crisp,[50] Sir Richard Couch, in the Privy Council, in considering the rights of an accommodation endorser of a promissory note, stated:[51]

> "It ... [is] a rule of equity that if the endorser of a bill of exchange pays the holder of it he is entitled to the benefit of the securities given by the acceptor, which the holder has in his hands at the time of payment, and upon which he has no claim except for the bill itself - Duncan, Fox, & Co. v North & South Wales Bank. The same rule ... [is] applicable to the endorser of a promissory note."

What then is the basis of the right to subrogation possessed by an accommodation party to a bill of exchange? Clearly, it could be seen as simply a consequence of classifying the relationship between the accommodation party and the party accommodated as one of suretyship, and a contractual suretyship in particular. According to that classification, the surety has certain rights, including a right of subrogation, derived from the "contract" of suretyship.

The difficulties with the notion of "contract" in this context have

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48 The law relating to promissory notes is similar to that relating to bills of exchange. Both are dealt with in the relevant bills of exchange Acts. See generally, Bills of Exchange Act 1882 (U.K.); Bills of Exchange Act (Can.). The provisions of the Acts relating to bills of exchange, including those relating to accommodation parties, apply equally to promissory notes, though with the necessary modifications.

49 (1857) 1 De G. & J. 461, 44 E.R. 802.

50 (1891) 8 T.L.R. 132.

51 Ibid., at 132.

already been discussed.[52] Given the absence of value or consideration, there can be no actual contract of suretyship from which the accommodation party's rights can be derived. Nor is it easy to sustain the fiction of an implied contract based on request in the face of modern legal analysis, in order to give a contractual basis to the accommodation party's right of subrogation. But once the idea of a fictional implied contract as the basis of an accommodation party's rights and remedies against the party accommodated is discarded, then the immediate problem is to find some other basis for the conferral of these rights and remedies on the accommodation party.

The answer comes with the recognition that the relationship between the accommodation party and the party accommodated is classified as one of suretyship because the parties are not viewed by the law as equally liable inter se for payment or performance of the relevant obligation. Once this is recognised, it follows that if the party not equally liable, but only secondarily liable, in the circumstances is compelled to make payment, or otherwise perform the relevant obligation, he or she should be able to seek recompense from the party primarily liable. Furthermore, since bills of exchange are essentially tripartite in nature, the party only secondarily liable should be entitled to have the technique of subrogation used in his favour, ie. be enabled to exercise for his own benefit the rights and remedies of the third party paid off by him in order to enforce his or her right of recompense against the party primarily liable.

But this, it is submitted, is essentially an expression of the accommodation party's rights and remedies against the party accommodated,

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[52] Supra, pp. 127-30.

including the right of subrogation, in restitutionary terms. The party primarily liable would, in other words, be unjustly enriched - because of the very fact that he or she has undertaken to bear primary responsibility for payment or performance - at the expense of the party only secondarily liable were the former allowed to retain the benefit of the latter's "compulsory" payment on his or her behalf; in order to remedy this potential unjust enrichment, the latter should therefore have both a restitutionary right of reimbursement against the former, and also, since the situation is tripartite, the restitutionary right to stand in the place of the third party and exercise for his own benefit all the rights and remedies of the third party insofar as they would facilitate recovery of the enrichment from the party primarily liable.

This view of the accommodation party's right of subrogation - his entitlement in other words to have the technique of subrogation applied in his favour to prevent the party accommodated from unjustly enriching himself at the expense of the accommodation party - entirely supports, it is submitted, the thesis of this paper.

C. Subrogation and Indorsers and Drawers for Value of Bills of Exchange[53]

The rights and liabilities of persons who, for value, either draw bills of exchange or subsequently indorse them are largely dictated by

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[53] See generally re England: Bills of Exchange Act 1882, 45 & 46 Vict., c. 61; and BYLES. Re Canada, see Bills of Exchange Act, R.S.C. 1970, c. B-5; Crawford & Falconbridge, op. cit.; Falconbridge, op. cit..

statutory provisions.[54] In some respects, these rights and liabilities are essentially the same as those of accommodation drawers and indorsers. But there are also differences. The basic principles laid down in the legislation can be shortly stated.

A person "draws" a bill of exchange, and is thus the "drawer" of the bill, when he or she unconditionally addresses an order in writing to another person (the "drawee") requiring that other person to pay on demand or at a fixed or determinable future time a sum certain in money to or to the order of a specified person, or to bearer.[55] The signature of the drawer is necessary before the bill is validly drawn.[56] By drawing a bill, the drawer undertakes that it will be accepted by the person to whom it is addressed (ie. the drawee[57]), and that it will be paid on the due date.[58] If either of these undertakings is not honoured, then all parties to the bill other than the acceptor may have recourse to the drawer.[59] Since there is no acceptor if the first undertaking is not honoured, the effect of the statutory provisions is that the drawer will be the party ultimately liable for payment of the bill.[60] If, however, the first undertaking is honoured

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54 Bills of Exchange Act 1882, (U.K.) 45 & 46 Vict., c. 61; Bills of Exchange Act, (Can.) R.S.C. 1970, c. B-5.

55 Ibid., s. 3(1).

56 Idem. See also s. 23.

57 Where the order addressed to the drawee requires payment at some future date, the drawee must agree to pay the bill on the due date. This constitutes "acceptance" of the bill and the drawee is thereafter known as the "acceptor". And see s. 17.

58 Bills of Exchange Act 1882, s. 55(1).

59 Ibid., s. 55(1), s. 57.

60 Ibid., s. 43.

and the bill is duly accepted, then the effect of the legislation is that the acceptor becomes the party primarily liable on the bill.[61] If the bill is then dishonoured by the acceptor when the holder presents it for payment, and recourse is had to the drawer, the payment by the drawer will not discharge the bill.[62] The acceptor remains liable on the bill and the drawer who is "compelled to pay the bill"[63] can recover over against the acceptor.[64]

An "indorser" of a bill of exchange is a party to the bill who effects the negotiation or transfer of the bill by writing his or her name on the bill as transferor and then delivering the bill thus indorsed to the

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[61] Ibid., s. 54. This was also the position at common law. In Jones v Broadhurst (1850) 9 C.B. 173, at 181, 137 E.R. 858, at 861, for example, it was said: "The acceptor is primarily and absolutely liable to pay the bill, according to its tenor. The drawers are liable only upon the contingencies of the acceptor's or drawee's making default, and of the holder's performing certain conditions precedent ... ."

