THE EQUITABLE LIEN: NEW LIFE IN AN OLD REMEDY?

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1. Introduction

The remedy of an equitable lien is of historic origin, stemming from the Courts of Chancery in the early 1800s. For much of this century the remedy has been applied on an infrequent basis and primarily to enforce unpaid vendors' liens.

The remedy seems to have been given new life, however, as it has been considered within a modern commercial context in two fairly recent decisions. In 1982 the English Court of Appeal considered the nature of an equitable lien at some length in *Swiss Bank Corp* v. *Lloyds Bank Ltd.*,[1] a decision subsequently upheld by the House of Lords. The New Zealand Court of Appeal has also considered the nature of an equitable lien within a commercial context in the 1974 case of *Waitomo Wools (N.Z.) Ltd.* v. *Nelson (N.Z.) Ltd.*[2]

In view of the new life given to equitable remedies, in general, by the Supreme Court of Canada in the recent decision of *LAC Minerals Ltd.* v. *International Corona Resources Ltd.*,[3] perhaps the remedy of an equitable lien should be reviewed so that practitioners may reflect on its modern utility. This article will commence with a general review of the remedy of an equitable lien, primarily within the context of a lien created by agreement as it is this type of lien which will ordinarily arise in a commercial context. It will then take a closer look at the two aforementioned leading decisions. American law with respect to equitable liens will be briefly reviewed, as the remedy has enjoyed a relatively robust application in American jurisprudence. The article will then briefly

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1 [1982] A.C. 584.

2 [1974] 1 N.Z.L.R. 484.

3 (1990), 61 D.L.R. (4^{th}) 14, [1989] 2 S.C.R. 574, 101 N.R. 239.

summarize the concomitant remedies available to enforce an equitable lien in order to illustrate its flexibility as a remedial tool.

Having reviewed the basic principles governing the remedy, the article will then turn to a consideration of the potential scope of the remedy in a modern commercial context and examine specific issues that arise as to how far the remedy can be pushed. The article will conclude with a brief discussion of a recent case considered by the Alberta courts which illustrates many of these issues.

2. Overview of the Remedy

(1) The Nature of an Equitable Lien

The terms "equitable lien" and "equitable charge" are frequently used synonymously. There is a difference, however. An equitable lien can arise in one of three ways: by the "course of conduct" of the parties, such that it is imposed by law upon them; by agreement of the parties and by virtue of a statute. A true "equitable lien" is the type imposed upon the parties; it "arises by operation of equity from the relationship of the parties",[4] e.g., an unpaid vendor's equitable lien. An "equitable charge", on the other hand, is the type that arises by agreement of the parties.

This distinction is made clear in *Snell's Principles of Equity* in which the nature of an equitable lien is described as follows:[5]

> Equitable lien. An equitable lien is very different [from a legal lien]. It confers a charge upon property until certain claims are satisfied, and differs from an equitable charge only in that it arises by operation of equity from the relationship between the parties rather than by acts of theirs. It exists independently of possession . . . It is enforceable by means of an order for sale.

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4 *Snell's Principles of Equity*, P.V. Baker and P. St. J. Langan, eds., 29th ed. (London: Sweet & Maxwell Ltd., 1990), p. 456.

5 *Ibid*., p. 450.

The distinction between an "equitable lien" and an "equitable charge" is very seldom made, or perhaps more accurately, correctly made, in the case-law.

Although there is frequent confusion in the use of the terms "equitable lien" and "equitable charge" in the case-law, it is clear that, regardless of what it is called, an equitable lien is an interest in property.[6]

The most recent expression of the nature of an equitable charge is that of the English Court of Appeal in *Swiss Bank* in which Buckley L.J. stated:[7]

> An equitable charge . . . is said to be created when property is expressly or constructively made liable, or specially appropriated, to the discharge of a debt or some other obligation, and confers on the chargee a right of realization by judicial process, that is to say, by the appointment of a receiver or an order for sale.

There is a real distinction between a "legal lien" and an "equitable lien" in English and Canadian jurisprudence; this distinction is not made in American law. It is important to be aware of this distinction as much of the case-law deals with legal liens.

A legal lien, or "common law lien", is described in *Snell's*[8] as follows:

> Legal lien. A common law lien is the right of one person to retain possession of the goods of another until his claims are satisfied. It depends upon possession, and so lasts only as long as possession is retained . . .

In general, a legal lien gives the lienholder merely the right to retain the possession of the property until the lien obligation is satisfied; there is no right to sell the property. It does not create an interest in property. An equitable lien is thus significantly different in that it creates an interest in property and gives the lienholder the right to

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6 The root case for this principle is *Palmer* v. *Carey*, [1926] A.C. 703.
7 *Supra*, footnote 1, at p. 595.
8 *Supra*, footnote 4, p. 456.

enforce the lien by selling the property. An equitable lien can be said to be of possessory or proprietary origins, however (a theme which will be expanded on later in this article), as it has its origins in the common law legal lien.

An equitable mortgage is an interest in property and is different from an equitable lien in that it grants the mortgage the additional right to foreclose against the property. All equitable mortgages are equitable liens, but not all equitable liens are equitable mortgages. The distinction between the two is articulated by Buckley L.J. in *Swiss Bank*:[9]

> An equitable charge may, it is said, take the form either of an equitable mortgage or of an equitable charge not by way of mortgage. An equitable mortgage is created when the legal owner of the property constituting the security enters into some instrument or does some act which, though insufficient to confer a legal estate or title in the subject matter upon the mortgagee, nevertheless demonstrates a binding intention to create a security in favour of the mortgagee . . . An equitable charge which is not an equitable mortgage is said to be created when property is expressly or constructively made liable, or specially appropriated, to the discharge of a debt or some other obligation, and confers on the chargee a right of realization by judicial process, that is to say, by the appointment of a receiver or an order for sale.

The case-law is clear that there is no particular form of words necessary to create an equitable lien by agreement (that is, an equitable charge), as long as the intention of the parties to create such a lien is clear.

