

**Judgment 27/2005**

**(i) Hammerschmidt and (ii) Kells Worldwide  
Limited v. Barclays Bank PLC – Royal Court  
(Civil Action File 712) – 3 May, 2005**

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**Exception de Fond – determination of relative priority of equitable interest in security/ies held by the First Plaintiff and the legal interest held by the Defendant.**

**IN THE ROYAL COURT OF THE ISLAND OF GUERNSEY**

The 3<sup>rd</sup> day of May, 2005 before Alan Robin Winston Hancox Esquire, EGH, CBE,  
Lieutenant Bailiff; sitting alone

In the matter of:

WOLF-RUDIGER HAMMERSCHMIDT  
(First Plaintiff)  
KELLS WORLDWIDE LIMITED  
(Second Plaintiff)  
and  
BARCLAYS BANK PLC  
(Defendant)

Whereas on 17<sup>th</sup>, 22<sup>nd</sup>, 23<sup>rd</sup> and 24<sup>th</sup> March, 2005, the Lieutenant Bailiff, having heard submissions from Advocates R. I. C. E. Harris and C. H. Edwards, Counsel for the Plaintiffs and for the Defendant respectively, on the question of law submitted for the determination of the Court on the 3<sup>rd</sup> day of September, 2004, namely:

That the following preliminary issue be tried on the assumption (for the purposes of the trial of that preliminary issue only) that the facts and matters pleaded in paragraphs 3 – 30, 33 and 35 of the Cause, and in paragraphs 3.2, 6, 21, 24.1, 25, 28, 33.1, 34, 41.1 and 41.2 of the Defence dated 12<sup>th</sup> June, 2003, are true:

The Preliminary issue

At the time Barclays enforced its security/ies under the First and/or Second Security Agreements, did Mr Hammerschmidt's equitable interest in the subject matter of the said security/ies as a beneficiary under a constructive trust take priority over Barclays' interest in the same pursuant to its security/ies (or vice versa)

1. Decided the said question of law in the Defendant's favour and gave judgment in the terms attached hereto
2. Reserved the question of costs thereof.

S. M. D. ROSS  
Her Majesty's Deputy Greffier

**Approved Text**

**IN THE ROYAL COURT OF GUERNSEY  
ORDINARY DIVISION.**

**Between:                   WOLF-RUDIGER HAMMERSCHMIDT.....First Plaintiff**

**KELLS WORLDWIDE LIMITED                   Second Plaintiff**

**And**

**BARCLAYS BANK PLC.....Defendant**

**Judgment on Preliminary Issue raised by Consent Order of 3<sup>rd</sup> September 2004**

1.                   On 23<sup>rd</sup> May, 2003, I dismissed the Defendant's Application for discovery of documents prior to the Defence being filed. This was lodged, together with a counterclaim for various declarations, on 13<sup>th</sup> June of that year, followed by the Reply and Defence to Counterclaim on 9<sup>th</sup> January, 2004. Since then the Plaintiffs and the Defendant (to which I referred as 'Barclays' or 'the Bank' in my previous judgment, and I will continue to do so) have filed several Cross Applications for Orders that the Court should try a Preliminary Issue based on the facts pleaded in various paragraphs of their respective Pleadings accepting (for the present purpose only) that those facts are true.

2.                   The Plaintiffs filed an amended Application on 10<sup>th</sup> May, 2004, without objection, and this expressed the matters included in their Application of 14<sup>th</sup> April rather differently. In particular the question formulated at paragraph 1 of the earlier Application, namely whether Barclays possessed valid security interests under the Security Interests (Guernsey) Law 1993, was put as an assumed fact and the other issues were partially re-cast. Then, on 11<sup>th</sup> May, 2004, I gave agreed directions that each party should submit memoranda within fourteen days specifying which in their opponents' list of questions should not be so determined by the Court, and that the issues which the parties did wish to submit to the Court should be narrowed down as far as possible.

3.                   Mr. Harris' Application of the 25<sup>th</sup> May was accompanied by a Memorandum explaining the reasons for this issue being determined at an early stage, and Mr. Shepherd, for his part, filed a Skeleton Argument on the same day. In the former Mr. Harris referred to a separate Royal Court action between Kells and one, James Turian, and submitted that his proposed Preliminary Issue would not impact on that case, but if, as is contended by Mr. Shepherd in his Skeleton Argument, this Court orders the determination of preliminary issues as between Barclays and Kells, then it might be necessary to consolidate this action with between Kells and Mr. Turian, who, I note, is a signatory to the Second, and possibly the First, Security Agreement.