[62] Ibid., s. 59(2). Goff & Jones query whether this needs to be the rule; GOFF & JONES, pp. 317-18: "No doubt bills of exchange are subject to special considerations. Nevertheless, on general principle there is much to be said against the rule ... established [in Jones v Broadhurst (1850) 9 C.B. 173, 137 E.R. 858, and s. 59(2) Bills of Exchange Act 1882]. It is true that the indorser of a bill of exchange is not, strictly speaking, a surety; nor has he, strictly speaking, indorsed the bill at the request of the acceptor. Yet the primary liability rests upon the acceptor, that of the indorser being 'only secondary'; and it is certainly within the contemplation of acceptors of bills of exchange that others will indorse the bills and so render themselves liable thereon. It is difficult to see, therefore, why the payment of a drawer or indorser should not operate to discharge the acceptor, pro tanto, if the payment is partial, and completely, if the payment is in full. The indorser is not an officious intervener and he should be entitled to recover the amount of any such payment from the acceptor."

[63] Ibid., s. 57(2).

[64] Idem.

transferee.[65] The signature of the indorser is necessary before the indorsement operates as a valid negotiation of the bill.[66] There may be more than one indorser of a bill, according to the number of times the bill was negotiated by indorsement. Indorsers rank according to the stage at which they indorsed the bill. The rights and liabilities of an indorser are similar to those of a drawer. Thus, the indorser also undertakes that on due presentation the bill will be accepted and paid;[67] if it is not, then like the drawer, the indorser will be liable to all subsequent parties.[68] An indorser will not, however, be liable to prior indorsers or the drawer. Instead, if recourse is had by the holder or a subsequent indorser to the indorser, the indorser who is as a result "compelled to pay the bill",[69] may in his or her turn have recourse to those prior indorsers or the drawer. In this regard, the rights and liabilities of an indorser differ slightly from those of the drawer. But payment by an indorser no more discharges the bill than does payment by the drawer;[70] in the event of payment, therefore, the indorser, like the drawer, may also have recourse to the acceptor[71] who remains ultimately, or primarily, liable.[72]

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65 Ibid., s. 2. See also Halsbury, LAWS OF ENGLAND (4th ed., 1973), vol. 4 "Bills of Exchange and Other Negotiable Instruments", para. 308.

66 Ibid., s. 32. See also s. 23.

67 Ibid., s. 55(2).

68 Idem. See also s. 57.

69 Ibid., s. 57(2).

70 Ibid., s. 59(2).

71 Ibid., ss. 57, 59(2).

72 Ibid., s. 54.

Two facts relevant to subrogation are noticeable from this brief account of the rights and liabilities of drawers and indorsers for value of bills of exchange. The first is that the situations outlined are tripartite - they involve at least three parties, namely the drawer or indorser, the holder, and the acceptor.[73] The second is that the recourse rights of the drawer and indorser against the acceptor and, in the case of an indorser, against prior indorsers and the drawer also, arise when the drawer or indorser is "compelled to pay the bill".[74] These two facts might be thought to indicate that the recourse rights of a drawer or indorser for value are derived from and through the holder who compelled the payment; in other words, that they are essentially the result of subrogation, of standing the drawer or indorser in the place of the holder so as to enable the drawer or indorser to have the benefit of the holder's rights and remedies against other parties to the bill, and, in particular, the acceptor. But this is not so. The recourse rights of the drawer and indorser are not derived from and through the holder; rather, they emanate from the fact that upon payment, the drawer or indorser <u>becomes</u> the "holder" of the bill. This was the effect of payment at common law,[75] and is specifically provided for in the relevant bills of exchange legislation.[76] Thus, s. 59(2)(b) of the Bills of Exchange Act 1882 (U.K.) provides:

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[73] It is necessarily the case that there will be three parties. One person may, however, bear more than one status on a bill of exchange.

[74] <u>Ibid.</u>, s. 57(2).

[75] <u>Ex p. Bishop, re Fox, Walker & Co.</u> (1880) 15 Ch. D. 400. At 411, James L.J. stated that "an indorser of a bill is not entitled to sue upon it, unless he becomes the holder."

[76] Bills of Exchange Act 1882, s. 59.

> "Where a bill is paid by an indorser, or where a bill payable to drawer's order is paid by the drawer, the party paying it is remitted to his former rights as regards the acceptor or antecedent parties, and he may, if he thinks fit, strike out his own [and] subsequent indorsements, and again negotiate the bill."[77]

The recourse rights of the drawer and indorser are therefore largely a result of the fact that, by statute, he or she, upon payment of the bill, becomes the holder of the bill and able to sue upon and enforce it in the normal way.

There are, however, several circumstances which are not clearly catered for by the statutory provisions, and where resort must be had to the common law, and possibly to subrogation, to determine the recourse rights of the drawer and indorser against the acceptor, or, in the case of an indorser, the drawer and any prior indorsers. First, it is clear that a drawer or indorser is remitted to his former rights only in the event of full payment of the bill by him.[78] Partial payment will not be sufficient. The party to whom the partial payment is made remains the holder of the bill, and may still seek full payment of the bill from the acceptor. If, in this case, the holder does subsequently receive full payment from the acceptor, does the drawer or indorser have any right to recover his partial payment? Authority suggests that this is possible, although the basis for recovery is not clear. In Pownal v Ferrand,[79] in 1827, the court held that an indorser who had paid the holder in part, could proceed directly against the acceptor in an action for money paid, on the basis that the acceptor

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77 Emphasis added.