There is early Canadian authority for this principle. In the case of *Dundas (Town)* v. *Desjardins Canal Co.*[10] the company which constructed the canal, Great Western Railway Company, had borrowed significant sums from the government. It executed a bond in favour of the town which said that the town had “precedence and priority of lien” on the canal and its tolls. The sheriff was attempting to sell the canal under an execution

9 *Supra*, footnote 1, at pp. 594-5.
10 (1870), 17 Gr. 27.

and the town claimed priority as against the execution creditor. Mowat V.C., citing *Fisher on Mortgages* as authority, stated:[11]

> That they have a lien as against the company, I have no doubt. The bond shews beyond a question that the object of both parties was to give the plaintiffs a lien; and the rule in equity is, that no formal instrument is necessary for that purpose, and that any writing from which the intent appears, is sufficient.

The root authority for this principle is considered to be *National Provincial & Union Bank of England* v. *Charnley*, [12] a decision of the English Court of Appeal. In this case the Fylde Bacon Curing Company executed a mortgage in favour of the bank under which the company "demised" unto the bank its land and chattels. The registrar under the *Companies Act* failed to register the mortgage correctly, omitting mention of the charge on the chattels. Charnley, a subsequent execution creditor, had the sheriff seize the chattels. The bank claimed priority over the chattels pursuant to their mortgage and the court considered whether the mortgage document was sufficient to create a floating charge upon the chattels. Although each of the three justices writing decisions articulated the principle that the court will look to the intention of the parties to determine whether an equitable lien was created, the following passage of Atkin L.J. is the most frequently quoted:[13]

> It is not necessary to give a formal definition of a charge, but I think there can be no doubt that where in a transaction for value both parties evince an intention that property, existing or future, shall be made available as security for the payment of a debt, and that the creditor shall have a present right to have it made available, there is a charge . . .

Thus, case-law clearly holds that, in considering whether an equitable lien has been created by way of agreement, a court must look to the intention of the parties. *Swiss Bank* is authority for the further proposition, however, that if the agreement between the

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11 *Ibid.*, at p. 30.
12 [1924] 1 K.B. 431.
13 *Ibid.*, at pp. 449-50.

parties clearly creates a charge on the property to secure discharge of an obligation, an equitable lien will be found to have been created, even though the parties may not have turned their minds to the issue. The courts will look to the words used in the agreement and their legal effect and, if appropriate, will presume an intention to create an equitable lien.

(2) The Equitable Lien In a Modern Commercial Context

There are two relatively recent decisions which have considered the nature of an equitable lien, *Swiss Bank* and *Waitomo Wools*. Although in each case the application for a declaration of an equitable lien, and concomitant enforcement remedies, was ultimately unsuccessful, the cases are the leading authorities discussing this remedy within a modern commercial context.

The facts of *Swiss Bank* are very complicated. The plaintiff Swiss Bank Corporation entered into a written loan agreement whereby it agreed to loan Israel Financial Trust Ltd. 10.5 million Swiss francs in order that it could purchase shares in First International Bank of Israel ("F.I.B.I."). The loan transaction was governed by the English *Exchange Contract Act*, 1947, and thus required the consent of the Bank of England. In giving consent the Bank of England imposed several conditions, most important of which were that the borrower was to keep the F.I.B.I. shares in a separate account, to apply the income earned from the shares against the loan and to repay the loan from the proceeds of the shares.

The F.I.B.I. shares purchased with the loan were held in the name of an Israel Financial Trust Ltd. subsidiary, "Triumph". Triumph subsequently experienced financial difficulties and had to borrow monies from the defendant Lloyds Bank. As security for the loan from Lloyds, Triumph granted a charge over the F.I.B.I. shares to Lloyds. The Swiss Bank Corporation then demanded repayment of its loan. Israel Financial Trust Ltd. could not repay the loan and Swiss Bank therefore claimed an equitable charge as against the F.I.B.I. shares. The issue before the court was whether the loan agreement, which incorporated the conditions imposed by the Bank of England, created an equitable charge.

The trial judge, Browne-Wilkinson J., held that an equitable charge was created in favour of Swiss Bank and that this charge took priority over the charge of Lloyds Bank. He therefore declared Swiss Bank entitled to the proceeds of sale of the F.I.B.I. shares and declared the Lloyds' charge void.

The matter was appealed to the English Court of Appeal and the decision of Buckley L.J. in considering this appeal is the leading modern authority on equitable liens. Buckley L.J. initially distinguished between an equitable mortgage and "equitable charge not by way of mortgage"[14] and went on to describe the nature of an equitable charge as follows:[15]

> An equitable charge . . . is said to be created when property is expressly or constructively made liable, or specially appropriated, to the discharge of a debt or some other obligation, and confers on the chargee a right of realization by judicial process, that is to say, by the appointment of a receiver or an order for sale . . .
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> It follows that whether a particular transaction gives rise to an equitable charge of this nature must depend upon the intention of the parties ascertained from what they have done in the then existing circumstances. The intention may be expressed or it may be inferred. If the debtor undertakes to segregate a particular fund or asset and to pay the debt out of that fund or asset, the inference may be drawn, in the absence of any contra indication, that the parties' intention is that the creditor should have such a proprietary interest in the segregated fund or asset as will enable him to realize out of it the amount owed to him by the debtor . . .

After examining the loan transaction in detail, Buckley L.J. held that it did not give rise to an equitable charge and thus allowed the appeal. Key in his consideration was that there was "no obligation to repay the loan out of the fruits of the borrowing in

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14 *Supra*, footnote 1, at p. 594.
15 *Ibid*., at pp. 595.

any event",[16] and thus there was no specifically enforceable right to have the loan repaid out of the F.I.B.I. shares. The decision of Buckley L.J. was upheld by the House of Lords. Lord Wilberforce stated: "I do not doubt the correctness of the principles of law … which were stated by the learned judge".[17]

Waitomo Wools is the leading authority discussing an equitable lien that is expressly created pursuant to a contract of the parties; it refers to a "contractual equitable lien". In this case Nelson "scoured" wool for Waitomo Wools and under their contract it was expressly agreed:

> 12. Lien. All wool whether greasy or scoured held by the Scourers for the account of a client may be retained as security for the payments of all sums which are or will be due by the said Client; this lien does not cease by the transfer of the wool to another owner.

Waitomo Wools went into receivership. As it owed a significant amount to Nelson for its scouring services, Nelson claimed a lien over the bales of wool that it still had in its possession as against the receiver.

