

Proprietary remedies in insurance subrogation

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The indemnity insurer's ability to reduce its loss has traditionally been achieved through the doctrine of subrogation. Classic subrogation allows the insurer to rely on the insured's chose in action and seek compensation from a liable third party. The doctrine has also been used to establish the insurer's claim to damages or compensation received by the insured.¹ The following is a discussion of the issues involved in the award of proprietary remedies to satisfy the insurer's claim to subrogated damages. It includes brief introductions to subrogation based on the indemnity relationship, and three different theories on the award of proprietary remedies. It will be shown that the nature of the insurer's right is far from settled, and that the award of the desired proprietary interest may depend on the justice of the particular situation. This may deprive insurers of commercial certainty. It is concluded that insurers seeking certainty of outcome should use statutory or equitable assignments to achieve the desired ownership.

I INTRODUCTION

For, as thou urgest justice, be assured
Thou shalt have justice, more than thou desirest.²

The large number of insolvencies which occurred in the 1980s, and the resulting litigation (some of which continues today), has demonstrated that the awarding of proprietary remedies impacts significantly on several different levels. Given the role of insurance in modern economies, the importance of subrogated proprietary interests should not be downplayed. Whether it is the collapse of a bank,³ or the bankruptcy of an individual, the commercial and domestic insurance industries will be affected. There is inevitably competition between a defendant's insurer and the defendant's general creditors. In such times the parties must know what to expect from the courts and the doctrine of subrogation. The future is sure to yield significant developments in the law of restitution, much of which will have a direct effect on the proprietary rights of insurers. The recent decision of the House of Lords in *Lord Napier & Ettrick v Hunter* has been seen as a victory for insurers, but as demonstrated below the "justice" of the case carries with it significant uncertainties.

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1 *Lord Napier & Ettrick v Hunter* [1993] AC 713.

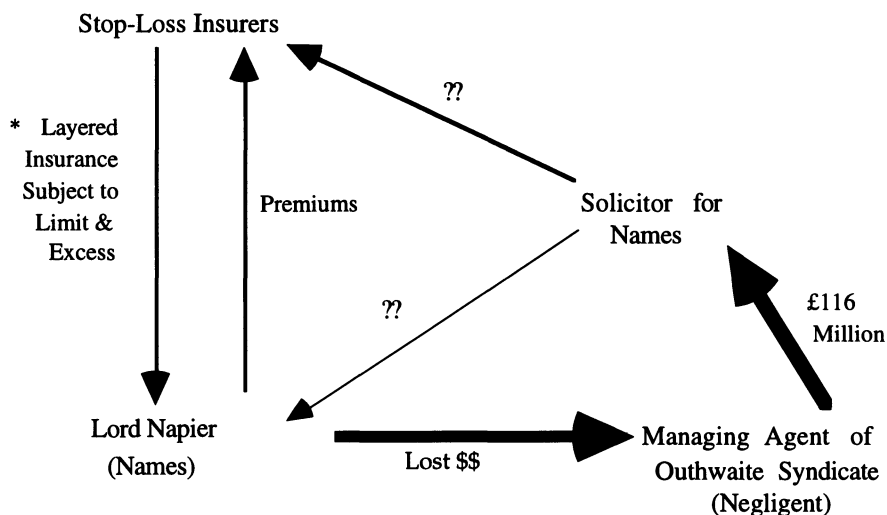
2 William Shakespeare *The Merchant of Venice*, Act IV, Scene I.

3 *In re Goldcorp Exchange Ltd* [1994] 3 WLR 199; *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Co (Bahamas) Ltd* [1986] 1 WLR 1072.

II THE HOUSE OF LORDS IN *LORD NAPIER & ETRICK V HUNTER*

A The Facts

A total of 246 Lloyd's names, members of the Outhwaite syndicate, were insured under personal stop-loss policies. The policies each included an "excess" and a "limit".⁴ If the name's loss was within the agreed excess amount then the stop-loss insurer was not obliged to compensate the name. The stop-loss insurer would compensate the name for any losses above the excess amount, but only up to the agreed limit of the policy. The names incurred losses and made claims under their stop-loss policies. The stop-loss insurers paid out under the policies and the names sued the managing agents of the syndicate, alleging that the losses had been caused by their negligence. The names eventually settled with the agents for £116 million, which was paid to the names' solicitors to await distribution.



However, the stop-loss insurers claimed an equitable proprietary interest in the settlement money to the extent they had paid out under the policies. This proprietary claim was chosen, because the stop-loss insurers wanted to minimise administration costs and to avoid the need for legal action against each of the 246 names.⁵

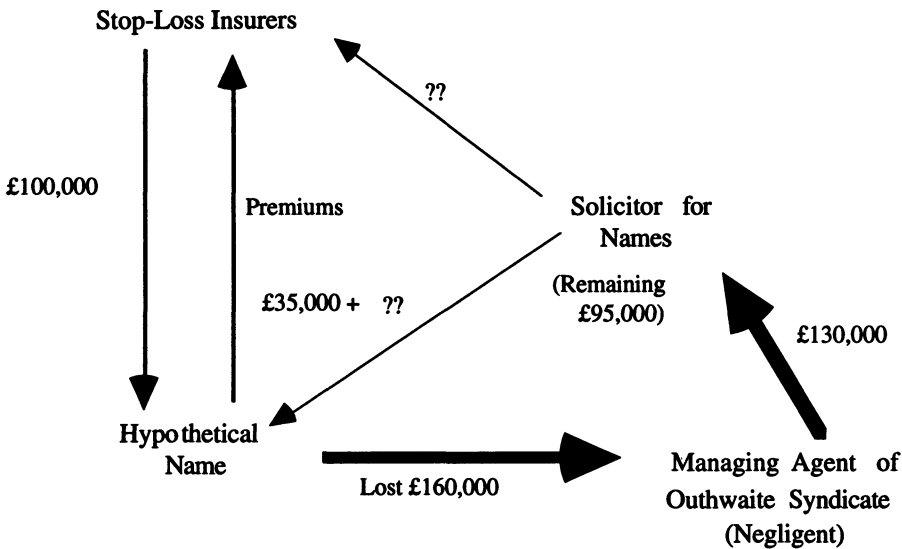
The flow of money is represented by the diagram above: the question at issue was whether any of the £116m should be paid by the solicitor for the names directly to the stop-loss insurers (rather than to the names), and if so what amount. For ease of understanding their Lordships chose to deal with a hypothetical case which represented

⁴ *Lord Napier & Etrick v Hunter* [1993] AC 713, 729.

⁵ Above n 4, 719.

the facts of each policy.⁶ Thus it was assumed that the hypothetical name had lost £160,000 in total, but had received £100,000 from the stop-loss insurers and now £130,000 (flowing from settlement in respect of the agent's negligence) was awaiting distribution. It was also assumed that the hypothetical stop-loss policy had an agreed excess of £25,000 and a limit of £100,000.

It should be noted that both parties agreed that the name could first be reimbursed for any loss above the £125,000 (including excess) limit set in the stop-loss policy. Thus the name would have priority to £35,000 of the £130,000 received from the negligent agent. Therefore the dispute really concerned the distribution of the remaining £95,000.



B The Issues

- 1 Whether the stop-loss insurers had an equitable proprietary interest in any of the settlement moneys and/or whether any of the moneys were impressed with a trust in favour of the stop-loss insurers.
- 2 Whether the remaining £95,000 should be apportioned firstly to the loss borne by the name alone (the £25,000 excess) and only thereafter to the insurer, or whether the insurer's £100,000 indemnity should take priority, leaving nothing for the name.

⁶ Above n 4, 729.

C *The Court Decisions*

In the High Court Saville J decided that the insurers were confined to their personal remedy for money had and received. Thus the damages would be distributed to the names. The insurers would have to determine, by application to the court, each claim against every individual name. His Honour also decided that each name would have priority to the damages to the extent necessary to meet their total loss. So of the £130,000 damages received, the name would keep £60,000 and pay £70,000 to the stop-loss insurers. The Court of Appeal, while agreeing with Saville J on the first issue, reversed his finding on the second issue and awarded the insurers priority up to the limitation amount. The decision of the House of Lords on the first issue was that the insurers, on payment of a name's claim, had an equitable interest in the damages received by that name. This equitable interest would be protected by an equitable lien. Their Lordships upheld the Court of Appeal's decision on the second issue.