78 The statute reads "is paid".

79 (1827) 6 B.& C. 439, 108 E.R. 513.

had received the benefit of the indorser's partial payment.[80] Goff and Jones suggest, however, that this case "must now be regarded as of doubtful authority",[81] because:

> "It is difficult to see how this case can be reconciled with Jones v Broadhurst,[82] [which of course held that the indorser's payment did not discharge the acceptor in whole or in part; ie. no "benefit" was conferred on the acceptor] or, indeed, with s. 59(2) of the Bills of Exchange Act 1882, except on the rather doubtful ground that the acceptor should be taken to have ratified the indorser's payment."[83]

An alternative explanation for recovery by the drawer or indorser, and one advanced in Jones v Broadhurst,[84] is to treat the partly paid holder, who has subsequently received full payment from the acceptor, as a trustee for the drawer or indorser of an amount equal to the partial payment previously made by the drawer or indorser.[85] In this way, the drawer or

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[80] Ibid., at 443-46, at 514-15. Each of the four judges in this case expressed themselves along lines similar to Lord Tenterden C.J., at 443, at 514: "I am of opinion that ... [the plaintiff, an indorser of the bill] is entitled to recover upon this general principle, that one man, who is compelled to pay money which another is bound by law to pay, is entitled to be reimbursed by the latter; and I think, that money paid under such circumstances may be considered as money paid to the use of the person who is so bound to pay it."

[81] GOFF & JONES, p. 536.

[82] (1850) 9 C.B. 173, 137 E.R. 858.

[83] GOFF & JONES, pp. 318-19.

[84] (1850) 9 C.B. 173, 137 E.R. 858.

[85] Cresswell J., in considering earlier authorities on the rights of an indorser who has partly paid the holder, suggested, at 185, at 863: "It may be that what was intended to be said was, that such a payment by the acceptor would make the indorsee [ie. the holder] a trustee for the drawer, and liable to refund to him what should be paid by the acceptor: ...". Goff & Jones see this as a better explanation for recovery of the partial payment, GOFF & JONES, p. 536: "The best course for an indorser who has paid a bill in part is to persuade the holder to recover the full amount of the bill from the acceptor. The holder will then hold on trust for the indorser an amount equal to the sum which the latter has paid on the bill."

indorser can recover whatever was previously paid by him to the holder. The difficulty with this explanation lies in identifying the factor giving rise to the trust in favour of the drawer or indorser. The court in Jones v Broadhurst itself expressed doubt about this explanation of a right of recovery, for the earlier authorities suggested it was the acceptor, not the holder, who was liable to refund the drawer.[86]

It is submitted that a further explanation for recovery by the drawer or indorser is possible. If, as the cases and statutory provisions state, the drawer or indorser's partial payment to the holder does not discharge the bill, and the holder can still seek full payment from the acceptor, it is arguable that the consideration given by the holder in return for which the partial payment was made, namely, discharge of the bill at least in part or non-recovery at least in part from the acceptor, has wholly failed. If so, then it can be argued that the holder has no legal entitlement to retain the money previously paid to him by the drawer or indorser; quasi-contractual, or restitutionary, proceedings based on this total failure of consideration could accordingly be taken to recover the same from him.[87] Recovery, in other words, would not be on the basis that the partial payment is legally effective to discharge the acceptor's liability in part, but on the opposite basis, that it is not legally effective. In this way,

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[86] Ibid., at 185, at 863, per Cresswell J.: "... but it is by no means clear that this [idea of a trust] was intended to be said, because the remarks [in an earlier case] refer to the acceptor's liablity to refund, in terms, and speak of a payment by the acceptor, after notice of payment by the drawer, - which would be quite immaterial, upon the question whether the indorsee would become a trustee for the drawer, in regard to the sum received from the acceptor." [Emphasis added]

[87] The indebitatus assumpsit count of money had and received was used where a total failure of consideration was alleged; see generally GOFF & JONES, p. 3, pp. 54-55.

it is submitted, the money could be recovered without doing any violence to the basic principles of liability laid down in Jones v Broadhurst[88] or s. 59(2) of the Bills of Exchange Act 1882.

A second situation which is not clearly catered for in the legislation, and where subrogation has its principal role in relation to drawers and indorsers for value, concerns securities deposited by the acceptor or, in the case of an indorser, by the drawer or prior indorsers, with the holder of the bill of exchange. The question that arises is whether a drawer or indorser who has paid the holder in full, and thereby been "remitted to his former rights as regards the acceptor or antecedent parties",[89] can claim the benefit of these securities in seeking recourse from the acceptor or antecedent party? A positive answer will, of course, be particularly important if, as is usually the case when securities are concerned, the party who deposited the securities has subsequently become bankrupt or insolvent. In that event, the drawer or indorser will wish to claim the benefit of the securities in order to obtain priority over general unsecured creditors.

The fact that the drawer or indorser becomes the holder and is remitted to his former rights when he or she pays the bill will not assist him or her in claiming these securities, for it is "his former rights" to which he is remitted, not those of the holder to whom payment was made. The drawer can only claim the benefit of the securities given by the acceptor or other antecedent party to the former holder of the bill if the drawer or indorser can compel the former holder to assign the securities to him or

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88 (1850) 9 C.B. 173, 137 E.R. 858.

89 Bills of Exchange Act 1882, s. 59(2)(b).

her, or can otherwise take the benefit of them through the former holder. Can a drawer or indorser do so? Clearly, he or she could if the relationship between them and the party depositing the securities can be classed as one of suretyship, for the drawer or indorser, as surety, would thereby be entitled to subrogation. As has been seen,[90] subrogation in the suretyship context entails and is typified by the assignment of securities held by the creditor to the surety; or alternatively, the entitlement of the surety to be stood in the place of the creditor to whom the securities were given in order to receive the benefit of them. The question, therefore, can be expressed as the question whether a drawer or indorser has a right of subrogation.

In answering this question this paper comes full circle, for the leading case on the right of drawers or indorsers of a bill of exchange to the benefit of securities deposited by the acceptor of the bill with the holder is Duncan, Fox, & Co. v North & South Wales Bank.[91] In that case, it will be recalled, the House of Lords extended the notion of suretyship to include certain analogous relationships, in order to endow the parties to those relationships with some at least of the rights and remedies of sureties in the normal sense, including the right of subrogation.[92] The particular relationship and problem under consideration in that case was exactly the problem here outlined, namely, the right of a indorser for value of a bill of exchange to the benefit of securities deposited by the

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90 Supra, p. 56.

91 (1880) 6 App. Cas. 1.