The New Zealand Court of Appeal held that, as the lien had been expressed in a contract, it was "purely contractual in nature" and its extent and the remedies available pursuant to it depended "solely upon the proper construction of language" of the lien. Richmond J. stated:[18]

> In accordance with ordinary principles of construction this language should be given effect according to its ordinary and natural meaning unless some good and sufficient justification can be found to depart from that meaning.

An issue was raised as to whether the lien was a "general lien", i.e., whether it extended to cover fees owing to Nelson for the scouring of wool in the past. The court

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16 *Ibid*., at p. 597.
17 *Ibid*., at p. 613.
18 *Supra*, footnote 2, at p. 487.

held that, notwithstanding early English authority that "general liens are looked on with disfavour as being an encroachment upon the common law", the court should give effect to language which clearly created a general lien. The court then considered whether the contract created a mere "legal possessory lien" or whether it created an equitable lien. The distinction was important in that the relevant *Companies Act* required a "charge" to be registered; failure to register would render it void. A mere legal lien, however, not being a "charge", would not be void for failure to register under the Act. The court therefore went into a detailed review of the difference between legal liens and equitable liens. In the result the court held that the contract did not expressly create a charge against the property, and thus was not an equitable lien, but merely a "legal possessory lien"; it therefore survived failure to register under the *Companies Act*.

In discussing the difference between a legal lien and an equitable lien Richmond J. adopted the distinction set out in Snell's. He implicitly equated a "charge" with an equitable lien and expanded on the definition of a "charge" as follows:[19]

> As such I think that in its ordinary and generally accepted meaning the word "charge" is apt only to describe a situation in which some particular property, real or personal, is appropriated or set aside in favour of someone who is given by law, or by agreement, will or otherwise, the right to resort to the property to satisfy or discharge some obligation . . . A charge involves some deduction from the right of ownership in the property rather than a mere interference with the right to possession which is normally an incident of ownership . . .
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> The most essential distinction is that a true possessory lien depends entirely on possession and is lost with the loss of possession. A charge, on the other hand, exists independently of possession and confers an interest in the property which carries with it a right to resort to the property (as opposed to merely detaining it) to satisfy or discharge some obligation secured by the charge.

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19 *Ibid*., at p. 488.

(3) American Treatment of Equitable Liens

American law with respect to equitable liens has been derived from English law. There is only one significant difference between the Anglo-Canadian and American view of equitable liens. In Anglo-Canadian law an equitable lien is considered to be an interest in property; American law holds that an equitable lien is not an interest in property but merely a right to have the property subjected to the payment of a debt or claim,[20] and thus a "mere floating equity".[21] An equitable lien in American law can arise from an express agreement of the parties or can be implied or declared by a court of equity "out of general considerations of right and justice as applied to the relations of the parties and the circumstances of their dealings".[22] American law refers to both types as equitable liens; there is no distinction made between "equitable liens" and "equitable charges".

The doctrine of equitable liens "is clearly an application of the maxim equity regards as done that which out to be done".[23] An equitable lien "arises at the time of the transaction from which it springs" and has priority over all claims except those of *bona fide* purchasers for value without notice or subsequent valid lien holders without notice.[24]

In assessing whether an equitable lien has been created by agreement of the parties, the American courts also look to the intention of the parties; no particular form is required to create an equitable lien if the intent is clear. Although most cases deal with equitable liens that secure debt, an equitable lien can also secure an "obligation".[25]

It is also clear in American law that even though a remedy may be available at law, an equitable lien may none the less be granted. "Existence of a remedy at law does not deprive equity of jurisdiction unless such remedy is clear, adequate and complete, and

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20 *Consolidated Oil Wells Services Inc* v. *State Oil Co.*, 747 P. 2d 183 (Kan. App., 1987).
21 *Loamis* v. *Priest*, 274 F. 2d 513 (U.S. Ct. Apps., 1960).
22 *Farmers & Merchants Bank* v. *Commissioner of Int. Rev.*, 175 F. 2d 846 (U.S. Ct. Apps., 1949).
23 *Syring* v. *Sartorious*, 277 N.E. 2d 457 (Ohio App., 1971).
24 *Blumin* v. *Ellis*, 186 So. 2d 286 (Fla. App., 1966).
25 *Supra*, footnote 20.

such remedy at law must be equally complete, efficient, practical and prompt with the remedy in equity . . ."[26]

The equitable lien is not as "historic" a remedy in American law as it is in Anglo-Canadian jurisprudence. Rather, the equitable lien has been applied on a frequent basis since its adoption near the turn of the century[27] and is frequently utilized within a modern commercial context.

(4) Enforcement of the Lien

The essence of an equitable lien is that it conveys a right to resort to the property to discharge the obligations secured by the lien. The traditional methods of enforcing the lien are to have the property sold and to have a receiver appointed to receive the revenues of the property to be applied towards satisfaction of the obligation.[28]

These enforcement remedies have been recently confirmed in *Swiss Bank*, in which Buckley L.J. stated that an equitable charge "confers on the chargee a right of realization by judicial process, that is to say, by the appointment of a receiver or an order for sale".[29]

The early Canadian case of *Dundas (Town)* v. *Desjardins Canal Co*.[30] illustrates that an equitable lien can be enforced through a variety of means. In this case, in which an equitable lien was found in favour of the town as against the canal and its tolls, the court granted the following:

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26 *Hill* v. *Hill*, 345 P. 2d 1015 (Kan., 1959).

27 *Ketchum* v.*St. Louis*, 101 U.S. 306 (S.C., 1879).

28 *Hope* v. *Booth* (1830), 1 B. & Ad. 498, 109 E.R. 872; *Munns* v. *Isle of Wight Railway Co.* (1870), 5 Ch. App. 414.

29 *Supra*, footnote 1, at p. 595.

30 *Supra*, footnote 10.

- a declaration of the lien as against the canal and its tolls;
- an injunction prohibiting the sale of the canal;
- an accounting of "What was due under the lien"; and
- appointment of a receiver to receive the tolls and other revenues to be applied toward satisfaction of the lien.