D *Analysis of the House of Lords Decision*

Their Lordships found that subrogation was not just a common law doctrine, but that the insurer's claim was also recognised in equity. In his speech to the House, Lord Templeman said:⁷

The principles which dictated the decisions of our ancestors and inspired their references to the equitable obligations of an insured person towards an insurer entitled to subrogation are discernible and immutable. They establish that such an insurer has an enforceable equitable interest in the damages payable by the wrongdoer. The insured person is guilty of unconscionable conduct if he does not provide for the insurer to be recouped out of the damages awarded against the wrongdoer. Equity will not allow the insured person to insist on his legal rights to all the damages awarded against the wrongdoer and will restrain the insured person from receiving or dealing with those damages so far as they are required to recoup the insurer under the doctrine of subrogation.

Lord Goff expressed "no doubt" that the task of the courts was to see the two strands of equity and the common law "moulded into a coherent whole".⁸

However, there appears to be a difference of understanding concerning the consequences of finding that subrogation was recognised in equity. To use the language of "implied contract" is to use the language of the common law analysis. To imply a term into every contract of indemnity, because of the nature of the contract, is a common law technique which would institutionalise the insurer's proprietary remedy.

7 Above n 4, 738.

8 Above n 4, 743.

The use of the common law's implied term was still present in the speeches of Lord Templeman:⁹

In my opinion promises implied in a contract of insurance with regard to rights of action vested in the insured person for the recovery of an insured loss from a third party responsible for the loss confer on the insurer an equitable interest in those rights of action to the extent necessary to recoup the insurer who has indemnified the insured person against the insured loss.

and Lord Browne-Wilkinson:¹⁰

In my judgment, the correct analysis is as follows. The contract of insurance contains an implied term that the assured will pay to the insurer out of the moneys received in reduction of the loss the amount to which the insurer is entitled by way of subrogation. That contractual obligation is specifically enforceable in equity against the defined fund (i.e., the damages) in just the same way as are other contracts to assign or charge specific property e.g. equitable assignments and equitable charges.

The writer suggests that if a proprietary remedy was to be given in this case, then the correct analysis was that of Lord Goff. His Lordship stated that subrogation in the law of insurance arises in a contractual context, and that it gave effect to the principle that insurance is intended to provide "an indemnity but no more than an indemnity". Lord Goff then went on to say that:¹¹

In so far as the principle requires the payment of money, it could no doubt be formulated as an implied term, to which effect could have been given by the old action of money had and received. But I do not see why the mere fact that the purpose of subrogation in this context is to give effect to the principle of indemnity embodied in the contract should preclude recognition of the equitable proprietary right, if justice so requires.

Following this statement, subrogation is a common law doctrine based on the contract of indemnity, and equity can give effect to subrogation if the unjust nature of the situation so requires. This is different from saying that in every situation the insurer will have a proprietary interest in the damages received by the insured. The writer suggests that the equitable recognition of insurance subrogation does not result in the insurer automatically receiving a proprietary remedy. The creation of a proprietary interest is not an institutionalised remedy that will be available to every indemnity situation. Under the proposed analysis the courts will have the option of granting a personal or proprietary remedy depending on the justice of the particular situation. This allows the analysis of whether a proprietary remedy is necessary in situations of insolvency.

The second finding of the House of Lords was to award the insurers a proprietary interest in the damages held by the solicitors. This proprietary interest was in the form

9 Above n 4, 736.

10 Above n 4, 752.

11 Above n 4, 744.

of an equitable lien. This prevented the solicitors from distributing the insurers' share of the damages to the names. An equitable lien was chosen instead of a constructive trust because the trust obligations were seen as too onerous for the situation. A constructive trust was also unnecessary as the insurers' rights only went to the amount of indemnity. Any increase in the value of the property would have gone to the names. It should also be noted that their Lordships assumed that the insurers should have priority over general creditors in the event of a name's insolvency. This is indicated by Lord Goff:¹²

... and further that the rights of the insurer to such money were sufficiently strong to entitle the insurer to priority in the event of the assured's bankruptcy, ...

and expressly affirmed by Lord Templeman:¹³

[I]f the argument on behalf of the names is correct, the unsecured creditors of the insured name will benefit by double payment. The stop loss insurers will be in a worse position than an unsecured creditor because the insurers could not resist payment under the policy whereas an unsecured creditor may choose whether to advance moneys or not. In the case of the bankruptcy of the name, the right of the insurer to subrogation will be useless unless equity protects that right.

Finally, their Lordships decided not to proclaim that the insurers had a proprietary interest in the insured's chose in action against the liable third party. Despite Lord Templeman's strong statements in favour of this conclusion, their Lordships resisted the temptation to make this obiter statement.¹⁴ This means that their Lordships separated any interest the insurer may have had in the chose in action, from the proprietary interest in the damages received from that chose in action. Their Lordships awarded a proprietary interest without finding that the insurer had a pre-existing proprietary interest in the original property. Without this pre-existing proprietary interest, or a specific intention on behalf of the parties to transfer such an interest,¹⁵ the court cannot be interpreted as enforcing an actual or intended trust obligation. Thus, the proprietary remedy in this case should be seen as an obligation created by the court independently from the contracting parties' intentions.

E Summary

As can be seen from the above, there are three aspects of their Lordships' decision which are relevant to this paper:

- (1) Their Lordships have indicated that the insurer's proprietary remedy over the damages received by an insured, could be awarded even if the insurer did not have

12 Above n 4, 744.

13 Above n 4, 737.

14 Above n 4, 740, 745, 752.

15 See A Burrows *The Law of Restitution* (Butterworths, London, 1993) 40 - 45, where it is argued that Burrows, Birks, and Goff and Jones all require one of these two factors to warrant granting a proprietary rather than a personal remedy.

a proprietary interest in the insured's chose in action against a liable third party. Thus, the House of Lords were able to decline giving a decision as to the nature of the insurer's interest in an insured's chose in action.

- (2) There is some uncertainty as to whether the proprietary lien will be an institutionalised remedy applying to all indemnity contracts. The writer suggests that following Lord Goff's speech, the preferable view is that the lien was a restitutionary proprietary remedy, and as such was dependant on the circumstances of the case.
- (3) Their Lordships placed a proprietary lien over the money held by the defendants' solicitors, which enabled the plaintiff to seek an injunction preventing the distribution of that money to the defendants. There is also some indication that this lien would have been imposed even if a defendant was insolvent.

III DOES SUBROGATION GRANT A PROPRIETARY INTEREST IN THE INSURED'S LITIGATION RIGHTS ?

In this Part classic subrogation is discussed. The classic definition of the doctrine is the insurer's ability to stand in the shoes of the insured and take the insured's legal action against a third party. The question discussed here is what sort of interest the insurer has in the insured's chose in action. If classic subrogation is a proprietary interest, the property in question is the ability to take a legal action against a third party. The success of the action, and the cost and reward for taking such an action, are equally uncertain events. The third party's understanding of to whom they owe a responsibility may also be an important policy consideration.

A *The Current Understanding*

The current understanding of the rule depends upon whether the insurer has indemnified the insured for the total loss or merely for a portion of the loss.¹⁶ If the insurer has compensated the insured for a total loss then the insurer is said to have *dominus litis*, in that the insurer has the right to take over or control proceedings in the name of the plaintiff. If the insured has not been indemnified for the total loss suffered then the insured retains control of the proceedings. Only upon the insured's failure to initiate proceedings can the insurer exercise the insured's rights by way of subrogation. It is the writer's contention that the retention of *dominus litis* by the insured who has not been fully indemnified demonstrates that such an insured retains ownership of the chose in action. In these situations subrogation gives the insurer the ability to bring an action if the insured declines, and the right to expect that the insured will give due regard to the interests of the insurer when conducting the action. If the insurer can show that the insured and third party were acting mala fide the insurer's interests, the insured is liable in personam to the insurer.

¹⁶ DStL Kelly and ML Ball *Principles of Insurance Law in Australia and New Zealand* (Butterworths, Wellington, 1991) 507.

Dominus litis lies at the heart of cases concerning the effect of insureds' releases of (or compromises with) liable third parties. In *State Government Insurance Office (Qld) v Brisbane Stevedoring Pty Ltd*, Barwick CJ made the following observation:¹⁷

It is ... settled law that an insured may not release, diminish, compromise or divert the benefit of any right to which the insurer is or will be entitled to succeed and enjoy under his right of subrogation. On occasions an attempt by the insured to do so will be ineffective against the insurer because of the knowledge of the circumstances which the person under the obligation to the insured may have. On other occasions when the insured's act has become effective as against the insurer, the insured will be liable to the insurer in damages, or possibly, on some occasions for money had and received.