92 Supra, p. 35 et seq..

acceptor of the bill with the holder to whom the indorser is required to make payment.

The problem arose because the bills in that case, indorsed by Duncan, Fox, & Co., and discounted to North & South Wales Bank, were dishonoured upon presentation to the acceptor, Radford & Sons, for payment.[93] The holder of the bills, North & South Wales Bank, gave formal notice of dishonour to Duncan, Fox, & Co. and demanded payment of the bills. The acceptor in the meantime had become insolvent and had executed a deed of inspectorship.[94] Duncan, Fox, & Co. admitted their liability on the bills but, having learned that the acceptor had deposited certain deeds of freehold property with the bank as security for the acceptor's liability to the bank, claimed that they were entitled, in calculating the amount due by them on the bills, to the benefit of these securities, on the ground that Duncan, Fox, & Co. was merely a surety for the acceptor. Prior to payment of the bills, Duncan, Fox, & Co. thus applied to the bank to realize the securities and apply the proceeds in payment of the amounts due on the bills, or to render to Duncan, Fox, & Co. an account of what was due from the acceptor and, on payment, transfer the securities for the same amount remaining in the bank's hands. The acceptor's other unsecured general creditors contested this claim and instead claimed that the securities should be paid over to the inspectors for general distribution. The North &

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[93] Two sets of bills were actually involved in the case, with slightly different parties. The discussion here outlines the facts as they relate to the bills indorsed by Duncan, Fox, & Co. The decision and principles outlined applied equally to the other set of bills.

[94] A deed of inspectorship was an instrument entered into between an insolvent debtor and his creditors, appointing a person or persons to inspect and oversee the winding up of such insolvent affairs on behalf of the creditors; see Bankruptcy Act 1869, ss. 125, 127.

South Wales Bank thereupon sought the direction of the court as to what should be done with the securities.

The House of Lords rejected Duncan, Fox, & Co.'s claim that it was a surety in the normal sense - ie., a surety within either the first or second of Lord Selborne L.C.'s three categories[95] - for the acceptor or antecedent parties on the bill.[96] To fall within these two classes of suretyship, the Lords recognised, the drawer or indorser of a bill must have agreed - or contracted - with the acceptor, or antecedent parties, that the former will only be a surety vis-á-vis the latter for payment of the bill. This, the Lords accepted, was not normally so in bills of exchange.[97] Thus, indorsing a bill for value did not per se constitute the indorser a surety for the acceptor with all the attendant rights of a surety, including the right to have the benefit of any securities lodged by the acceptor with the holder of the bill.

However, as has already been seen,[98] the law does not view all the parties to a bill of exchange as being equally liable inter se for payment of the bill, though this may be so as far as the holder is concerned. The chain of recourse rights stops at someone. A hierarchy of liability thus exists, according to which one party to the bill may be said to be only secondarily liable on the bill in relation to another party, with that latter party consequently bearing primary liability for payment. The

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95 Supra, pp. 36-37.

96 Ibid., at 13-14, per Lord Selborne L.C.

97 Of course, the parties to a particular bill of exchange may have reached such an agreement.

98 Supra, p. 140.

immediate legal consequence of classifying the relationship between two parties to the bill as one of primary and secondary liablity is that if the party only secondarily liable is compelled to pay the bill, then, according to the common law, he or she should be able to recover the amount of that payment from the party primarily liable. This was recognised by the Lords in Duncan, Fox, & Co. in referring to cases:[99]

> "in which there is, strictly speaking, no contract of suretyship, but in which there is a primary and secondary liability of two persons for one and the same debt, by virtue of which, if it is paid by the person who is not primarily liable, he has a right to re-imbursement or indemnity from the other ...".

Such cases, stated Lord Selborne L.C.,[100] formed a third class of suretyship for the pupose of assessing the rights and liabilities of the parties to them.

It has already been seen[101] that the law views the acceptor of a bill of exchange as the party who is ultimately liable on the bill. Thus, a drawer of the bill can be said to be only secondarily liable for payment of the bill vis-á-vis the acceptor; and an indorser can be said to be secondarily liable for payment vis-á-vis not only the acceptor, but also the drawer and prior indorsers. In each of these cases, therefore, if the drawer or indorser is compelled by the holder to pay the bill, he or she will have at least a right of re-imbursement against the acceptor. To this extent, the drawer or indorser upon payment possesses rights analogous to those of a surety in the normal sense.

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[99] (1880) 6 App. Cas. 1, at 13, per Lord Selborne L.C.

[100] Ibid., at 11.

[101] Supra, pp. 125-26.

By the same reasoning, concluded the House of Lords, a drawer or indorser who has been compelled to pay the bill should be entitled to the benefit of any securities lodged by the acceptor with the holder to secure the acceptor's liability to the holder. Lord Selborne L.C. concluded:[102]

> "I am unable to conceive any ground on which the principle [of equity upon which a surety is discharged if the creditor discharges or suspends his rights against the principal without the consent of the surety] which prevails in cases of suretyship should go so far as this, in favour of the drawer or indorser, and not also extend (when the indorser is compelled to pay the bill, and when the question arises between him and the acceptor only) to securities deposited by the acceptor with the holder. ... No case before the present has been cited, in which the right of a drawer or indorser to the benefit of such securities, as between himself and the acceptor, has ever been denied or doubted. ... I think that the principles deducible from all the authorities lead, necessarily, to the conclusion, that, under circumstances like the present, the equity between the indorser and the acceptor is the same as that between a surety and a principal debtor when the creditor is not a party to the contract of suretyship [ie. Lord Selborne L.C.'s second class of suretyship]."

Thus, an indorser for value of a bill of exchange, or, it would seem, a drawer for value, who has been compelled to pay the holder of the bill is entitled, in addition to his or her recourse rights under the bills of exchange legislation by virtue of his or her becoming the holder, also to have the benefit of any securities deposited by the acceptor (or other antecedent parties) with the former holder in respect of the acceptor's (or other's) liability on the bill. This latter entitlement, it is submitted, is the result of subrogating the indorser or drawer to the position of the paid off holder.

What is the nature of this entitlement to subrogation? Clearly, it is not contractual in nature. This was accepted in Duncan, Fox, & Co. v North

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102. (1880) 6 App. Cas. 1, at 14-15.