4.                   It is appropriate to record at this stage that while Mr. Harris only incidentally mentions Kells in his earlier Applications, inasmuch as the three sums in question, namely DM 100,000, DM 4.9 million and DM 9.4 million were paid into Kells' account with Barclays in late 1997 and early 1998 (which is not substantially disputed except as to the trivial amount of approximately DM18) Mr. Shepherd maintained from the outset that there are two issues concerning Kells, to which I shall refer below.

5.                   When the case was listed in the Interlocutory Court on 28<sup>th</sup> May, the parties (Advocate Shepherd then appearing for the Bank) were still not entirely *ad idem* as to the issue to be submitted to the Court for decision. Mr. Shepherd felt he needed further

clarification, while Mr. Harris said he would be relying on Section 14(1)(d) of the Law, to which he later referred in the course of his submissions on the 17<sup>th</sup> and 21<sup>st</sup> March this year. That provision is as follows:

“14(1) The rights of —

(a).....

(b).....

(c).....

(d) Any person (other than the debtor)’ meaning, in this instance Kells ‘who was the owner of, or who had an interest in, any collateral at the time when a debtor purported to cause or permit a security interest to be created in it,

are to be determined without regard to this Law.”

6. However, by 19<sup>th</sup> August, 2004, the parties had reached substantial agreement, and, in particular, Mr. Shepherd omitted the two last Clauses from his earlier application, namely (4) Whether Barclays acted in breach of its man- date with Kells, and (5) If so, whether Kells is precluded from bringing an action against Barclays, no doubt in the interests of having the main preliminary issue, namely which of Mr. Hammerschmidt’s and Barclay’s respective interests should take priority over the other, decided.

7. Consequently, on 3<sup>rd</sup> September the Court recorded this Order:

“That the following preliminary issue be tried on the assumption (*for the purposes of the trial of that preliminary issue only*)’ [my italics] ‘that the facts and matters pleaded in paragraphs 3 to 30, 33 and 35\* of the Cause, and in paragraphs 3.2, 6, 21,24.1 25, 28, 33.1,34,41.1 and 41.2 of the Defence’ (which were the same as those referred to in both parties’ earlier Applications) ‘are true:

“At the time Barclays enforced its security/ies under the First and/or Second Security Agreements, did Mr. Hammerschmidt’s equitable interest in the subject matter of the said security/ies as a beneficiary under a constructive trust take priority over Barclays’ interest in the same pursuant to its security/ies (or vice versa).”

\*[With the exception, obviously, as far as the Defendant is concerned, of the word ‘Wrongfully’ at the commencement of paragraph 35 of the Cause.]

8. In the result it is unnecessary for me at this juncture to deal with the issues said to appertain only to Kells, (the corporate entity which was allegedly used as the vehicle by which the fraudsters were enabled to milk Mr. Hammerschmidt’s funds for their enrichment) and I can now concentrate on the main issue of law which I have just set out, and which is by agreement to be decided before any of the others to which reference has been made.

9. I have ventured to recall the protracted and difficult negotiations which resulted in eventual *consensus* as to the preliminary issue of law to be decided as a tribute to the efforts of Counsel, who did so in the ultimate interests of their clients and of the saving of Court time and of considerable costs. It is, accordingly, well understood that while Mr. Harris and Mr Shepherd, and his successor, Advocate Edwards, will use their best endeavours to maintain this position even after the determination of this preliminary issue, neither can irrevocably commit his client to doing so other than for this purpose.

10. With all this in mind, I will now refer briefly to the passage over the years of the Rules regarding preliminary issues of law. The jurisdiction to dispose of a case on a point of law on the basis that the facts in question are all accepted as proved is derived, both in the Channel Islands and in England from the same source, namely the ancient plea of demurrer. This is described in Wharton's Law Lexicon as:

“A pleading which admits the facts as stated in the pleading of the opponent, and referring the law arising thereon to the judgment of the Court, waits until by such judgment the Court decides whether he is bound to answer.”