Unfortunately, this statement was interpreted as applying to both full and partial indemnity situations. Thus, in *Morganite Ceramic Fibre Pty Ltd v Sola Basic Australia Ltd*,¹⁸ Smart J did not draw any distinction based on whether the insured had *dominus litis*, and simply focused on the third party's knowledge of the insurer's interest. His Honour found that a release by the insured did not prevent the insurer's later action against the third party. However, the possession of *dominus litis* should make the difference in deciding whether an insurer is bound by the actions of the insured. Indeed, Derham states that:¹⁹

The correct rule would seem to be that a release granted by the insured to the third party will not be effective as against a subrogated insurer if that release indicates mala fides by the insured and the third party in respect of the insurer. Of course, the fact that the third party has knowledge of the insurer's payment invariably will lead to a presumption of mala fides, *though this would not be so if the insured was entitled to be dominus litis*. (Emphasis added).

Of course, the party in control owes an obligation to consider the loss being borne by the other party. Thus if the controlling party prejudices the dependent party's claim against the third party, the dependent party could possibly claim damages in compensation. However the obligation is not absolute and, as long as the controlling party acts reasonably, liability to the dependent party will not be incurred.²⁰ The "costs" of the proceedings usually results in the insurer bringing the action against the liable third party. But as far as the justice system is concerned, if the insurer has met only a portion of the insured's actual loss, the plaintiff is still the insured.²¹

17 (1969) 123 CLR 228, 241.

18 (1988) 5 ANZ Insurance Cases 60-883.

19 SR Derham *Subrogation in Insurance Law* (The Law Book Company, Sydney, 1985), Chap 8, 92.

20 See *Arthur Barnett Ltd v National Insurance Co of New Zealand* [1965] NZLR 874, where the insured was obliged to sue the third party only for reasonable damages as opposed to the total loss suffered.

21 Of course, several judges have recognised that the parties concerned are really insurance companies. Some have suggested that the filing of affidavits should be enough for the insurance companies to take action in their own name.

B When should the Insurer have a Proprietary Interest in the Legal Action?

Proprietary ownership of the potential legal action is a concern only in those cases where the insurance does not cover the actual loss. The eventual benefits of a legal action can be apportioned, but the legal action itself is only a potential. It cannot be used in portions unless all the "interested parties" or "owners" of the portions attend the hearing. This is why the insurer and the insured seek *dominus litis*. The courts should not do more than is necessary to enable the insurer to recover her loss. If the insured fails to use a legal action which would reduce the insurer's loss, or fails to claim damages sufficient to compensate the insurer's loss, then the insurer should be able to force the insured to assist the insurer in reducing that loss. But the insurer cannot settle a claim with the third party, nor can the insurer prevent the insured from taking a legal action against a liable third party.²² Thus, it is unnecessary to grant the insurer a proprietary interest in the insured's legal action.

The importance of the indemnity principle should not be overlooked when discussing this aspect of subrogation. The indemnity principle does not prevent the insured from attaining compensation for her total loss; it merely prevents the retention of any further profit. This also means that the insurer should not benefit any more than the amount paid to the insured under the policy. Given that the insured is directly affected by the third party's wrongful act, and that the insured is still suffering an uncompensated loss, the courts cannot justify automatically awarding the insurer a proprietary interest in a portion of the legal action. If the insured still has losses to recover from the liable third party, then those losses (unless the insured has agreed to forgo priority to the insurer) must be met before the insurer can take control of the legal action. The insurer should receive a proprietary interest in the legal action only when the insurer has compensated the insured for the actual total loss suffered. Indeed, the writer postulates that similar reasoning results in only absolute assignments of choses in action being recognised by section 130 of the Property Law Act 1952. Such an approach is also consistent with the "actual or constructive total loss" required for the doctrine of abandonment, which gives the insurer proprietary ownership of the surviving property.

22 *Morley v Moore* [1936] 2 KB 359; *Hobbs v Marlowe* [1978] AC 16.

IV BIRKS AND BURROWS: THE NEED FOR A PRE-EXISTING PROPRIETARY INTEREST IN THE AWARD OF PROPRIETARY REMEDIES

There is little doubt that the insured is unjustly enriched when she receives indemnity from the insurer, and then receives damages from a liable third party. The question is whether the courts should remedy this situation with a proprietary or personal remedy. At issue is the effect proprietary remedies will have on an insolvent insured's third party creditors.²³

In all these cases, where the primary aim is to assert a right *in rem*, the reason why the plaintiff turns to the second measure of restitution is, not because he finds that measure intrinsically more attractive than the other, but that rights *in rem* yield priority in an insolvency over unsecured creditors and cannot be asserted in the first measure. In order to be able to say that he owns or has a lien, he must be able to identify in the defendant's hands the asset in which he claims to have that right. Hence in these cases the plaintiff's desire for restitution in the second measure is consequential upon his desire to assert a right *in rem*.

Because commerce requires a degree of certainty in ownership, academics in the area of restitution have attempted to predict when the court will and should award a proprietary remedy. In this Part three of those theories will be discussed.²⁴

A *Birks and the Pre-existing Proprietary Base*

According to Professor Birks, plaintiffs seeking proprietary remedies should show that when the property in question originally came into the control of the parties the plaintiff retained (or obtained) a legal or equitable proprietary interest in the property.²⁵ The plaintiff must have had an *in rem* interest from the very beginning of the story, which was not lost by any subsequent transfers or intermixtures by the defendant.²⁶

The shortest summary of all this is that if the plaintiff wants to assert a right *in rem* in the surviving enrichment he must show, not only that the enrichment originally received does at least in part survive, but also that the story of the changes which

23 P Birks *An Introduction to the Law of Restitution* (Clarendon Press, Oxford, 1985) 376.

24 It would be beyond the scope of this paper to discuss all the theories of when proprietary remedies should be awarded. But the interested reader should see: WMC Gummow "Unjust Enrichment, Restitution and Proprietary Remedies" in PD Finn (ed) *Essays on Restitution* (The Law Book Company Limited, Sydney, 1990); PD Maddaugh & JD McCamus *The Law of Restitution* (Canada Law Book Inc, Aurora, Ontario, 1990); P Millett "Bribes and Secret Commissions" [1993] *Restitution Law Review* 7; DM Paciocco "The Remedial Constructive Trust: A Principled Basis for Priorities Over Creditors" (1989) 68 *Can BR* 315; and AJ Oakley "Proprietary Claims and their Priority in Insolvency"- *Occasional Paper Series No. 2* (Centre for Commercial and Property Law, Queensland University of Technology, 1994).

25 Above n 23, 377-391.

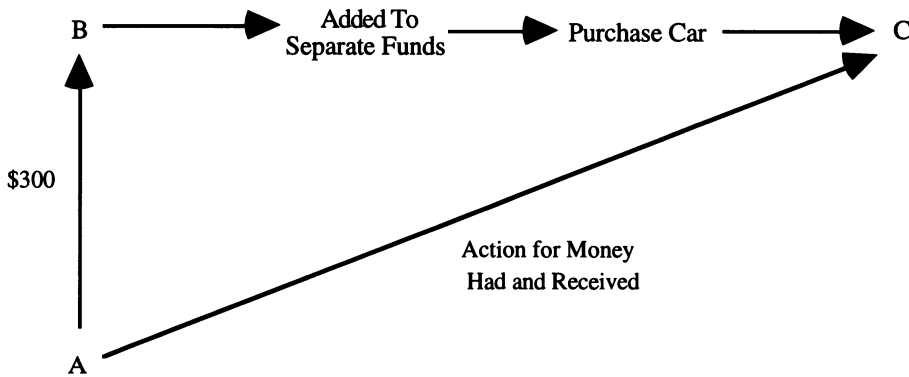
26 Above n 23, 380.

have overtaken it began from matter belonging to him and passed through no events (other than the neutral events of intermixture and substitution) such as would by nature extinguish his title: to end with a right *in rem* he must start with a right *in rem* and nothing must happen to extinguish that right *in rem*, other than loss of identity.