There is also authority that liened property can be recovered "in specie". In *Hastie* v. *Hastie*,[31] an early decision of the Chancery Court, a "lady of fortune" entered into a marriage settlement whereby, although the husband was granted the right to deal with the bulk of her estate, certain stocks were reserved unto her. The husband squandered most of her estate and got hold of the stocks, which he transferred to a bank. The court declared an equitable lien in favour of the wife as against her property that was still in the possession of the husband in order to "make good the equivalent of that which he bargained to allow to be settled upon her".[32]

3. The Scope of the Remedy in a Modern Commercial Context

As previously noted, the remedy of an equitable lien is of historic origin and has been considered by the courts infrequently and generally within a limited context. The potential scope of the remedy in a modern commercial context is therefore little understood. Although many interesting issues arise as to its modern utility, the dearth of jurisprudence results in many questions and few answers. None the less, in the absence of clear answers, I will explore some of the issues raised.

(1) The Extent of the "Obligations" that Can be Secured

Although the case-law generally deals with equitable liens created to secure the discharge of a debt, it is also clear that an equitable lien can be given to secure the discharge of another type of obligation.

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31 (1876), 2 Ch. D. 304.
32 *Supra*, footnote 4, at p. 450.

In defining an equitable lien, *Snell's* states that: "it confers a charge upon property until certain claims are satisfied".[33]

The principle that an equitable lien can secure an "obligation" is illustrated by the case of *Uziell-Hamilton* v. *Keen*,[34] a decision of the Chancery Division. In this case a retiring solicitor agreed to sell his practice to another. The written agreement provided for a purchase price, which was paid, and further provided in cl. 8 that the purchaser would use his best efforts to collect any monies owing to the retiring solicitor. Presumably this clause was included because the purchasing solicitor was taking over work in progress which could not be billed until sometime after the closing date. The purchaser further agreed to allow the retiring solicitor free access to the accounting books and other documents in order to ascertain what debts should have been collected and paid over to him.

A dispute arose as to the amount of money that should have been collected by the purchaser as owing to the retiring solicitor and the matter was referred to arbitration. The arbitrator concluded that approximately £7,000 were owing. As this amount was not paid, the retiring solicitor registered a general equitable charge against the leases of the office premises sold as part of the practice; the purchaser applied to the court to vacate this charge. Although the agreement "contained no words of charge at all", the retiring solicitor submitted to the court "that the court could properly infer from the agreement that it was intended that there should be a charge against the leases in respect of the performance of obligations by the purchaser under the agreement which were outside the cash sum paid over".[35]

Whitford J. held that the equitable lien was validly registered, primarily on the basis that it was an unpaid vendor's equitable lien. He further stated:[36]

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33 *Supra*, footnote 2, at p. 490.
34 (1971), 22 P. & C.R. 655.
35 *Ibid*., at p. 658.
36 *Ibid*., at p. 660.

> I have to consider the agreement as a whole, and I think, on the true construction of the agreement, it was the intention of the parties that the sale transaction should be subject, not only to the payment of £5,000, but to the observance by the purchaser of his obligations under, inter alia, clause 8 of the agreement, and that, in these circumstances the lien should prevail.
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> Having reached that conclusion, it is not necessary to deal with the second point relied on by counsel for the vendor, namely that even if I were not in his favour on the argument in relation to an unpaid vendor's lien, nevertheless the lease constituted a security for the performance by the purchaser of the obligations contained, in particular, in clause 8 . . . If it had been necessary to do so, I would, in any event, have concluded that one can infer from the agreement that it was the intention of the parties that here there should be a lien against the property that must subsist as a security for the due performance of the obligations of the purchaser under clause 8.

Although this case clearly illustrates the principle that an equitable lien can secure an obligation other than the discharge of a debt, as a result of the dearth of case-law in this area the scope of the types of obligation that can be secured does not appear to be clear. Even American jurisprudence which, because of its sheer volume, can usually be counted on to suggest an answer, does not appear to assist with this issue. *Uziell-Hamilton*, however, seems to be clear authority that the remedy of an equitable lien can be extended to charge property to secure the performance of contractual obligations in general. Such an extension would give the remedy a great deal of utility in a modern commercial context.

(2) Must the Remedy be Tied to a Proprietary Interest in Specific Property?

Another interesting issue which arises is whether the courts will give effect to an equitable lien only when, in the case of an equitable charge, specific property is found to have been charged to secure an obligation[37] or only when, in the case of a true equitable lien, the courts can find some "proprietary" roots to the claim which can be traced to the

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[37] The author recognizes, of course, that an equitable charge can be given to secure then-undefined or future property, in the nature of a floating charge (*Tailly* v. *Official Receiver* (1888), 13 App. Cas. 523), and uses the term "specific property" in the sense of being ascertainable or identifiable.

assets against which the lien claim is asserted. Is the remedy tied in this manner to specific property? Or, having found an intention of the parties to create lien rights without reference to any specific property, or upon a finding that an equitable lien should be imposed by operation of law because "justice and good conscience so require",[38] will the courts grant an equitable lien against such property of the obligator as can then be ascertained? This issue essentially raises the question of how far the courts will push the remedy of an equitable lien beyond its proprietary origins.

The case-law seems to suggest that, at least with respect to equitable charges, the charge must be secured against specific property. Thus, Buckley L.J. defined an equitable charge in *Swiss Bank*[38a] as "created when property is expressly or constructively made liable or specifically appropriated" to the discharge of an obligation. He further found on the facts of the loan transaction in question that an equitable charge had not been created as against the F.I.B.I. shares primarily because there was no specifically enforceable right granted to have the loan repaid out of the F.I.B.I. shares. Further, Richmond J. in *Waitomo Wools* defined a charge as "apt only to describe a situation in which some particular property real or personal, is appropriated or set aside" to secure an obligation.

This may not be the situation for a true equitable lien, however. Goff and Jones have suggested that, in their view, equitable liens are imposed by operation of law primarily to redress situations of unjust enrichment. As such, the courts should feel free to grant an equitable lien against such assets of the defendant as can then be ascertained, notwithstanding the inability of the lien claimant to point to a proprietary origin to the claim or to trace the claim to identifiable assets, where it is "just and equitable" to do so.[39]

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[38] *Hussey* v. *Palmer*, [1972] 1 W.L.R. 1286, *per* Lord Denning M.R. at p. 1290.

[38a] *Supra*, footnote 1.

[39] Lord Goff of Chieveley and Gareth Jones, *The Law of Restitution*, 3rd ed. (London: Sweet & Maxwell, 1986), pp. 60-3, 78-80.