& South Wales Bank.[103] Instead, according to Lord Selborne L.C., as just seen, it is broadly based upon notions of "equity". Lord Blackburn agreed, but saw the source of this equity in cases such as Deering v Earl of Winchelsea,[104] and Craythorne v Swinburne.[105] In his view, these cases established that:

> "[W]here a creditor has a right to come upon more than one person or fund for the payment of a debt, there is an equity between the persons interested in the different funds that each shall bear no more than its due proportion. This is quite independent of any contract between the parties thus liable. ... I think that though the indorser of a bill is not exactly a surety for the acceptor, or a co-surety with those who are sureties for the acceptor, yet he stands in a position sufficiently analogous to that of a surety to bring him within the principle of Deering v Lord Winchelsea."[106]

Lord Watson also saw the indorser's right of subrogation to be a product of "equity":

> "[I]t has long been a settled rule of Equity that, in circumstances analogous to those of the present case, the creditor is bound to take payment from that one of his debtors who is inter eos primarily liable for his debt."[107]

This notion of "equity", it has already been submitted,[108] in essence arises from the interplay of two factors in the circumstances of this case: first, the fact that there is something in the circumstances of the case, other than a contract, which legally compels the "quasi-surety" to pay the debt of another; and secondly, the fact that there is something in the

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103 (1880) 6 App. Cas. 1.

104 (1787) 2 Bos. & P. 270, 126 E.R. 1276.

105 (1807) 14 Ves. Jun. 160, 33 E.R. 482.

106 Duncan, Fox, & Co. v North & South Wales Bank (1880) 6 App. Cas. 1, at 19.

107 Ibid., at 22.

108 Supra, pp. 39-40.

circumstances - perhaps the same thing, but again something other than a contract - which dictates that as between the two of them, the one who failed to pay the debt was the one who bore the primary liability for it, while the other who was compelled to pay bore only secondary responsibility. The "equity" that then arises is in essence, it is submitted, an expression of the injustice that would be seen to result were the party who bore primary responsibilty in the circumstances permitted to retain the benefit of the payment made under compulsion by the party only secondarily liable.

The notion of "equity" used in this case, in other words, is an encapsulation of the principle of unjust enrichment, and the basis, therefore, for effecting restitution of the benefit conferred on the acceptor. Subrogating the indorser to the position of the holder of the bill to enable him or her to receive the benefit of securities lodged by the acceptor with the holder for the common debt on the bill is, therefore, it is submitted, an expression of this need to effect restitution in the circumstances of the case. It is the fact that the acceptor (the party primarily liable on the bill) would be unjustly enriched, at the expense of the indorser (the party only secondarily liable as against the acceptor) if the former were allowed to retain the benefit of the latter's payment under compulsion to the holder, that leads to the use of the technique of subrogation to effect restitution.

The restitutionary nature of subrogation in this context is emphasised by the fact that this right of the indorser to stand in the place of the holder and receive the benefit of securities in the hands of the latter does not arise until the indorser has been compelled by the holder to pay

the bill. The "equity", the "unjust" enrichment in other words, does not arise until a benefit, an enrichment, has been conferred on the acceptor. This was recognised by the Lords in Duncan, Fox, & Co..[109] Lord Selborne L.C., for example, stated that the equity arose "... when the indorser is compelled to pay the bill ...".[110] Lord Blackburn also recognised the necessity for payment before the equity in favour of the indorser arose:[111]

> "[T]here is neither principle nor authority for saying that the indorsers are, during the currency of the bill, sureties, or in the nature of sureties to the indorsee, or that they have any equity to prevent the indorsee from dealing as it may seem to him most desirable, with any other parties ... . But though the indorsers had no such right by contract, yet after the bills were dishonoured and notice of dishonour had been given to the indorsers, the position of the parties is altered. Though the indorser is primarily liable as principal on the bill, and is not strictly a surety for the acceptor, he has this in common with a surety for the acceptor, that he is entitled to the benefit of all payments made by the acceptor, and is entitled, on paying the holder, to be put in a situation to have the right to sue the acceptor."

Lord Watson emphasised another feature of the indorser's right of subrogation that can be seen to be an indication of the restitutionary nature of the right, namely, that retention of the benefit conferred on the party primarily liable by the party only secondarily liable, must be unjust. This is not necessarily so, and other factors may need to be taken into account in a particular case. He stated:[112]

> "[W]hilst ... the indorser is not in the likeness, and therefore cannot claim the equities of a surety, so long as the bill is current, I am not prepared to hold that he becomes necessarily, and in all circumstances, entitled to these equities whenever the bill matures. It is possible that, after maturity, the holder of the bill may have

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109 (1880) 6 App. Cas. 1.

110 Ibid., at 14.

111 Ibid., at 18. [Emphasis added]

112 Ibid., at 22-23.

such interest, arising from his relations with the acceptor, as will entitle him even then to deal with his securities without respect to the interests of the indorser."

This passage also re-emphasises the distinction between contractual and restitutionary rights of subrogation, as regards the range of rights available to the indorser - ie. party paying off the bill - prior to payment by the indorser. In the latter case, as has been seen,[113] the range is much wider, and clearly includes protective rights against conduct by the creditor which might have the effect of depriving the latter of his entitlement to have the use of the holder's rights and remedies against the acceptor, including securities.

It would follow, of course, that a right of subrogation should not be held to exist in favour of a drawer or indorser in the absence of the "equity", or "unjust enrichment", that, it has been submitted, underpins the right of subrogation. That this is indeed so was usefully illustrated in a recent decision of the Privy Council on appeal from the Supreme Court of Victoria, namely Scholefield Goodman and Sons Ltd. v Zyngier.[114] In that case, the appellant, Scholefield Goodman and Sons Ltd. ("Scholefield"), had, during 1976, drawn five bills of exchange on a company, Zinaldi & Co. Pty. Ltd. ("Zinaldi"), payable to the Commercial Bank of Australia Ltd. (subsequently renamed Westpac Banking Corporation) ("the bank"). Each bill had been accepted by Zinaldi, and then delivered to and discounted by the bank, which accordingly became the holder of the bills. The discounted value of the bills was paid to Zinaldi. All five bills were dishonoured by Zinaldi upon presentation in early 1977. The bank thereupon presented the

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113 Supra, p. 37.