Birks suggests that tracing is simply a means of identifying any remaining enrichment in the possession of the defendant, and that equitable tracing should not require a fiduciary relationship.²⁷ Equitable tracing will enable the courts to identify remains of property that would normally have been incapable of separation from the defendant's assets. But this ability to reidentify property is unrelated to whether a proprietary remedy should be granted. Hence, once tracing has established that the asset in the possession of the defendant is the remaining enrichment derived from the plaintiff's loss, the courts should then consider whether the plaintiff retained a proprietary base in the original property.

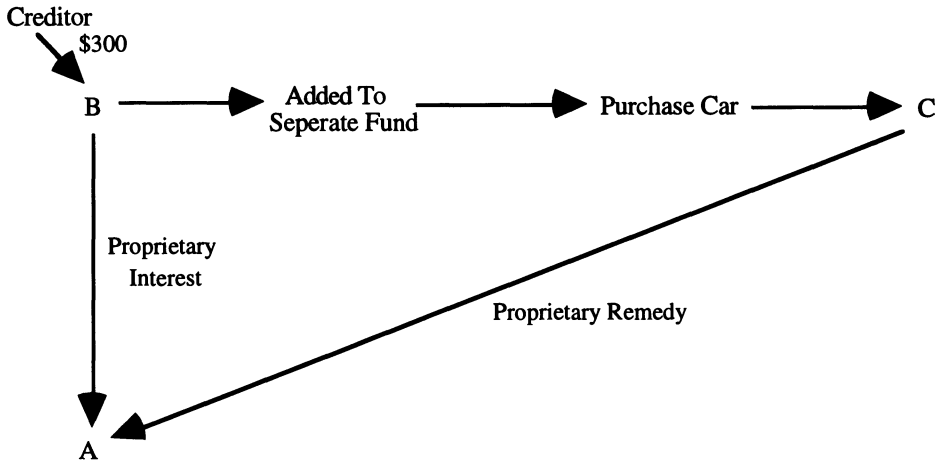
For example:

Assume that A mistakenly paid B \$300, and B then used that \$300 along with his own money to buy a car, which he gave to C. A would be able to trace C's enrichment to A's loss, but would be unable to seek a proprietary remedy due to the fact that A failed to retain a proprietary interest in the money originally given to B.



In contrast to this, suppose that B, acting as A's agent, received that \$300 from A's creditor. In this situation A would be able to seek a proprietary remedy because the nature of A and B's relationship meant that A was entitled to a proprietary interest in the money.

27 Above n 23, 375.



Following Birks' analysis, if it was discovered that the car once belonged to Elvis and subsequently doubled in value, the proprietary remedy available to A would be a constructive trust so as to enable A to benefit from the increased value of the original property.

B Burrows and the Retention of the Plaintiff's Property

Burrows' theory should be examined in light of his different approach to constructive trusts and tracing. Burrows advocates that constructive trusts are substantive remedies which create equitable ownerships.²⁸ In his opinion "pure proprietary remedies" are those remedies that simply "revest" or reassert the plaintiff's property rights. Thus, only the "equitable lien and the proportionate share chosen or imposed following tracing are restitutionary proprietary remedies triggered by pre-existing equitable ownership".²⁹ This views the equitable lien as a "tracing remedy" that is based on the concept that equitable ownership of the property never left the hands of the plaintiff. As far as common law or legal proprietary interests are concerned, Burrows would leave those situations to be remedied by the existing common law actions such as rescission, recaption, conversion. Hence, Burrows states that the approach adopted in his book is:³⁰

[T]hat proprietary restitutionary remedies (for example, the recovery of land, equitable liens, and the proportionate share remedy) are, with justification, triggered by the retention of the plaintiff's property without his consent

Under Birks' analysis, if equitable tracing reidentifies an enrichment in the hands of the defendant, it is necessary then to consider if there was a proprietary base in which to

28 A Burrows *The Law of Restitution* (Butterworths, London, 1993) 38.

29 Above n 28, 39.

30 Above n 28, 369.

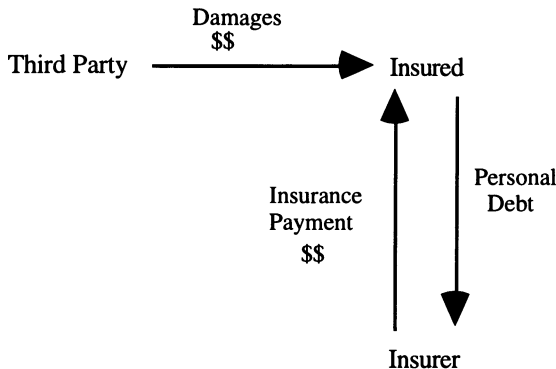
ground a claim for a proprietary remedy. If there is no proprietary base, then a personal remedy should be granted. But according to Burrows' analysis, equitable tracing is the remedy sought (because it establishes that the property in question always belonged to the plaintiff) and an equitable lien over the property is the consequence of that remedy.

C Birks, Burrows, and the Absence of a Proprietary Interest in the Insured's Chose in Action

Essentially, both authors require the plaintiff to have some sort of pre-existing proprietary interest/ownership before they would grant a proprietary remedy to prevent the defendant's unjust enrichment. This means that, if the insurer is to be given a proprietary remedy over the damages, the insurer needs a pre-existing proprietary interest in the origin of the damages received by an insured. Without such an interest, the courts should confine the insurer's recovery to personal remedies such as money had and received.

For example:

The insured makes a claim for indemnity for a loss suffered in a motor-accident. The insurer investigates the claim and agrees to indemnify the insured. While the insurer is processing the payment, the insured receives a payment of damages from the party responsible for the accident. The insured then receives the payment from the insurer.

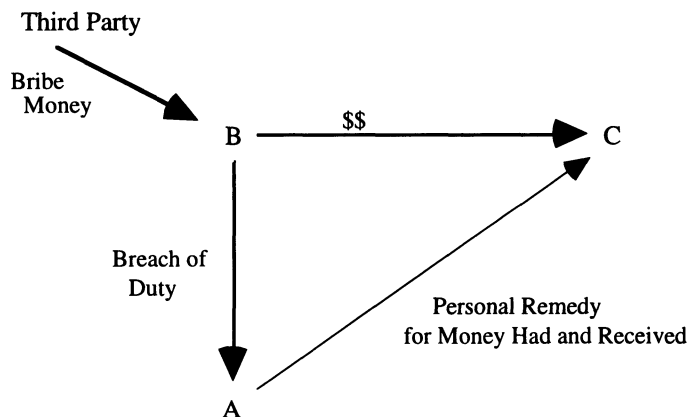


Because the insurer never retained a proprietary interest in the money paid to the insured, and never had any proprietary ownership of the money paid by the third party, the insurer should have only the personal remedy of money had and received.

The payment by the third party is a product of the insured's legal action. Thus an insurer seeking a proprietary remedy over the third party's payment would have to show a pre-existing proprietary interest in the insured's legal action. If classic subrogation had given the insurer a proprietary interest in the insured's legal action, the insurer could have traced that proprietary interest into the third party's payment. However, in cases of

partial indemnity it is difficult to establish that classic subrogation represents a proprietary interest in the insured's legal action.³¹ If there is no proprietary interest in such cases, the analysis of both Birks and Burrows suggests that the courts should not grant an insurer a proprietary remedy over damages received by an insured, unless the insurer had previously indemnified the insured for the actual total loss.

To support his analysis, Birks cites the decision in *Lister v Stubbs*,³² which dealt with the following situation:



As the money was never intended for A, it was not possible for A to assert an equitable ownership or claim that he originally had a proprietary interest.

In that case the Court of Appeal found that the plaintiff was unable to assert a proprietary interest. Burrows also cites the decision of Stirling LJ in *Stearns v Village Main Reef Gold Mining Co*,³³ but notes that Stirling LJ drew an analogy with *Lister v Stubbs*.

However, the authority of *Lister v Stubbs* has been overturned by the Privy Council decision of *Attorney-General for Hong Kong v Reid*.³⁴ In this decision, their Lordships found that a fiduciary, who received bribe money for breaching his fiduciary duty, was a

31 See above, Part III of this paper.

32 (1890) 45 Ch D 1.

33 (1905) 10 Comm Cas 89. In this case Stirling LJ rejected an insurer's trust claim over money given by the South African government to the owners of a mine from which the government had previously confiscated gold bullion.