This viewpoint has recently been discussed by David M. Paciocco within the context of the equitable remedy of the constructive trust:[40]

> Goff and Jones have pointed out that there is a difference between a "pure proprietary claim", where the plaintiff's call on the conscience of equity is that the defendant has property that was, as a matter of title, his own, and a "restitutionary proprietary claim", in which the plaintiff suggests that, as a matter of equity, the property should be considered to be his. Where a plaintiff is asserting a pure proprietary claim, the proprietary interest justification is compelling. The existence of a proprietary interest arising from a remedial constructive trust, on the other hand, is not an independent fact from which legal significance can be culled; the decision to give a plaintiff a proprietary interest is itself based on the conviction that it is fair or appropriate to do so. Consequently, in the context of the remedial constructive trust, the view that the existence of a proprietary interest justifies the beneficiary's priority does no more than beg the question as to what it is that makes giving the beneficiary a proprietary interest appropriate in the first place.

Although the issue of whether the remedy of an equitable lien need be tied to a proprietary interest in specific property does not appear to have been squarely addressed by an English or Canadian court, the Privy Council decision of *Space Investments Ltd.* v. *Canadian Imperial Bank of Commerce Trust Co. (Bahamas) Ltd*.[41] and the subsequent English Court of Appeal case of *Guinness Plc* v. *Saunders*[42] suggests that, at least in the English courts, the view of Goff and Jones may well prevail. In *Space Investments*, Mercantile Bank and Trust Co. Ltd. ("M.B.T."), as trustees deposited monies in favour of M.B.T. as bankers pursuant to a broad trust instrument. The bank became insolvent and the issue before the courts was whether the liquidator, in winding up the bank, was obliged to pay the trust deposit accounts in priority to the general bank customers' deposit accounts and the debts owed to other unsecured creditors. Lord Templeman, writing for the Privy Council, stated that, as a general principle, a trustee may only apply trust money as authorized by the trust instrument and that, if the trustee commits a breach of trust, the beneficiaries, in addition to other remedies, "possess the equitable remedy of

40 David M. Paciocco, "The Remedial Constructive Trust: A Principled Basis for Priorities Over Creditors" (1989), 68 Can. Bar Rev. 315 at p. 323.

41 [1986] 3 All E.R. 75.

42 [1988] 2 All E.R. 940, aff'd on other grounds [1990] 2 A.C. 663 (H.L.).

tracing the trust money to any property into which it has been converted . . .".[43] He characterized this remedy as an equitable charge as follows:[44]

> A bank in fact uses all deposit monies for the general purposes of the bank. Whether a bank trustee lawfully receives deposits or wrongly treats trust money as on deposit from trusts, all the monies are in fact dealt with and expended by the bank for the general purposes of the bank. *In these circumstances it is impossible for the beneficiaries interested in trust money misappropriated from their trust to trace their money to any particular asset belonging to the trustee bank. But equity allows the beneficiaries . . . to trace the trust money to all the assets of the bank and to recover the trust money by the exercise of an equitable charge over all the assets of the bank* . . .It is therefore equitable that where the trustee bank has unlawfully misappropriated trust money by treating the trust money as though it belonged to the bank beneficially, merely acknowledging and recording the amount in trust deposit account with the bank, then the claims of the beneficiaries *should be paid in full out of the assets of the trustee bank* in priority to the claims of the customers and other unsecured creditors of the bank . . . .[Emphasis added.]

Thus the Privy Council was prepared, in principle, to grant an equitable lien against all of the assets of the bank. The dicta of Lord Templeman can arguably be read as authority that a court need not find proprietary origins to a claim to an equitable lien which are traceable to existing assets against which the equitable lien is sought to be secured, but rather that a court, having decided that an equitable lien should be granted, may grant the lien against such assets as are then ascertainable. However, this is an admittedly broad reading.

In the result of *Space Investments* the Privy Council held that the broad trust instrument under which the monies were deposited allowed the bank to treat the trust monies "as if it were customers' money" such that it could be used in its banking business in any manner that it pleased. The court therefore held that the effect of this broad grant was that the trust money ceased to be impressed with the trust and, as a

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43 *Supra*, footnote 41, at p. 76.
44 *Ibid*., at pp. 76-7.

result, there was "no justification for the intervention of equity".[45] The claim for priority was dismissed and M.B.T. was held to rank *pari passu* with the unsecured creditors in the distribution of the bank assets. The quoted passage of Lord Templeman is thus merely *dicta*.

This passage has been soundly criticized in a recent article by Professor R.M. Goode.[46] Professor Goode states that the grant of equitable remedies presupposes the continued existence of identifiable property for tracing purposes; if the property is no longer traceable, because of commingling or dissipation, there is nothing equity can do beyond conferring a personal remedy.[47] He stated:[48]

> The reference in Lord Templeman's speech to cases on the commingling of trust funds with the trustee's own assets suggests that he was himself assuming the continued existence of the fund and that it was this he had in mind when referring to "all the assets of the bank". If, however, he was intending to go further and suggest that where the commingled fund itself has been lost the beneficiaries have a proprietary claim to all the remaining assets of the trustee, then I would suggest that this is heterodox and does not represent English law.

Professor Goode noted the contention of Goff and Jones that "where tracing fails it may nevertheless be just in certain cases" to impose a lien over such assets as can then be ascertained but dismissed this "swollen assets" theory as unconvincing.[49]

Moreover, Lord Templeman himself cautioned against unduly extending equitable remedies in the subsequent case of *Ross* v *Lord Advocate*.[50] In this case the issue of whether the depositors of a bank had a proprietary interest in the assets of the bank, with the result that their claims would achieve a priority over other claimants, was

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45 *Ibid*., at p. 78.

46 R.M. Goode, "Ownership and Obligation in Commercial Transactions" (1987), 103 L.Q. Rev. 433.

47 *Ibid*., at p. 446.

48 *Ibid*.

49 *Ibid*., at p. 447.

50 [1986] 3 All E.R. 79,

directly raised. In holding that they had no such proprietary rights Lord Templeman stated:[51]

> The proposition that a statutory trustee savings bank held its assets on trust to provide for repayment of the depositors is as heretical as the theory that a trustee bank holds its assets on trust to provide for repayment of its authorized trust deposits: see *Space Investments* . . . The proposition that a statutory trustee savings bank held its assets on trust to repay its depositors would create a new kind of floating charge hitherto unknown to the law and possessing unexplored incidents and priorities. Alternatively, the theory would produce a new kind of equitable interest hitherto unknown to the law and valueless and unnecessary.