114 [1986] A.C. 562.

bills to Scholefield as drawer, and was duly paid by the latter, which thus became the holder of the bills. Scholefield could, therefore, as holder of the bills of exchange, and also because, as has already been seen,[115] the relationship between acceptor and drawer is essentially one of principal and surety, have demanded reimbursement from Zinaldi. It seems, however, that Zinaldi was not in a financial position to reimburse Scholefield.

Instead, Scholefield subsequently claimed contribution from the respondent, Mrs Zyngier, who was alleged by Scholefield to be equally liable with it as surety for payment of the dishonoured bills of exchange. Scholefield's claim against Mrs Zyngier was based upon a mortgage given by her to the bank in early 1976 over property owned by her, in which she had guaranteed both Zinaldi's and her own indebtedness to the bank. In particular, she had guaranteed Zinaldi's indebtedness by way of overdraft, and its indebtedness "for or in respect of any bills of exchange ... to which ... Zinaldi is or may hereafter be a party and on which ... Zinaldi is or may hereafter be liable (solely or jointly with any other person) either primarily or only in the event of any other failing to duly pay the same which are or may hereafter be discounted or paid or which may for the time being be held by the bank ...".[116]

Scholefield's claim against Mrs Zyngier was not brought to her notice until 1978, when the bank called on Mrs Zyngier, pursuant to the terms of the mortgage, to discharge Zinaldi's outstanding indebtedness on its overdraft to the bank. When she duly did so, and then asked the bank to discharge the mortgage, she was only then informed of Scholefield's claim

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115 Supra, pp. 125-26.

116 Ibid., at 568.

against her for contribution in respect of its payment of the sum due on the five bills of exchange. Furthermore, Scholefield by then claimed that it was also entitled by virtue of section 72 of the Victoria Supreme Court Act 1958[117] to be subrogated to the rights of the bank as mortgagee in order to secure payment of the contribution claimed by it.

Scholefield advanced these claims with the assertion that the bank could have sought payment of Zinaldi's indebtedness on the bills of exchange either from Mrs Zyngier pursuant to the terms of the mortgage, or from Scholefield as a party to the bills of exchange, and that "it would be inequitable to allow the choice of the creditor to determine the matter [and throw the whole of the liability upon Scholefield]."[118] Mrs Zyngier and Scholefield, in other words, were both alleged to be sureties of Zinaldi's indebtedness on the bills of exchange - Mrs Zyngier according to the terms of the mortgage, and Scholefield according to the statutory rules regulating the rights of the respective parties to bills of exchange - and equally liable therefore to the bank. "The doctrine of contribution", it was argued,[119] "is designed to equitably apportion the loss in such a situation." The alleged right to subrogation was in turn said to flow from the existence of a right to contribution - from the same equitable considerations in other words that underpined the alleged right to contribution.

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117 This is the Victorian equivalent of section 5 of the Mercantile Law Amendment Act 1856, discussed supra, p. 71 et seq..

118 Ibid., at 569.

119 Idem.

Mrs Zyngier denied these claims and sought a declaration that Scholefield was not entitled to contribution from her, and an order that the bank discharge the mortgage. Her argument rested in essence on the fact that she was not a party to the relevant bills of exchange. Because of this, she argued, her liability in respect of the bills of exchange arose only from the mortgage and was therefore different in nature to that of Scholefield as a party to the bills of exchange. The two liabilities, she argued, "were not such co-ordinate liabilities as would attract the principles of contribution. ... [T]he liabilities ... were not of equal status, and ... [Mrs Zyngier and Scholefield] were not co-sureties for the purpose of the doctrine of contribution."[120] She was, she said, "a surety in a different degree of suretyship from the suretyship of the drawer Scholefield";[121] "... not a co-surety but a surety for a surety."[122]

The trial judge, the Supreme Court of Victoria, and ultimately the Privy Council all held in Mrs Zyngier's favour. Scholefield was not entitled to contribution from Mrs Zyngier in respect of Zinaldi's liability on the five bills of exchange. Nor was it entitled to be subrogated to the rights of the bank as mortgagee. In reaching this conclusion, the Privy Council accepted and affirmed that contribution was essentially an equitable right. Lord Brightman, delivering the judgment of the Privy Council, stated:[123]

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120 Ibid., at 570.

121 Idem.

122 Idem.

123 Ibid., at 571.

> "The right of one of two or more sureties to contribution from a co-surety is founded upon equitable principles, and exists independently of whether the sureties are bound by the same or different instruments, and whether one surety became bound with or without the knowledge of his co-sureties.
>
> 'The principle of equity operates...upon the maxim, that equality is equity: the creditor, who can call upon all, shall not be at liberty to fix one with payment of the whole debt; and upon the principle, requiring him to do justice, if he will not, the court will do it for him.' Per Lord Eldon L.C. in Craythorne v Swinburne (1807) 14 Ves. Jun. 160, 165."

Similarly, the drawer or indorser's right of subrogation, though put forward in terms of the relevant statutory provision, was also seen to rest upon equitable considerations - the same ones that underpined the right to contribution:

> "Scholefield sought to argue in the alternative that section 72 of the Supreme Court Act 1958 ... gave it a right of recourse against the security held by the bank. It is however clear from the wording of the section, and implicit in the proviso thereto, that it does not confer on a person claiming to be a surety, a right of subrogation exercisable against another who is under no equitable obligation to make contribution."[124]

After considering several leading cases on contribution and subrogation in the context of bills of exchange, including Craythorne v Swinburne[125] and, importantly, Duncan, Fox, & Co. v North & South Wales Bank,[126] the Privy Council concluded that the fundamental question in the appeal was simply one of construction:

> "[W]hether upon the true construction of the bargain between the bank and Mrs Zyngier, Mrs Zyngier placed herself, as regards bills of exchange accepted by Zinaldi and thereafter dishonoured, in the position of a co-surety alongside the drawer or indorser; or whether, upon the true construction of the bargain, her liability to the bank upon a bill was intended to be limited to a case of default by the parties liable upon the bill. If it were the true meaning of the

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[124] Ibid., at 575. [Emphasis added]

[125] (1807) 14 Ves. Jun. 160, 33 E.R. 482.