34 [1994] 1 NZLR 1.

constructive trustee of the bribe money and any other property purchased with that money. Lord Templeman, in delivering their Lordships' decision, stated:³⁵

As soon as the bribe was received it should have been paid or transferred instant to the person who suffered from the breach of duty. Equity considers as done that which ought to have been done. As soon as the bribe was received, whether in cash or in kind, the false fiduciary held the bribe on a constructive trust for the person injured.

This reversal of the *Lister v Stubbs* authority is consistent with their Lordships' decision in *Lord Napier & Ettrick v Hunter*. As has been seen, the House of Lords separated the creation of a proprietary interest in the damages, from the issue of whether there was a pre-existing proprietary interest in the chose in action. This demonstrates an assumption that pre-existing proprietary interests are not required for the award of proprietary remedies. This assumption was also made by the New Zealand Court of Appeal in *Elders Pastoral v Bank of New Zealand*.³⁶ The writer suggests that the decisions in *Attorney-General for Hong Kong v Reid* and *Lord Napier & Ettrick v Hunter* firmly establish that current judicial opinion is contrary to the theories advocated by both Birks and Burrows. This effectively opens the pathway for the growth of the Goff and Jones judicial discretion approach.³⁷ Lord Templeman indicated that the Court's view of "what ought to have been done" will depend on considerations of prophylaxis and policy. It remains to be seen what value will be given to the concerns of general creditors in bankruptcy and the commercial desire for institutionalised certainty in the award of proprietary interests. Indeed, in *In re Goldcorp Exchange* Lord Mustill stated:³⁸

The law relating to the creation and tracing of equitable proprietary interests is still in a state of development. In *A-G for Hong Kong v Reid* [1994] A.C. 324 the Board decided that money received by an agent as a bribe was held in trust for the principal who is entitled to trace and recover property representing the bribe. In *Lord Napier and Ettrick v Hunter* [1993] A.C. 713, 738-739, the House of Lords held that payment of damages in respect of an insured loss created an equitable charge in favour of the subrogated insurers so long only as the damages were traceable as an identifiable fund. When the scope and ambit of these decisions and the observations of the Board in the *Space Investments* case fall to be considered, it will be necessary for the history and foundations in principle of the creation and tracing of equitable proprietary interests to be the subject of close examination and full argument and for attention to be paid to the works of Paciocco (1989) 68 Can. Bar Rev. 315, *Maddaugh and McCamus, The Law of Restitution* (1990), Emily L. Sherwin's article "Constructive Trusts in Bankruptcy" (1989) U. Ill. L.Rev. 297, 335, and other commentators dealing with equitable interests in tracing and referring to concepts such as the position of "involuntary creditors" and tracing to "swollen assets".

35 Above n 34, 4.

36 [1989] 2 NZLR 180.

37 See below, Part V of this paper.

38 [1994] 3 WLR 199, 227.

V GOFF AND JONES: JUDICIAL DISCRETION IN THE AWARD OF PROPRIETARY REMEDIES

A *What is Just and Equitable?*

With the Privy Council's recent abandonment of the *Lister & Co v Stubbs* authority, it is doubtful whether the need for a pre-existing proprietary interest will continue to play a role in decisions to award proprietary remedies.³⁹ Therefore, it is likely that the awarding of proprietary remedies will follow the developments advocated by Goff and Jones. In previous editions of their book they said that the award of proprietary remedies will depend on "whether it is just and equitable to do so".⁴⁰ But in response to critics in search of a more certain "generic" test,⁴¹ the authors went on to formulate a test in terms of whether the plaintiff had taken the risk of the defendant's insolvency.⁴² In the latest edition this test seems to have further developed into whether the defendant knew or did not know the facts of the plaintiff's equitable claim and whether the defendant is solvent.⁴³

When the plaintiff does rely on a pre-existing equitable title, Professor Jones provides four guidelines for the exercise of the court's discretion. They are said to take into account the ground of the plaintiff's claim, the defendant's knowledge of the facts which form its basis, and the fact of the defendant's solvency or insolvency. The four guidelines are:

- (i) *If the defendant did not know the facts which form the basis of the plaintiff's restitutionary claim and is solvent*
In this situation the plaintiff should be entitled only to the value received by the defendant, thus an equitable lien should be used to secure this amount. However, room was left for the court's underlying discretion by stating that the nature of the parties' relationship may be such as to warrant a constructive trust, even where the defendant is completely honest.⁴⁴
- (ii) *If the defendant did not know the facts which form the basis of the plaintiff's restitutionary claim and is insolvent*
As this situation dealt with two equally innocent parties, the plaintiff was not to get a windfall at the expense of the general creditors. Thus, an equitable lien was

39 See above, Part IV C of this paper.

40 *The Law of Restitution* (3rd ed, Sweet & Maxwell, London, 1986) 63.

41 See Birks above n 23, 378; Where it was stated that the issue could not be cured by "tackling the issue as though it were something to be decided from case to case on the basis of abstract reasonableness or justice."

42 Above n 40, 115. See also DM Paciocco "The Remedial Constructive Trust: A Principled Basis for Priorities Over Creditors" (1989) 68 Can BR 315; and PD Maddaugh & JD McCamus *The Law of Restitution* (Canada Law Book Inc, Aurora, Ontario, 1990) 95-96, 137-139.

43 G Jones (ed) *Goff and Jones The Law of Restitution* (4th ed, Sweet and Maxwell, London, 1993) 93-102.

44 See *Boardman v Phipps* [1967] 2 AC 67.

again used to secure the value received by the defendant. The important point is that the court is to view the parties competing as the plaintiff and general creditors. With the court's discretion, it does not necessarily follow that the plaintiff will always receive priority.

(iii) *If the defendant knew the facts which form the basis of the plaintiff's restitutionary claim and is solvent*

In this situation the defendant's knowledge brings to bear the full force of restitution in the form of a constructive trust over any property bought with the plaintiff's property.

(iv) *If the defendant knew the facts which form the basis of the plaintiff's restitutionary claim and is insolvent*

Contrary to English case law, Jones argues that the plaintiff should receive only a lien to the value of the defendant's receipt. Again, this is seen as a dispute between the plaintiff and general creditors who are not affected by the defendant's knowledge.

It should be noted that Jones' guidelines depend on the plaintiff's claim being one of equitable title.⁴⁵ But the prior existence of this equitable title does not result in the automatic award of a proprietary remedy.⁴⁶

Professor Jones also states that the court can award proprietary remedies in the absence of a pre-existing equitable title. The *Lord Napier & Ettrick* situation is cited as an example of such an award. Thus, the only justification for the award in favour of the insurer was the justice of the particular situation.⁴⁷

In other situations where a plaintiff has been granted an equitable remedy it is not easy to support the court's decision on the ground that it was protecting the plaintiff's existing equitable title. ... In these contexts, the constructive trust and the equitable lien were in reality remedies imposed by the court because it was thought just to do so. They are "nothing more than a formula for equitable relief". Similarly, it has been held that an insurer has a lien over a fund, namely, moneys paid by a third party in settlement of the assured's claim against him, in the hands of the assured's agents. It would be unconscionable not to impose the lien since the assured had been fully (sic) indemnified.

In *Lord Napier & Ettrick* Lord Goff's statements support this approach.⁴⁸

In so far as the principle requires the payment of money, it could no doubt be formulated as an implied term, to which effect could have been given by the old action of money had and received. But I do not see why the mere fact that the purpose of subrogation in this context is to give effect to the principle of indemnity embodied in

45 Above n 43, 94.

46 Above n 43, 95.

47 Above n 43, 74.

48 Above n 4.

the contract should preclude recognition of the equitable proprietary right, if justice so requires.

Indeed, Jones goes back to the broader language of "just and equitable" when discussing the effect of subrogation on third party creditors:⁴⁹

As Lord Salmon said:⁵⁰ "The test as to whether the courts will apply the doctrine of subrogation to the facts of any particular case is entirely empirical. It is ... impossible to formulate any narrower principle than that the doctrine will be applied only when the courts are satisfied that reason and justice demand that it should be." In our view the law can only be extended in a coherent and just fashion if this general principle is recognised.