A decision of the English Court of Appeal subsequent to *Space Investments* suggests that the English courts may well be moving in the direction suggested by Goff and Jones, however. In *Guiness Plc* v. *Saunders*[52] a director of the plaintiff company, Guiness, had been paid a substantial sum of money for his services to the company in warding off a take-over bid. The director was held to have breached his fiduciary duty to the company by entering into these payment agreements and, in accordance general equitable principles, was held to be obliged to repay the monies. The trial judge declared that the director was liable, as a constructive trustee, to repay the company and granted Guinness an "equitable charge over any bank or other account or over any property" of the director to secure repayment.[53] This order was upheld by the English Court of Appeal.

Guinness Plc v. *Saunders* seems to be a clear example of the type of case envisioned by Goff and Jones in which it is "just" that the court extend the remedy of the equitable lien in order to redress a situation of unjust enrichment. In this case, even though there was no "proprietary" origin to the lien claim, the court found it just to impose an equitable lien over such assets of the director as could be ascertained in order to secure repayment of the monies he had improperly received. Neither the trial judge

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51 *Ibid*., at pp. 92-3.
52 *Supra*, footnote 42.
53 *Ibid*., at p. 941.

nor the Court of Appeal addressed the fact that, in granting the equitable lien over then ascertainable assets, they were largely breaking new ground.

Thus, an argument can be made on the basis of the dicta of Lord Templeman in *Space Investments* and the subsequent decision of *Guinness Plc* v. *Saunders* that the English courts may well be prepared to take the view suggested by Goff and Jones and extend the application of the remedy of an equitable lien far beyond its proprietary origins. On this view the English courts may well extend the remedy to grant an equitable lien against such assets of the defendant as are then ascertainable in order to redress situations of unjust enrichment.

Canadian courts do not appear to have considered whether they are prepared to extend the remedy in this manner (although the issue was implicitly raised, without a final resolution, in the *Canadian Commercial Bank* case, discussed *infra*). The modern trend of Canadian courts has been to apply the equitable proprietary remedy of the constructive trust to redress situations of unjust enrichment, however,[54] and in one recent case, *Atlas Cabinets & Furniture Ltd.* v. *National Trust Co*.[55] a Canadian court granted a constructive trust against the general assets of the defendants in the face of counsel's argument that there need be an identifiable "separate fund" of assets to which the trust could attach. This case has recently been upheld on appeal and is worth examining as it suggests that, if the Canadian courts are prepared to extend the remedy of an equitable lien to situations of unjust enrichment as suggested by Goff and Jones, they may impose an additional requirement that there be a "causal connection" between the property sought to be secured by the equitable lien and the unjust enrichment.

In *Atlas Cabinets* the plaintiff subcontractors worked on a large construction project which was being funded through mortgage financing by National Trust Co. The owner of the project fell into arrears in payments to the subcontractors and, as a result, the subcontractors and their workers had the right to file statutory lien claims for the

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54 See *Sorochan* v. *Sorochan* (1986), 29 D.L.R. (4th) 1, [1986] 2 S.C.R. 38, [1986] 5 W.W.R. 289.

55 (1988), 50 D.L.R. (4th) 159, 24 B.C.L.R. (2d) 389 at p. 395, 39 B.L.R. 90 (S.C.), var'd 68 D.L.R. (4th) 161, 45 B.C.L.R. (2d) 99, 38 C.L.R. 106 (C.A.).

monies owed. An officer of the mortgagee, National Trust Co., represented to the subcontractors that their claims would be paid if they completed their work and, on this basis, they stayed on the job and failed to file their statutory lien claims on a timely basis. The real estate market subsequently collapsed and the mortgagee refused to advance further funds, leaving the subcontractors with claims to monies owing in excess of $1 million.

The subcontractors commenced an action against National Trust which alleged that, by "urging the subcontractors to complete the work, and causing them to forgo their alternative of stopping work, cutting their losses, and exercising their rights to lien the uncompleted project" National Trust Co. was unjustly enriched at their expense. The subcontractors asked the court to declare a remedial constructive trust as against the general assets of National Trust Co. to secure declaration at trial.

The discussion of the nature of a remedial constructive trust by Lambert J.A., writing for the majority of the British Columbia Court of Appeal, is of considerable interest. He stated:[56]

> A remedial constructive trust is a trust imposed by court order as a remedy for a wrong. The entitlement to that remedy may be a matter of substantive law, but the trust itself is not created by the acts of the parties, or even by obligation to make restitution, but by the order of the court . . . There must, of course, be a causal connection between the property in question and the unjust enrichment. See *Sorochan* . . .

In the result, however, the Court of Appeal noted that the trial judge had awarded a money judgment against the defendant, notwithstanding his declaration of a constructive trust. The court upheld this judgment and stated that there was therefore no need to consider the factors which might determine the "causal connection".

Atlas Cabinets is of considerable interest, however, as it suggests that, in the event the Canadian courts are prepared to extend the remedy of an equitable lien to situations of

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56 *Ibid*., at p. 112 B.C.L.R.

unjust enrichment as suggested by Goff and Jones, they might also impose an additional requirement that a "causal connection" be found between the property sought to be impressed with the lien and the unjust enrichment. Thus, unlike the apparent direction of the English courts, the Canadian courts, by imposing this additional requirement, might require a greater degree of adherence to the proprietary origins of the remedy.

(3) The Priority of an Equitable Lien

Another interesting issue which arises is how far the courts will push the remedy of an equitable lien beyond its proprietary origins in situations where the assets of the person or company against whom the claim to a lien is being asserted are being distributed amongst competing claimants, e.g., on an insolvency. The lien claimant, if successful, would gain a priority over the unsecured creditors because the property impressed with the equitable lien would no longer form part of the bankrupt estate and hence would no longer be available for distribution to the other claimants. Should a claim for an equitable lien, being a proprietary remedy in nature, be granted given that the effect of the remedy would be to give the lien claimant such a priority?

In *Space Investments* Lord Templeman was clearly prepared, in principle, to grant an equitable lien over the assets of the bank with full cognizance that such a grant would confer a priority over the unsecured creditors.