[126] (1880) 6 App. Cas. 1.

> mortgage that the bank was required to call upon the parties to the bill before it called upon Mrs Zyngier to make good a default, then ex hypothesi no injustice ensued to the drawer upon the bank's adoption of that course and no case for the intervention of a court of equity could arise."[127]

After considering the nature of Mrs Zyngier's contract with the bank, and distinguishing both Craythorne v Swinburne[128] and Duncan, Fox, & Co. v North & South Wales Bank[129] on their facts, the Privy Council concluded that Mrs Zyngier was not liable as a co-surety on the bills of exchange alongside the drawer and indorser. Lord Brightman explained this conclusion on the following basis:[130]

> "If a third party ... guarantees a bill of exchange for the benefit of a bank which discounts it, the normal understanding will be that the surety guarantees that payment will be made by one or other of the parties to the bill who are liable upon it, whether as acceptor or drawer or indorser. It will not be the normal understanding that the surety intends to place himself on a level with the drawer, so as to be answerable equally with the drawer if the acceptor defaults. There is no reason why he should be. There is no reason to suppose that, in a contract between the bank and the surety, the surety desires to confer a benefit on the drawer and to share with him the responsibility for the dishonoured acceptance. ... It would be possible for a bank guarantee to be so worded that the surety deliberately places himself upon an equal footing with the drawer or indorser of the bill discounted by the bank, but it would produce an irrational result. ... In the opinion of their Lordships the mortgage imposed no liability on Mrs Zyngier in respect of the bills unless there was default both by the acceptor and the drawer."

Thus, as between Zinaldi and Scholefield on the one hand, and Mrs Zyngier on the other, having regard to the circumstances of the case, and the terms of the mortgage granted by Mrs Zyngier in particular, Mrs Zyngier's liability on the bills was only secondary to that of Zinaldi and

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127 Ibid., at 574 [emphasis added].

128 (1807) 14 Ves. Jun. 160, 33 E.R. 482.

129 (1880) 6 App. Cas. 1.

130 Ibid., at 574-75. [Emphasis added]

Scholefield. This was so even though the relationship between Zinaldi and Scholefield, as acceptor and drawer, was itself, as has already been seen,[131] one of primary and secondary liability on the bills. "Consequently," the Privy Council concluded,[132] "Scholefield, upon paying as drawer the amount due upon the bill, had no right of contribution against Mrs Zyngier." Neither, of course, for the same reason, was it entitled to be subrogated to the rights of the bank as mortgagee under the mortgage granted by Mrs Zyngier to secure her guarantee.

It is submitted that this case fully supports the thesis of this paper. According to this thesis, Scholefield should only have succeeded in its claims against Mrs Zyngier for subrogation - and, it could be added, for contribution - if it could show that Mrs Zyngier had been "unjustly enriched" at Scholefield's expense by its payment to the bank of the amount due on the five dishonoured bills of exchange. Undoubtedly, Mrs Zyngier had been "enriched" by Scholefield's payment to the bank, for the bank could not subsequently seek payment from her, as it might otherwise have done previously pursuant to the terms of her guarantee. She was, in other words, "enriched" in the sense that she was discharged from her liability to the bank as Zinaldi's surety in respect of the five bills of exchange - she was "saved expense".

But Scholefield also had to establish that there was something in the circumstances of the case which made it "unjust" or "inequitable" for Mrs Zyngier to retain that enrichment or benefit at its expense. Only then would Scholefield be entitled to the equitable or restitutionary remedies

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131 Supra, pp. 125-26.

132 Ibid., at 575.

of subrogation and contribution. That "something", Scholefield contended, was the fact that pursuant to the mortgage, Mrs Zyngier was, like itself, a surety for Zinaldi's performance of its obligations to the bank. Both itself and Mrs Zyngier, it contended, were in the same position, and were equally liable when Zinaldi dishonoured the five bills of exchange.

The Privy Council accepted that if this was the correct construction of Mrs Zyngier's liability under the mortgage, then her retention of the benefit of Scholefield's payment to the bank would have been "inequitable" or "unjust", and Scholefield would have been entitled to contribution and subrogation to remedy that result. But, in their Lordships' view, as has been seen,[133] this was not the correct construction of the mortgage. In the absence of any clear indication in the mortgage to the contrary, the correct construction in their view was that Mrs Zyngier was only liable in respect of the bills of exchange in the event of "default both by the acceptor and the drawer." It would be "irrational", said Lord Brightman,[134] were the mortgage to be construed in the manner contended for by Scholefield. This being the correct construction, it was not, therefore, inequitable or unjust for Mrs Zyngier to retain the benefit of Scholefield's payment to the bank. As Lord Brightman expressed it, upon this construction of the mortgage:

> "ex hypothesi no injustice ensued to the drawer upon the bank's adoption of that course [ie. calling upon the parties to the bills of exchange before calling upon Mrs Zyngier] and no case for the intervention of a court of equity could arise."[135]

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133 Supra, p. 159.

134 [1986] A.C. 562, at 575.

135 [1986] A.C. 562, at 574.

Had the bank adopted the course of calling upon Mrs Zyngier first, then injustice might have ensued, not however to Scholefield, but rather to Mrs Zyngier. For, upon the above construction of her liability, Mrs Zyngier was only secondarily liable vis-å-vis Scholefield on the bills of exchange. Yet her payment would thereby discharge Scholefield's liability, as a party to the bills of exchange, to the bank as holder of the bills. Given that Scholefield was primarily liable vis-å-vis Mrs Zyngier for payment of the bills of exchange, it would be unjust for Scholefield to retain the benefit of her payment. A restitutionary case for the intervention of a court of equity by way of reimbursement and subrogation would thus have arisen. It would not necessarily have to be pursed in this way, however, for the same result is achieved by the relevant bills of exchange legislation, as the Privy Council recognised:[136]

> "[I]f Mrs. Zyngier had taken over the bills from the bank [as she would be entitled to do upon payment by her], she as holder could have demanded payment from Scholefield as drawer, and it is not immediately apparent on what ground Scholefield could have resisted payment. This suggests that there may be an underlying fallacy in Scholefield's claim [for contribution and subrogation in the event that it paid the bank]."