11. The Rule which replaced the plea of Demurrer, was Order 25 Rule 2. This permitted either party to raise any point of law by his pleading and provided that the Judge should dispose of it at or after the trial, or, with the parties' consent, before the trial. It was known as the 'Demurrer Rule': see National Real Estate & Finance Co Ltd v. Hassan [1939] 2 K.B at page 73, per Scott L.J, a case which involved a repairing covenant in a lease. As MacKinnon L.J said at page 77:

“.....where advantage is sought to be taken of this procedure under Order xxxv., r.2, care should be taken that a real point of law is being raised and that there should be a clear definition of what the point of law raised is.”

As regards the Channel Islands, Hoffmann J.A. observed in the Cherub Investments case (*infra*,) the Guernsey plea of *Exception de Fonds* is very close to the former demurrer. At page 4 he said:

“An *Exception de Fonds* approximates to what in the old English practice was known as a 'demurrer'. Essentially it is a defence which challenges the validity of the claim on a ground which requires no evidence from the Defendant, apart from such facts as may be agreed between the parties, and which cannot be cured by any admissible evidence which might be adduced by the Plaintiff.”

12. It is evident that this salutary rule could, on occasion, save much time and expense. It could also, as Lord Scarman said in Tilling v. Whiteman [1980] A.C 1 at page 25 result in 'treacherous short cuts' whose price can be 'delay, anxiety and expense'. That was a case where the joint owners of a house in Canterbury which was within the provisions of the Rent Act 1968 let it to the Respondent. The owners subsequently sought possession on the ground that one of them was an owner-occupier who required the house as a residence for herself. The preliminary point for the decision of the Court was whether Case 10 of Part II of Schedule 3 of the Act applied where one only, and not both, of joint owners needed the dwelling as a residence, and that the prescribed notice had been given to the tenant.

13. That was all very well, and no doubt the affirmative answer to the question was invaluable in view of the difficult questions of interpretation posed by the use of the terms 'owner-occupier' and 'landlord' in the singular in the same statutory provision. However, it unfortunately left out of account one vital matter, namely, whether Miss Tilling genuinely required the premises as a residence for herself, or she did not. That, as Lord Scarman said, would have taken half an hour of extra evidence to ascertain. As it was the case had to go back to the Dover County Court to decide the case on the basis that Case 10 applied to the agreed, assumed or proved facts.

14. This situation led to the following statement by Lord Wilberforce, who delivered the leading Speech, which I take as the starting point as to whether the instant case is suitable for an advance or preliminary decision on a matter of law. At pages 17 to 18 of the Report he said:

“So the case has reached this House on hypothetical facts, the correctness of which remain to be tried. I.....have often protested against the practice of allowing preliminary points to be taken, since this course frequently adds

to the difficulties of courts of appeal and tends to increase the cost and time of legal proceedings. If this practice cannot be confined to cases where the facts are complicated and the legal issue short and easily decided, cases outside this guiding principle should at least be exceptional.”

15. A case on the other side of the line was Bennett Steamship Co v. Hull Mutual Steamship Protecting Society [1914] 3 K.B 57 in which the sole issue was as to whether a collision had occurred between the plaintiffs’ ship *s.s Burma* and a fishing vessel whose nets had enveloped the steamer and its propeller. The respective hulls did not come into contact. The Court of Appeal unanimously held that the fishing nets were not part of the vessel and that no collision had taken place.

16. I should also mention two local cases, or, rather, two cases which emanated from the Bailiwick Courts, which bear on this question. First, though not in point of time is the well-known decision of the Guernsey Court of Appeal delivered by Hoffmann J.A (as he then was) in Cherub Investments v. The Channel Islands Aero Club (Guernsey) Ltd [1982] 13<sup>th</sup> January, Civil Appeal No. 11. The second was the Privy Council decision in Vaudin v. Hamon [1974] A.C 569 which involved a complicated question of succession to an estate in Sark which in turn depended on whether an action to establish the appellant’s relationship to the deceased and therefore whether he was entitled to succeed to property there was or was not prescribed by the Loi relative à Prescription Immobilière 1909. The case was remitted to the Court of first instance in order to establish the necessary facts, Lord Wilberforce saying at page 586:

“Unfortunate though it is for the process of litigation to be prolonged, their Lordships consider that justice to the appellant requires that the case return to the Court of the Seneschal of Sark to find the necessary facts to support or repel a case of acquisitive prescription.” My emphasis.