The issue of whether persons exercising equitable remedies of a proprietary nature such as the equitable lien and constructive trust should, by the nature of their remedy, achieve such a priority has been the subject of considerable academic discussion and much attention has been paid to whether such a priority is fair or not.[57] It should be remembered that the remedy of an equitable lien is possessory in origin; it is derived from the "common law" or "legal" lien, which could only be exercised as long as the lien claimant remained in possession of the charged property. The courts of equity developed

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[57] See David M. Paciocco, "The Remedial Constructive Trust: A Principled Basis for Priorities Over Creditors", *supra*, footnote 40, and R.M. Goode, "Ownership and Obligations in Transactions", *supra*, footnote 46.

the remedy of an "equitable lien" from this position such that an equitable lien can be granted to secure a claim against property notwithstanding the loss of possession of the property.

The possessory origins of the lien must not be lost sight of. The inherent "fairness" of granting an equitable lien claimant priority over unsecured claimants by virtue of the proprietary nature of the remedy arguably stems from its possessory origins, or at least from the ability to trace the "charge" which gives rise to the equitable lien back to some specific property.

Even Goff and Jones, in recommending the extension of the remedy to redress situations of unjust enrichment, recognized that "fairness" was a valid consideration in situations of insolvency. The authors stated:[58]

> The mere fact that a defendant has been unjustly enriched does not mean that the plaintiff is entitled to a proprietary claim. A restitutionary proprietary claim should be granted only if the court considers it proper to allow the plaintiff the additional benefits which flow from the grant of such a claim. There are certain cases where it is clear that a proprietary claim should not be allowed. Thus, a proprietary claim should never lie where the plaintiff is simply an unsecured creditor, even if the transaction in question proved to be ineffective; for it would be unjust in the circumstances to prefer the plaintiff to the defendant's general creditors … In concluding whether to allow a proprietary claim the court may take into account, in the context of each case, a number of diverse factors. The plaintiff's and the defendant's conduct may be relevant; the plaintiff may have been negligent or the defendant may have cynically disregarded the plaintiff's rights. If the dispute occurs in the context of the defendant's insolvency, the courts should inquire whether it is proper to prefer the plaintiff to the defendant's general creditors . . .
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> The grant of equitable remedies has always been discretionary. Similarly, the courts should have a discretion whether or not to grant a restitutionary proprietary claim.

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58 Sir Robert Goff and Gareth Jones, *The Law of Restitution*, 2nd ed. (London: Sweet & Maxwell, 1978), pp. 62-3.

Thus, inherent "fairness" arguments may well be raised when the remedy of an equitable lien is sought to be extended in a modern commercial context to novel situations, especially when there are numerous claimants competing for limited assets. The inherent "fairness" of granting a proprietary equitable remedy, as opposed to a remedy in personam, may well be a consideration which should be assessed by a court in considering whether to extend the application of the remedy far beyond its proprietary origins. As we shall see, such "fairness" arguments featured prominently in the Canadian Commercial Bank case.

(4) Does the Remedy of an Equitable Lien Necessarily Survive on Insolvency?

Although the courts frequently grant the equitable remedies of a lien or constructive trust following an insolvency (as the court was prepared, in principle, to do in *Space Investments*), there is a troubling Supreme Court of Canada decision which calls into question whether equitable remedies may be available in the event of an insolvency. In *Elliott* v. *Canadian Credit Men's Trust Assn. Ltd.*[59] R.J. Whitlas & Company had purchased certain lands, with title to these lands taken in the name of Elliott, the company president. Elliott subsequently executed a mortgage against the lands in order to secure a loan. Many years later the company was assigned into bankruptcy and the Canadian Credit Men's Trust Assn. Ltd. was appointed trustee. The trustee attempted to have title to the lands of the bankrupt company registered in its name, but this was unsuccessful. Canadian Credit Men's Trust Assn. Ltd. assumed the responsibility of managing the lands nonetheless. Elliott, as title holder, then took the position that he stood in the position of a trustee of the lands for the benefit of Canadian Credit Men's Trust Assn. Ltd. and claimed indemnity, on the basis of general equitable principles, for liabilities which might arise from assuming this position of trust. His claim was dismissed, however, on the basis that, as the property of the bankrupt vested in its trustee upon insolvency, the equitable remedy was not enforceable against the trustee in his personal capacity. It is not clear whether this case can be confined to this narrow proposition,

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[59] [1935] 1 D.L.R. 353, [1935] S.C.R. 1, 16 C.R. 120.

however, and it might be read as holding that, upon insolvency, the equitable remedy could no longer be given effect.

Thus, although in *Space Investments* the Privy Council was, following an insolvency, in principle prepared to grant an equitable lien which would take priority over unsecured creditors, in *Elliott* the Supreme Court of Canada was, following an insolvency, not prepared to grant the equitable remedy claimed. *Elliott* does not appear to have been subsequently applied for the broader reading of its principle and this principle seems to stand in contradiction to more modern authorities. As a decision of our highest court, however, *Elliott* must at least give those seeking to claim equitable remedies following an insolvency some pause for consideration.

(5) Testing the Limits: the Canadian Commercial Bank Case

A case has recently come before the Alberta courts, *Canada Deposit Insurance Corp*. v. *Canadian Commercial Bank*,[60] which, to some extent, probed the limits of the remedy of an equitable lien. As the case was resolved by settlement just prior to its scheduled hearing by the Supreme Court of Canada, however, it did not result in definitive judicial pronouncements on the issues. Nonetheless, the case is interesting as an illustration of a testing of the limits of the remedy in a modern commercial context.

The failure of the western based Canadian Commercial Bank gave rise to the Estey inquiry into the reasons for the bank's failure as well as several lawsuits. Following its insolvency the bank was would up under the federal *Winding-up Act*[61] and Price Waterhouse Ltd. was appointed by the court as its liquidator. One of the major claimants against the bank's assets was the Canadian Deposit Insurance Corporation ("C.D.I.C."), and it soon became apparent that there would not be sufficient assets in the estate of the bank to satisfy all claims against it.

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60 (1989), 61 D.L.R. (4th) 161, 98 A.R. 353, 68 Alta. L.R. (2d) 194 (C.A.), leave to appeal granted 65 D.L.R. (4th) vii, 101 A.R. 160*n*, 102 A.R. 80*n*.