B The "Indemnity" Principle and the "Justice" of the Situation

In *Lord Napier & Ettrick v Hunter* the House of Lords declared that, although the insureds were not compensated for their total loss, the insurers were awarded a proprietary interest in any damages received from a liable third party. The amount of this proprietary interest was equal to any amount paid by the insurer to the insured under the indemnity policy. This meant that the insured would not receive an unconscionable double benefit from being insured. However, this does not mean that the indemnity principle required the creation of the proprietary interest. The indemnity principle requires only that insureds not receive more than a full indemnity for their real loss, and must not be permitted to make a profit out of being insured. It is not necessary to create a proprietary interest in order to prevent the insured from making a profit. The creation of a personal debt obligation in favour of the insurer would also prevent the insured's enrichment. Thus, the reason for the creation of the proprietary interest must have been based upon other factors. It may not be deniable that, in the *Lord Napier & Ettrick v Hunter* situation, the justice of awarding a proprietary remedy was in the insurer's favour:⁵¹

There are 246 names, some of whom are resident in the United States of America and elsewhere abroad. In order to succeed in an action for money had and received stop loss insurers might be obliged to pursue litigation at considerable expense and subject to considerable delay in a country which knows nothing of an action for money had and received or does not recognise the doctrine of subrogation or confines its civil litigation to the tender mercies of juries who are unsympathetic towards insurers.

but this does not support a finding that all indemnity insurance situations will warrant the court using its discretion to award a proprietary remedy. There must be other factors which would mean that a personal remedy would result in unconscionable consequences.

49 Above n 43, 594.

50 *Orakpo v Manson Investments Ltd* [1978] AC 95, 110.

51 Above n 4, 737.

VI PROPRIETARY REMEDIES AND THE SITUATION OF AN INSOLVENT INSURED

A *The "Indemnity" Principle and the "Justice" of the Insolvency Situation*

Even if the indemnity principle supported the granting of a lien, justice may be less demanding of a proprietary remedy if the insured is insolvent. The indemnity principle is concerned to prevent the insured from making a profit. But if the insured is insolvent, the competing parties become the insured's general creditors and the insurer. It is a question of whether the insurer's claim should be paid before the unsecured creditors, or whether the insurer should rank alongside the other creditors and share in the assets proportionally. If the indemnity principle is aimed at preventing insureds from viewing insurance as a chance to make a profit, the insured's insolvency makes the concern redundant. In reality, the insured is out of the picture and should not be the court's consideration in deciding this issue of priority. It is the writer's contention that if the "average" insured were insolvent, the insurers would have adequate protection under a personal action for money had and received.

B *If the Insured was Insolvent, would the Unsecured Creditors be Unjustly Enriched?*

The result in *Lord Napier & Ettrick v Hunter* may not be the justifiable result in the average insurance situation. Situations of insolvency will involve comparing the claims of the unsecured general creditors and the insolvent person's insurers. In deciding whether an insurer should receive priority over unsecured creditors, the question is essentially: who, in the particular situation, should be seen as having taken the risk of the insured's insolvency?⁵² This does not discount any argument that the creditors will get a windfall or enrichment at the possible expense of the insurer, but acknowledges that the real issue is whether it would be unjust to allow this possible enrichment to occur. Indeed, Burrows argues that if enrichment at the expense of someone was enough to warrant a proprietary remedy, then all restitutionary remedies will be proprietary.⁵³ In an insolvency situation, all the unsecured creditors are potential losers who each have a liability owed to them by the insolvent insured. The only issue is the extent to which their loss can be wholly, or more often partially, avoided. It should be remembered that the pool of unsecured creditors will include some suppliers, trades people, and purchasers. These parties could also be viewed as having contributed to the pool of general assets, thus enriching the greater pool of creditors.

Nevertheless, it could still be argued that the insurer never undertook to bear the risk of the insured's insolvency. But what is the payment of an insurance premium for? If the role of insurance is the spreading of loss, and the paying of premiums compensates the insurer for bearing the risk of that loss, the insured's insolvency should fall within

52 DM Paciocco "The Remedial Constructive Trust: A Principled Basis for Priorities Over Creditors" (1989) 68 Can BR 315; and PD Maddaugh & JD McCamus *The Law of Restitution* (Canada Law Book Inc, Aurora, Ontario, 1990) 95-96, 137-139.

53 Above n 28, 42.

that risk. The insurer, by indemnifying the insured, takes a portion of the insured's loss. That loss then becomes the insurer's. The risk attached to that loss is that some or all of the loss will not be recoverable. The insurer agrees to bear the loss even if there is no liable third party. If the insured had not avoided the risk of the liable third party's insolvency, the insurer would have to join the third party's general creditors and share in the third party's assets proportionately. In the absence of agreements to avoid the risk of the insured's possible insolvency, it is difficult to see why the insurer should be viewed as having more rights against insured's third party creditors, than the insurer has against the liable third party's general creditors.⁵⁴ So the insured's insolvency should also fall within the risk taken by the insurer. In consideration for that risk, the insurer takes premiums from the insured. Given that unsecured creditors are generally parties who are seeking to recover compensation for unpaid debts, it is somewhat circular for the insurer to receive premiums and also claim priority over these other parties. Brett LJ, began his classic judgment in *Castellain v Preston* with the following point:⁵⁵

In order to apply the doctrine of subrogation, it seems to me that the full and absolute meaning of the word must be used, that is to say, the insurer must be placed in the position of the assured.

But this does not mean that the insurer should have priority over the assured's third party creditors. An insolvent assured cannot assert priority over her general creditors, and to say that subrogation gives an insurer priority over those same creditors is to give the insurer greater rights than the assured ever had.

Lord Templeman has indicated that the unjust factor will often be the ability to contract out of the risk of insolvency. Hence, in *Lord Napier & Ettrick* his Lordship stated that:⁵⁶

The stop loss insurers will be in a worse position than an unsecured creditor because the insurers could not resist payment under the policy whereas an unsecured creditor may choose whether to advance moneys or not.

And in *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Co (Bahamas) Ltd* his Lordship,⁵⁷ in an obiter statement, justified granting an equitable lien to beneficiaries tracing funds into the hands of an insolvent bank trustee. He stated that a settlor and beneficiaries, unlike a bank's customers and unsecured creditors, did not voluntarily accept the risk of the bank's insolvency. With respect, this fails to recognise that the pool of unsecured creditors may include employees,⁵⁸ suppliers,

54 This analysis reflects an attitude that the courts should not give one party the ability to gain priority over another's general creditors, unless the parties agreed to or intended this outcome.

55 (1883) 11 QBD 380, 388.

56 Above n 13.

57 *Space Investments Ltd v Canadian Imperial Bank of Commerce Trust Co (Bahamas) Ltd* [1986] 1 WLR 1072, 1074 (PC).

58 For wages in excess of \$1,500; see s 104 Insolvency Act 1967.

service providers and judgment creditors. It is doubtful whether these people could have contracted out of the insured's insolvency. Indeed, in the case of judgment creditors, a victim of the insured's wrongdoing should at least be viewed on an equal footing with the insurer. Alternatively, it could be said that insurers have the opportunity to avoid bearing the risk of the insured's insolvency. Like many commercial creditors, the basis of the insurer's relationship with the insured is contractual. But the types of plaintiff that Lord Templeman cites as not having taken the risk of the defendant's insolvency were those parties who could show a vitiated intention or an agreement that gave the plaintiff equitable title. An insurer has the same contractual opportunities as other creditors. If a court is going to award insurers priority over those other creditors, insurers must show that they did not agree to take the risk of the insured's insolvency.

VII THE INSURER'S ABILITY TO AVOID THE RISK OF THE INSURED'S INSOLVENCY BY STATUTORY AND EQUITABLE ASSIGNMENT

A Contractual Subrogation Clauses

Many insurers seek to refine and modify the parties' subrogation rights by the inclusion of subrogation clauses in the indemnity contract. This is not discouraged by the courts, for as James LJ said in *Morris v Ford Motor Co Ltd*.⁵⁹

It is open to the parties to a contract of indemnity to contract on the terms of their choice, and by the terms they choose they can exclude rights which would otherwise attach to the contract.

Like many obligations that are created by the operation of the law, it is thought that if the parties freely choose to alter or ignore those obligations, then the court will only interfere if the contract is ambiguous or does not address the matter.⁶⁰ However, it has been argued that the above general rule is affected by the different possible origins of subrogation. If the origin of subrogation is an implied contractual term, then the mere fact that the parties have provided an express clause may be enough for an argument that the parties' obligations are strictly confined to those provided in the contract.⁶¹ But Derham suggests that:⁶²

Once it is accepted that subrogation is an equitable doctrine, it should follow that the equitable rights and duties normally attaching to it should still be operative unless there is some inconsistency with the express clause. Therefore any unambiguous express term contained in the clause will be given effect. However, if the clause is ambiguous on certain points, reference may be made to the general principles of subrogation as an aid to construction, and if it is clear that these principles have not been excluded, they will still apply.