Thus, it is submitted, the result and reasoning in this case fully support and provide a useful illustration of the thesis of this paper.

D. Conclusion

This examination of the operation of subrogation in relation to bills of exchange reveals yet again, it is submitted, the essentially restitutionary nature and operation of subrogation. There is little

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[136] [1986] A.C. 562, at 569.

difference, it is submitted, at base between the operation of subrogation in favour of accommodation parties to bills of exchange, and its operation in relation to those who indorse or draw bills for value, despite the misleading perception that accommodation parties are sureties in the strict sense, whereas indorsers and drawers for value are only quasi-sureties at best. The right of subrogation possessed by both classes of party, it is submitted, rests in substance on the existence of unjust enrichment between the party claiming subrogation, and the party against whom relief, in particular the right to securities, is sought. In the absence of this unjust enrichment, it has also been seen, a right to subrogation should be denied. The thesis of this paper, it is submitted, holds true.

CONCLUSION

Chapter 8

CONCLUSION

Subrogation is a subject fraught with difficulties. Even fundamental questions - "what is subrogation?", "where does it come from?", "how does it operate?", "what is the basis of its operation?" - are far from being easily answered. One of the principal reasons for this is simply that subrogation is all too often considered in a fragmented form, filtered through the perceptions of a particular category of user, rather than as a discrete subject worthy of study in its own right. Thus, subrogation is dealt with in texts on suretyship, in texts on insurance, in texts on bills of exchange, and so on, in each case according to the precepts of those areas of law. Only rarely do such texts attempt to integrate their particular treatment of subrogation with treatments of subrogation in other contexts.

Examination of particular categories of user - such as the surety's right of subrogation - do not necessarily reveal a better state of affairs. Even in this limited context, subrogation is still often subject to the same fundamental difficulties - "is there a right of subrogation?", "what is its nature?", "what does it entitle one to?", "how does it operate?". Furthermore, this may be so notwithstanding the antiquity of the particular category of use. Time, of itself, is no guarantee that these difficulties have been overcome.

This is true, it has been submitted in this paper, even in relation to the surety's right of subrogation, despite the fact that this particular category of use of subrogation is generally considered the oldest, most

established use of subrogation. Thus, the traditional explanations and analyses of the surety's "right of subrogation" are beset with problems. They are often inconsistent; they often fail to comprehend and consider all the various rights subsumed by the expression "the surety's right of subrogation"; they are uncertain whether subrogation is primarily a "right" or a "remedy"; and they generally fail to explain satisfactorily the theoretical basis of the "right" or "remedy", beyond the expression of general notions of "equity and justice". Many of these problems have been outlined and explored in some detail in this paper.

The overriding impression one could easily be left with, after examining these traditional explanations and analyses of the surety's right of subrogation, is that there is little hope of ever satisfactorily explaining either this particular category of subrogation, or subrogation generally. But this, it has been submitted, is not necessarily so. For Anglo-Americn law, as it has developed over the course of the twentieth century, and particularly in the last two or three decades, has offered a new explanation and analysis of subrogation, one which views subrogation in restitutionary terms, based upon the principle of unjust enrichment. Subrogation, it is said, is essentially a remedial technique that can be used to effect restitution in certain given situations. The only essential preconditions for its use are a tripartite relationship, and unjust enrichment between two of the parties to that tripartite relationship. Subject to other restitutionary constraints, the party who has conferred the enrichment on the other may prima facie be subrogated to the place of the third in order to exercise for his own benefit any rights or remedies the third may have against the party unjustly enriched.

This explanation and analysis of subrogation is an attractive one, for it offers a theoretical basis for reconciling all the various categories of use of subrogation, and for devising new uses of subrogation in the future. The immediate implication of this approach, however, is that the established categories or "rights" of subrogation need to be reassessed, with a view to their being individually explained in restitutionary terms based on the unifying principle of unjust enrichment. If this cannot be done, then the attractiveness of this new restitutionary explanation of subrogation may prove to be both superficial and, in the end result, as inadequate as the traditional explanations.

The thesis of this paper has been that this new view of subrogation as a general restitutionary remedial technique does offer a sound basis for understanding and explaining subrogation, both generally, and in relation to particular established categories of subrogation. The particular category of use primarily considered in this paper has been the oldest, most established of the various so-called "rights" of subrogation, namely the surety's right of subrogation. Examination of this right of subrogation has revealed, it has been submitted, many features that do evidence and reflect the view that it is essentially restitutionary in nature and can be explained in accordance with the principle of unjust enrichment. It has been submitted that the thesis of this paper therefore holds true in relation to the paradigm, or quintessential, tripartite relationship.

This has been further tested by considering the use of subrogation in the context of bills of exchange. It has been seen that the remedial technique of subrogation has been used in aid of various parties to bills of exchange. This is done in some instances on the basis that the relevant

parties are essentially sureties, and entitled thereby to subrogation; and in some instances on the basis that the parties are in a sufficiently analogous position to sureties to merit the use of subrogation in their favour. It has been shown, it is submitted, that the supposed differences in this regard between the various parties to bills of exchange are largely illusory, at least in relation to the availability and explanation of the use of subrogation. Instead, the use and operation of subrogation in this context, it has been submitted, also evidences and supports the thesis of this paper that subrogation, both generally and as it operates in its particular established categories, is essentially restitutionary in nature and can be explained in accordance with the principle of unjust enrichment.

This is not to say, however, that this explanation of subrogation in restitutionary terms necessarily solves all the problems surrounding subrogation, either at a general level or in relation to a particular category of use. Quite clearly, it would be going too far at this stage in the process of assimilating subrogation into the law of restitution to say that it does. But this objection, it is submitted, is, in large measure, a peripheral objection to the reformulation of subrogation in restitutionary terms. For, at base, this restitutionary view of subrogation provides us with a conceptually integrated, theoretical model of subrogation which can be used to understand and explain subrogation both generally and particularly, now and in the future. Ultimately, this is perhaps the greatest reward that the law of restitution has to offer the common law. With respect, it is a reward that should not lightly be denied.

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