61 The *Winding-up Act*, R.S.C. 1970, c. W-10 (as it then was) – now R.S.C. 1985, c. W-11.

The liquidator applied for and received a court order authorizing it to sue the former principals of the bank for negligence in the management of its operations. The liquidator then commenced a lawsuit against essentially three classes of defendants: the "management defendants", i.e., the officers and senior managers of the bank, the bank directors and the auditors. The action claimed damages of $294 million and asserted detailed allegations of "breach of contractual, statutory and common law duties to act honestly and in good faith". The statements of defence filed on behalf of most of the defendants denied these allegations and, most interestingly for the purposes of this article, asked for the following further relief:

- a declaration that the defendants were entitled to be fully indemnified against all costs, charges and expenses incurred in the action;
- an order setting up a fund out of the assets of the estate of the bank as security for the satisfaction of these indemnification rights, and
- an order that each of the defendants was entitled to an equitable lien or charge in priority to the claims of the other creditors in respect of the estate of the bank.

The defendants' claims to indemnification rights stemmed from their former fiduciary relationship with the bank. Their argument for indemnification as former fiduciaries was essentially three pronged and relied on the bank's obligations pursuant to the *Bank Act*, pursuant to the bank's by-laws and pursuant to a fiduciary's right of indemnification at equity as established in the seminal decision of *Wallersteiner* v. *Moir (No. 2)*.[62]

In June of 1988 a preliminary application was made on behalf of most of the defendants before Wachowich J. of the Alberta Court of Queen's Bench to stay the action until the liquidator posted an amount for security for costs. Counsel for the defendants also requested that Wachowich J. further order that the defendants have a priority of claim as against the amount posted so that they were assured that monies would be available to satisfy their indemnification rights should they ultimately be successful in establishing this entitlement. Concurrent applications were also made for "up-front and ongoing" funding of the defence of the management defendants.

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[62] [1975] 1 All E.R. 849.

At the hearing of the applications counsel for the liquidator conceded that some amount need be posted for security for costs and the application was essentially contested on the basis of what scale of costs should be provided for and whether there should be a funding order. In the result, Wachowich J. ordered that:

- the liquidator post the sum of $15 million as security for costs of the defendants by placing funds from the estate of the bank in a separate interest-bearing account;
- the liquidator "top-up" this amount on an annual basis in order to meet prospective costs;
- the defendant directors and auditors have a "first and prior claim, in preference to any and all other claims in the estate"; and
- that the liquidator fund the defence of the management defendants on an ongoing monthly basis.

Thus, Wachowich J. granted the defendants relief that was substantively akin to the granting of an equitable lien. The order was made to ensure that the defendants' claims to indemnification rights, founded largely in equity, could ultimately be satisfied. The order had the effect of carving out a fund of money from the general assets of the insolvent bank and charging this fund with satisfaction of any indemnification rights of the defendants that might be established. The order further granted the defendants a priority in claim against these funds, a feature customarily accorded to a proprietary remedy.

As might be expected, the liquidator, supported by the C.D.I.C., appealed the order. The liquidator challenged most of the provisions of the order and asserted a strong challenge to the priority granted against the funds posted for security for costs. The liquidator argued that: "The order completely disregarded the interests of the creditors (both secured and unsecured), of the bank and its shareholders", and further that: "Courts of Equity should not be relied upon to remedy an alleged contingent hardship, where such claim has not in the past been recognized either at common law or equity."

Counsel for the respondents sought to uphold the order, and especially the granting of the priority, by advancing arguments as to why it would be unjust and "monstrously unfair" if the defendants were not granted such relief. Thus, for example, it was argued that it would be unfair not to carve out this fund and thereby ensure that there were assets to satisfy their indemnification rights as, in the absence of such a charged fund, the liquidator and the creditors of the bank would have all the benefits resultant from pursuing the lawsuit without having to shoulder the burden of indemnifying the defendants, because of insufficient assets, should the lawsuit be unsuccessful.

In the result, the Court of Appeal largely overturned the order of Wachowich J. It continued the order that the liquidator post an amount for security for costs, but in an amount to be determined "from time to time". It quashed the granting of a priority against these monies as well as the obligation to "top-up" the fund. It also wholly quashed that part of the order which had allowed funding of the defence of the management defendants.

The judgment of the Court of Appeal is very unsatisfying, however, in that the court did not fully address the substantive issues arising nor seem cognizant of the novelty of the relief granted by Wachowich J. The court held that the defendants were not entitled to indemnification on the basis of the *Bank Act* or bank by-laws and stated that *Wallersteiner* was of "no application". The matter was appealed to the Supreme Court of Canada, but resolved by settlement prior to that court's adjudication.

Canadian Commercial Bank is of interest in that it highlights many of the issues as to the scope of the remedy of an equitable lien discussed in this article. In this case there was no prior agreement between the parties that certain property would be made available to secure obligations; rather, the interlocutory relief applied for by counsel for the defendants was akin to the remedy of a true equitable lien as it would arise purely by imposition of law. The claim was to secure an "obligation" in its broadest sense in that the obligation claimed, the right to indemnification, was largely founded in equity. There was no proprietary origin to the claim and the relief granted by the trial judge had the effect of carving out a fund from the general assets of the bank in order to secure the prospective indemnification rights of the defendants.

As the relief granted was a purely “equitable” intervention with no possessory or other proprietary origins, any justification for the relief was far from the philosophical moorings of the traditional remedy of an equitable lien. Indeed, most of the arguments advanced on behalf of the defendants in seeking to uphold the order of Wachowich J. were based on what was “fair” and “just”. Thus, in many ways it was a pity that the case was not thrashed out by the Supreme Court of Canada as it could have provided considerable guidance as to how far the Canadian courts may be prepared to push the remedy of an equitable lien.

4. Conclusion

Although the remedy of an equitable lien is of historic origin and has been infrequently applied in Anglo-Canadian jurisprudence throughout this century, the recent cases of *Swiss Bank* and *Waitomo Wools*, together with its robust application in American law, suggest a new life for the remedy in a modern commercial context. There is also considerable flexibility in the “menu” of concomitant remedies that are available to enforce an equitable lien. For these reasons, as well as the apparent new life given to equitable remedies in general by the *LAC Minerals* decision, the practitioner may want to reflect on the utility of this remedy. The potential scope of this remedy in a modern commercial context is largely unknown, however, with many issues arising. It will be interesting to observe how its limits are explored in future litigation.