59 [1973] 1 QB 792, 812.

60 *Lucus v Exports Credit Guarantee Department* [1974] 1 WLR 909.

61 See J Birds *Modern Insurance Law* (3ed, Sweet & Maxwell, London, 1993) 289; "Contractual Subrogation in Insurance" [1979] JBL 124.

62 SR Derham *Subrogation in Insurance Law*, above n 19, Chap 13, 144.

The question that must also be considered is "When do these clauses become subject to the rules concerning the assignment of choses in action?" This question lies at the heart of the difference between subrogation and assignment or abandonment. Traditional subrogation places obligations on the insured to protect the interests of the insurer. But it never removes ownership of the chose in action from the insured. Thus, an insured is obliged to assist the insurer's action against a liable third party, or even to reimburse the insurer if the third party compensates the insured for her loss. But the insurer cannot stop the insured from using the chose in action against the third party, or from claiming her total loss when she has been partially indemnified.⁶³ An assignment or an equitable agreement to assign, represents the transfer of ownership rights in the chose in action. Thus, an assignee could refuse to enforce her portion of the chose in action; she could benefit from any increase in the value of her portion of the chose in action; and as equity views the subject of an agreement to assign as owned by the assignee from the moment it comes into existence, any benefit received by the assignor from that chose in action will belong to the assignee.⁶⁴ Given the above distinctions, if the subrogation clause goes as far as giving ownership rights or powers to the insurer, then the clause should be seen as an actual or attempted assignment of future property and the benefits of that property.⁶⁵

B Statutory and General Assignment

The common law has not traditionally recognised general assignments of future property⁶⁶ or the bare right to sue. This was due to conceptual difficulty with the notion of transferring property that did not exist, and the courts refusal to condone maintenance or champerty.⁶⁷ Derham defines maintenance as: the promotion or support of contentious legal proceedings, in the absence of justifying circumstances, by a stranger who has no direct concern in them.⁶⁸ Thus, Derham concludes that the role of insurance in modern society makes it highly unlikely that an indemnity insurer will be viewed as lacking a legitimate interest or concern in the proceedings.⁶⁹ If Derham is

63 *Arthur Barnett Ltd v National Insurance Co of NZ Ltd* [1965] NZLR 874, per McCarthy J at 885.

64 *Halsbury's Laws of England* (4th ed, Butterworths, London, 1991) Vol 6, Choses In Action, Para 32; *Tailby v Official Receiver* (1888) 13 AC 523; *Re Brooks' Settlement Trusts*, *Lloyds Bank Ltd v Tillard* [1939] Ch 993; *Re Gillott's Settlement*, *Chattock v Reid* [1934] Ch 97; *Re Lind, Industrial Finance Syndicate Ltd v Lind* [1915] 2 Ch 345.

65 For an alternative discussion of the relationship between assignment and "express subrogation clauses", see SR Derham *Subrogation in Insurance Law*, above n 19, Chap 13, 144.

66 *Holroyd v Marshall* (1862) 10 HLC 191, 210; 11 ER 999, 1006.

67 See AG Guest (ed) *Chitty on Contracts* (26ed, Sweet & Maxwell, London, 1989) Vol 1, Chap 19; GH Treitel *The Law of Contract* (8ed, Sweet & Maxwell, London, 1991) Chap 16.

68 Champerty is seen as an extreme version of maintenance. The offences of maintenance and champerty have been abolished.

69 SR Derham *Subrogation in Insurance Law*, above n 19, Chap 10, 112. However, this argument is not sustainable for non-indemnity insurance; Chap 13, 149.

correct, then it is possible for the insured to assign a chose in action to an insurer, as long as the chose in action is in existence at the time of assignment.⁷⁰

Following section 130 of the Property Law Act 1952, the three requirements for a valid statutory assignment are: (i) it must be absolute; (ii) it must be written; (iii) written notice must be given to the debtor.

Thus, for insurers to have a statutory assignment of the insured's chose in action, the insured must assign to the insurer the entire chose of action against the wrongful third party. This would be in return for being indemnified for the insured loss. This enables the insurer to take legal proceedings in its own name and retain the entire proceeds of the chose in action, even if the proceeds exceed the insurer's payment to the insured. Like abandonment, statutory assignment would give the insurer complete ownership of the chose in action and its benefits. The practical issue for insurance companies is whether an insured, who has not been indemnified for her total loss, will be willing to assign the entire chose in action. Such a step would require the insured to agree to bear the unindemnified loss completely, and forego the opportunity of recovering compensation from the liable third party. Depending on the size of the excess or uninsured loss, it is likely that many consumers would refuse to give absolute assignments of the chose in action, unless the insurer met their total loss. Indeed, following the traditional rules of subrogation the insurer should not gain more than what it paid the insured. Thus, in situations of partial compensation the insured should retain the right to as much of the chose in action as is necessary to meet the total loss. But statutory assignments may avoid this result and provide the insurer with a windfall.

It is also possible for insureds to assign only a portion of their choses in action to their insurers.⁷¹ Such an assignment is recognised in equity, which could be called upon to enforce the assignor's (insured) obligation to the assignee (insurer). This would enable the insurer to take legal proceedings in its own name, but the insured (who retains an interest in the action) must be joined as a co-plaintiff or a co-defendant. If the insured also wished to enforce a claim against the defendant, the insured would be a co-plaintiff. But if the insured did not want to enforce her portion of the chose in action, the insurer would call for the insured to be joined as a co-defendant. Equity would require the presence of the insured (assignor) for two reasons:⁷²

[Firstly], the assignor might retain some interest in the debt, *e.g.* he might only assign part of it: in such a case, it was desirable to have him before the court, so that the relative rights of all the parties could be determined in a single action. [Secondly], the assignor might wish to dispute the validity of the assignment: this possibility again made it desirable to have him before the court at some stage.

70 For discussions of this possibility, see *King v Victoria Insurance Co Ltd* [1986] 2 AC 250; *Compania Colombiana de Seguros v Pacific Steam Navigation Co* [1965] 1 QB 101; and *Trendtex Trading Corp v Credit Suisse* [1980] QB 629.

71 See AG Guest (ed) *Chitty on Contracts* above n 67, 1398; GH Treitel *The Law of Contract* above n 67, 581.

72 GH Treitel *The Law of Contract* above n 67, 578.

This separation of the interested parties may be preferable, compared to subrogation which allows the insurer to sue in the name of the insured. It could be said that subrogation allows the insurer to hide behind the insured. It has also been seen as one of the major benefits of the subrogation doctrine.⁷³

Given that the chose in action needs to be in existence at the time of the assignment, the insurer will probably seek an assignment on payment of the insured's claim. Thus, when an insured receives compensation from the insurer, the receipt documents may attempt to assign the insurer the insured's chose in action against a liable third party. But if the assignment is for a portion of the chose in action, then caution is necessary to avoid the agreement being classified as an attempt to assign future property.⁷⁴ In *Williams v Commissioner of Inland Revenue*⁷⁵ the New Zealand Court of Appeal considered whether a deed which purported to assign "the first £500 of the net income which shall accrue to the assignor" was a valid assignment of an existing interest, or an agreement to assign future property. The court found the deed to be an attempt to assign future property, and thus invalid for lack of consideration. In the joint decision of North P and Turner J it was stated that -⁷⁶

We do not doubt that where it is possible to assign a right completely it is possible to assign an undivided interest in it. The learned Solicitor-General was therefore right, in our opinion, in conceding that if here, instead of purporting to assign "the first £500 of income", the assignor had purported to assign (say) an undivided one-fourth share in his life estate, then he would have assigned an existing right, and in the circumstances effectively.