The successor to the English Order 25 Rule 2, Order 18 Rule 11, was in a shortened form and was distilled down so as to enable a party to raise any point of law in his pleading *simpliciter*. It was read together with Order 33 Rule 3. The authorities show that the same principles are to be followed as under its predecessor.

17. It is plain from the foregoing that the issue as now agreed is a proper one to be submitted for determination within the foregoing principles, and I therefore turn to consider the submissions of Mr. Harris and of Mr. Edwards in the light thereof. Mr. Harris says that the first Plaintiff’s case is that he retained equitable interests under constructive trusts in the funds deposited in Kells’ account, namely DM 100,000 on 25<sup>th</sup> November, 1997, DM 4.9 million on 10<sup>th</sup> December, 1997, and DM 9.4 million on 27<sup>th</sup> February, 1998.

18. Advocate Edwards, who now appears for the Bank, accepts that proposal, of course without prejudice to his client’s future position. Accordingly the all-important matter for the Court now to determine is whether or not these beneficial interests, being created earlier in point of time, take priority over the Banks’ interests created by the Assignment of the 20<sup>th</sup> January, 1998 and the Security Agreement of 9<sup>th</sup> April, 1998, both of which are said to be statutorily sanctioned under the provisions of the 1993 Law.

19. Mr. Harris referred at the outset of his legal submissions to the Guernsey Court of Appeal case of Stuart-Hutcheson v. Spread Trustee Co Ltd [2002] WTLR 1213 which I have found particularly helpful. In that case Clarke J.A. said at page 1222:

“That prior to the’ [Trusts Law 1989] ‘trusts had become part of the Guernsey law is not in dispute; what is in issue is the extent to which the general law of trusts in England has become part of the law of Guernsey.”

He then continues, at pages 1222-3:

“In thus importing, as it were, the English concept of a trust and trustees’ [by the 1989 Law] ‘those concerned must be regarded as having intended to introduce the trust concept with its usual incidents unless they were inconsistent with some provision of Guernsey’ [law] ‘or otherwise inapposite or inapplicable.’”

20. As regards the concept of constructive trusts Collins J.A cited with approval an earlier passage from Frossard D.B in C.K Consultants (Plastics) Ltd v.Vines & Barnett Christie Finance Ltd [1982] (Unreported), as follows:

“I now turn to the more difficult question and that is, is the concept of constructive trusts part of our law. In my opinion, I answer, yes, because we recognise trusts.”

He continued:

“In other words, the recognition and acceptance of trusts in Guernsey carried with it the need to seek guidance from jurisdictions, which have a law of trusts, and recognition of the concept of constructive, as well as express trusteeship, as an integral part of the law of trusts.”

According to Mr. Harris, one of the usual incidents of the concept of the law of trusts under English jurisdiction is the rule as to priorities. This is enshrined in the maxim *Qui prior est tempore, potior est jure*: he who is earlier in time is stronger in law. On the authority of the Stuart-Hutcheson case Mr. Harris says that this rule should be applied in Guernsey in the instant case.

21. Mr. Harris continued that in respect of each set of transactions in the instant case there are two competing equitable interests, but not, and this is of some importance to his case, two competing equitable assignments. It is common ground that Mr. Hammerschmidt paid in to Barclays in Guernsey DM 100,000 on 25<sup>th</sup> November, 1997, and DM 4.9 million on 10<sup>th</sup> December of that year. These two amounts, were, as stated in paragraphs 6.1 and 6.2 of the Defence, in accordance with instructions acted on by Barclays, paid into account Number 43713233, which, it is accepted, was an account maintained by Kells Worldwide Ltd, a company registered in the British Virgin Islands.

22. The aggregate of the two sums so paid in, which was just short of DM 5 million, was transferred by the Bank successively into accounts maintained in Kells’ name, namely currency deposit account 6129918 and (on 23<sup>rd</sup> December, 1998) into 6130514 (see paragraphs 3.2.3, 21.1 and 21.2 of the Defence). Mr.Harris has maintained throughout that the First Plaintiff acquired, from the moment when the two sums comprising that amount were deposited with the Bank, an equitable interest under a constructive trust in the DM 499,865.88 specified in the Schedule to the First Security Agreement.