However, the decision should not be read as allowing proportions only in the form of percentages or fractions. If such measures were used, the assignee could receive more than what was originally intended, ie "one-fourth" of the income could be more than £500. If assigning a chose in action, it should be possible to place a limit on the amount the assignee receives from that chose in action, by specifying a limit on the amount the assignee can claim in damages from the defendant. Thus, if an insured suffers \$200 total loss, and the insurer indemnifies the insured for \$125 of that loss, then the insured should be able to assign the insurer the right to sue the defendant for \$125. As long as the assignment does everything necessary to transfer a specific portion of the right to claim the damages, and not the damages themselves as after-acquired property, then the assignment should be enforceable.⁷⁷ An assignment of this nature would not suffer from the same problems as the "first £500 of the net income

73 See SR Derham *Subrogation in Insurance Law*, above n 19, Chap 6. Derham concludes that there is no compelling reason to change this rule.

74 See AG Guest (ed) *Chitty on Contracts* above n 67, 1404, 1409.

75 [1965] NZLR 395.

76 Above n 75, 399.

77 See *Shepherd v Federal Commissioner of Taxation* (1965) 113 CLR 385; and *In re McArdle* [1951] Ch 669, where the court acknowledges the possibility of an assignment of part of a debt. The writer has been unable to find any direct authority that dealt with an assignment of a right to a specific sum as opposed to a proportional measure.

which shall accrue to the assignor" because, unlike the "income which shall accrue to the assignor", the insured's ability to claim \$125 damages exists at the time of assignment. The uncertainty only lies in whether the court will grant damages in that amount. As Kitto J said in *Shepherd v Federal Commissioner of Taxation*:⁷⁸

The tree, though not the fruit, existed at the date of the assignment as a proprietary right of the [assignee] of which he was competent to dispose; and he assigned ninety per centum of the tree. The case is of the general class of which *Brice v Bannister*⁷⁹ is an example, and may be usefully compared with *Bergmann v Macmillan*⁸⁰ and *Hughes v Pump House Hotel Company Ltd.*⁸¹

Under subrogation the insurer would not be entitled to any more than the amount of indemnity that the insured received. Hence, if the legal proceedings resulted in the insurer receiving, from the defendant, more than what the insurer had paid to the insured, the insurer was presumed to be under an obligation to give the excess money to the insured. But in reality, it is doubtful whether there is sufficient incentive for insurers to protect the insured's smaller claim, and resist settling for only the amount the insurer has lost. If the insured assigns to the insurer a set interest in the chose in action, the responsibility of protecting the insured's retained portion of the claim is left with the insured.

C Assignment of Future Choses in Action

Equity can be used to enforce such attempts by calling them "agreements to assign property in the future", and invoking the maxim that equity considers done that which ought to be done.⁸² But for the court to enforce the assignor's obligation, the assignee must show that consideration for the future property had been given. Thus, a creditor who took assignment of the proceeds of a slander action, had to establish that his forbearance from enforcing the assignor's debt and the provision of additional funds for the cost of the slander action, were sufficient consideration for the assignor's promise to transfer any damages resulting from the legal action.⁸³ This requirement of consideration was also mentioned by the Court of Appeal in *Williams v CIR*:⁸⁴

But while equity will recognise a voluntary assignment of an existing equitable interest, it will refuse to recognise in favour of a volunteer an assignment of an interest, either legal or equitable, not existing at the date of the assignment, but to arise in the future. Not yet existing, such property cannot be owned, and what may not be owned may not be effectively assigned. If, not effectively assigned, it is made the subject of an agreement to assign it, such an agreement may be good in equity, and

78 Above n 77, 396.

79 (1878) 3 QBD 569.

80 (1881) 17 Ch D 423.

81 [1902] 2 KB 190.

82 See AG Guest (ed) *Chitty on Contracts* above n 67, 1395; GH Treitel *The Law of Contract* above n 67, 586.

83 *Glegg v Bromley* [1912] 3 KB 474.

84 Above n 75, 399.

become effective upon the property coming into existence but if, and only if, the agreement is made for consideration,⁸⁵ for equity will not assist a volunteer.⁸⁶

However, if this consideration requirement is combined with the typical insurance situation, the result is that an insurer seeking the assignment of future choses in action (or the future benefits of a chose in action) must make that agreement to assign at the initial formation of the insurance contract. This is different from the situation of the insurer who could take an assignment of a particular chose in action upon indemnifying the insured, because consideration is not required for the assignment of existing property. This difference is due to the inability of the insurer to show that, at the stage of indemnifying the insured who has suffered a covered loss, the insurer has done more than what she was originally bound to do. If an insurer indemnifies an insured because the insured has suffered a loss that comes within the terms of the indemnity cover, the insurer has not given consideration for the added benefit of the proceeds of the insured's chose in action against a third party. This should not be perceived as an insurmountable difficulty for the insurer. The insurer simply needs to create the agreement to assign future choses in action at the formation of the insurance contract with the insured. Thus, when an insurer indemnifies the insured for a covered loss, the insurer can enforce the insured's equitable obligation to assign the appropriate chose in action to the insurer. If this is done, the insurer will be entitled to any benefits or court awards given in satisfaction of that chose in action. If the insured has received compensation from the liable third party before assigning the chose in action, it would be inequitable for the insured to retain benefits that should have been the insurer's.

D Summary

The issue is whether the insurer's right to damages received by the insured from a liable third party, should be an institutionalised proprietary right or simply left to the court's equitable discretion. The desire to make this an institutionalised right, and hence have a proprietary remedy in all claims to subrogated damages, is still present in some of the speeches delivered in *Lord Napier & Etrick*.⁸⁷ However, the writer suggests that this outcome is unlikely given the developments in the law of restitution. What exists instead is an equitable discretion which allows the court to view each situation and adjudge the quality of the different claimants. Hence, an insurer may well benefit from a proprietary remedy when the insured is solvent, but the insurer may be refused that same remedy if the insured is insolvent and the pool of unsecured creditors is affected. This choice may be seen as consistent with the policy of minimal court intervention in commerce in that it provides the insurer with the minimum rights necessary to fulfil the principle of indemnity. The courts will view each claim on its merits, and find the remedy that most adequately meets the indemnity principle's requirements, and does not cause any injustice in the particular circumstances.

85 *Spratt v Commissioner of Inland Revenue* [1964] NZLR 272.

86 *In re Ellenborough, Towry Law v Burne* [1903] 1 Ch 697.

87 See above, Part II D of this paper.

However, it may be argued that commerce needs certainty in the law: That insurers need to be sure as to what their rights are. Indeed, Sir Peter Millett argues that -⁸⁸

It is a counsel of despair which too readily concedes the impossibility of propounding a general rationale for the availability of a proprietary remedy. The advantage which such a remedy affords the plaintiff over the unsecured creditors of an insolvent defendant makes it imperative that the circumstances in which it will be granted should be known in advance.

An institutionalised proprietary interest would be consistent with this as it could be asserted at any time.

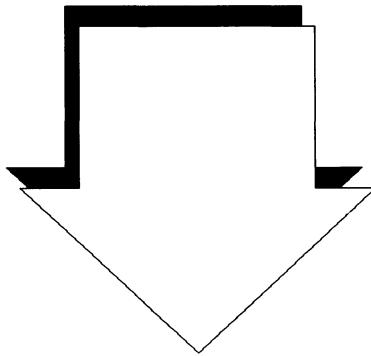
The reply to this is that the insurers are free to contract out of the common law, and hence they are able to secure any extra proprietary rights they desire. As has been seen, it is possible for the insurer to take assignments of choses in action, or to make agreements to assign future choses in action and any damages awarded by the court. It is also relevant that, like abandonment and the rules concerning *dominus litis*, statutory assignment is unlikely to give complete ownership of the chose in action unless the insurer compensates the insured's total loss. Statutory and equitable assignments can achieve the same results as traditional subrogation, while providing the parties with certainty of outcome and ownership. Assignment may also result in the parties being able to be viewed independently, with complete control over their portion of the chose in action.⁸⁹ Another benefit of a contractual approach is that the parties negotiate and agree on what rights are to be transferred to the insurer. This should be seen as more desirable than courts formulating and creating rights which apply automatically to all insurance contracts, regardless of what the parties may desire. Given the probable judicial discretion in the award of proprietary remedies, insurers cannot assume that the court's conception of justice will necessarily lead to a proprietary remedy. If such a remedy is desired they should use statutory and equitable assignments to secure legal or beneficial ownership of any damages the insured may receive from a liable third party.

88 P Millett "Bribes and Secret Commissions" [1993] Restitution Law Review 7, 9.

89 For an illustration of the possible benefits of viewing the insured and the insurer independently, in situations of partial indemnity, see PT Rishworth "Insurance Law" [1989] NZ Recent Law Review 152.

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