23. On the 8<sup>th</sup> January, 1998, (see paragraph 21.3 of the Defence) Barclays provided a loan to the Company known as Ivyside (see paragraph 4 of my earlier Judgment) of DM 4,750,000, and the rights conferred on Barclays by the First Security Agreement, which bears the date of 20<sup>th</sup> January, formed the security for the loan so provided. Barclays has consistently maintained that it did no more and no less than it was entitled to do under the terms and conditions of the loan and in accordance with normal and accepted banking practice.

24. Later in his address Mr. Edwards referred to Inland Revenue Commissioners v. Gribble [1913] 3 KB 212. He said that in realising its security interest pursuant to the Security Agreement of 20<sup>th</sup> January, 1998, Barclays fell into the third category propounded by Buckley L.J. at page 218 of the Report, and thus became a *bona fide* purchaser for value. The consideration was the advance of the first tranche of monies to Ivyside as instructed by the persons mandated to operate Kells’ account, namely two of the alleged fraudsters, Messrs Rochelle and Brillaud (the arrest of the former in Luxembourg having alerted the Plaintiff and caused him to consult German lawyers in early 1999) and Standard Mercator signatories—

presumably a company connected with the Mercator Trust Company which had initially introduced Kells as a customer, and the subject of the Defendant's discovery application of 7<sup>th</sup> January, 2003.

25. The Defendant's contention, accordingly, as stated in paragraph 3 of its first Skeleton Argument, is that it took an equitable assignment under and by virtue of the First Security Agreement of the balance of the account number 6130514. Therein lies the kernel of one of the main areas of disagreement between Mr. Harris and Mr. Edwards, for Mr. Harris relies on the maxim (this, in turn forms the basis for his submission in relation to Section 14(1)(d) and (5) of the 1993 Law) *nemo dat quod non habet*: no one can give to or confer on someone else that which he, or, in this case, Kells, did not possess. It must, of course, be borne in mind throughout that Kells, and not the Bank, was the legal owner of the monies held on deposit in the account prior to 9<sup>th</sup> April, 1999.

26. Consequently, Mr. Harris submits, that since it has not been, and cannot be, advanced that Kells ever had a beneficial, that is to say, equitable, interest in the money resting, in its name, in an account at the Bank, it could not do that which it purported to do under the First Security Agreement, namely assign to the other party to that Agreement, that is to say the Bank, the beneficial interest in the 'monies due or owing to the Assignor', as they are described in Clause 2. Consequently the Bank did not have the right to sell or otherwise dispose of that which was purportedly, but inaccurately stated to be, assigned to it, namely the moneys described in the Schedule.

27. It follows from this, Mr. Harris continued, that the Bank could not perfect its title to, and thus acquire the legal ownership of, the moneys deposited with it by taking the necessary steps to notify the principal debtor (Ivyside) and the guarantor (meaning Kells) of the former's default, and debiting Kells' account in order to repay itself on the 9<sup>th</sup> April, 1999, (which it did according to paragraph 35(d) of the Cause, and which is taken to be true for the purposes of the question of law which the parties have submitted to the Court for decision).

28. The second set of transactions encompassed the paying-in on 27<sup>th</sup> February, 1998, of DM 9.4 million by Mr Hammerschmidt into Kells account No. 43713233 with Barclays following a meeting with the fraudsters in Luxembourg some three days earlier. The bulk of this sum was transferred into currency treasury deposit account No.6130514 by deal reference No. 66164199 shortly afterwards. It was scheduled to mature on 12<sup>th</sup> March, 1999, which was later extended to 26<sup>th</sup> March, 1999.

29. On 3<sup>rd</sup> March, 1998, Barclays entered into another loan agreement with Ivyside, and, pursuant thereto, advanced DM 9million from Kells' account to Ivyside. This was subject to the security said to be provided by the Second Loan Agreement of 9<sup>th</sup> April, 1998, whereby Kells, in Clause 1(a) guaranteed the repayment of a sum not exceeding DM 9.4 million, and, *as beneficial owner* (my italics) granted to Barclays security over all sums standing to the credit of Account No. 6130514 (into which the second tranche of monies provided by Mr Hammerschmidt had by then been transferred).

30. Similarly, as in the case of the first set of transactions, Counsel are agreed that Mr. Hammerschmidt became the beneficiary under a constructive equitable trust in respect of the DM 9.4 million he paid into Kells' account with Barclays, and Barclays took an equitable assignment of the DM 9.4 million under and by virtue of the Second Security Agreement. Barclays contends that in due course, after serving notices of default and realising its security, it became a *bona fide* purchaser for value of the balance in Kells' Account 6130514.

31. In regard to its acquisition of the two equitable assignments to which I have just referred, and to the Bank's contention that, in respect of each set of transactions, it was a *bona fide* purchaser for value when the legal interests in these amounts became vested in it, it is important to be clear as to the case advanced by Mr. Edwards, epitomised in paragraph 41 of the Defences, which I now reproduce:

“41. At the dates of execution of the First and Second Security Agreements (namely 20 January 1998 and 9 April 1998 respectively), when Barclays’ security interests were created:

41.141.1 Mr. Hammerschmidt had not given notice to Barclays of his alleged equitable right or interest in respect of the credit balances in the Kells accounts;

41.241.2 Barclays had no knowledge of Mr. Hammerschmidt’s equitable right or interest in respect of the said credit balances, or of the alleged fraud perpetrated against Mr. Hammerschmidt;

41.341.3 Barclays complied with the notice requirements of Section 1(8) of the 1993 Law in relation to its security interests in respect of the said credit balances.

32. The quotation in Mr. Harris’ first Skeleton Argument from the 30<sup>th</sup> Edition of Snell’s Equity appearing at paragraph 39 has now been replaced by the 31<sup>st</sup> Edition. Paragraph 4—03 states as follows:-

“At law, as in equity, the basic rule is that estates and interests primarily rank in the order in which they are created. The precise explanation of this result differs between the two systems. At law the result is generally expressed in terms of the donor’s capacity to confer a good title on the donee of an estate or interest. ....no person can confer a better title than he himself has. The donee therefore takes subject to prior interests affecting the estate or interest..... In equity, the result is expressed more directly in terms of temporal priority.’ [Then the maxim to which I have referred is set out.] Accordingly, where there are two competing equitable interests, the general rule of equity is that the person whose equity attached to the property first will be entitled in priority over the other”

33. The foregoing extract is the cornerstone of Mr. Harris’ argument. Mr. Edwards, however, has maintained that in the instant case the Bank is entitled to rely on two of the modifications to the rule as to priorities, which in his submission form exceptions to it, and which appear in the text immediately before the passage just set out. These are:

- (i) (numbered as (iii) in paragraph 4—02) As a purchaser for value of the legal interest in the property
- (ii) (numbered as (v)) the rule in Dearle v. Hall [1828] Volume XXVII Revised Reports 1, and 38 English Reports 475, the latter being the fuller and more comprehensive report.

I will now examine the authorities cited for and against these propositions.

34. I turn first to the early case of Dearle v. Hall as it was in the forefront of both parties’ submissions, inasmuch as by paragraph 40 of its Defence Barclays relies on it as authority for the proposition that priority is accorded to the party who first gave notice of his interest to the holder of the legal estate in Kells’ account, while the Plaintiffs, in their Replique, deny (for the reasons upon which Mr. Harris expanded in his submissions) that Dearle v. Hall has any application to the instant case. In order properly to understand that decision it is necessary to delve fully into the facts, the two judgments of the Master of the Rolls, and that of the Lord Chancellor, Lord Lyndhurst, affirming them.

35. Peter Brown, by his will dated 11<sup>th</sup> September, 1794, had directed his executrix and executors to invest the residue of his estate, some £4,600, in government or real securities and to pay the interest and produce to his son Zachariah for his life. This resulted in an

annuity of £93. The legal title to the assets remained in the executors. During the ensuing years Zachariah had purported to make successive assignments for value of equitable interests in the form of annuities to different individuals.

36. In 1808 Zachariah decided to sell to Dearle an annuity of £37 for the capital sum of £204. Persons other than the executors joined in an Indenture of 19<sup>th</sup> December, 1808, with Zachariah and Dearle, and secured it by an assignment to Dearle and his executors of the £93 annuity. This provided that Zachariah should continue to receive the produce, interest and dividends of the original capital sum unless and until default should be made for more than 21 days in paying the £37 annuity, quarterly, to Dearle.

37. The following year Zachariah sold a further annuity of £27 to one, Caleb Sherring in return for a capital payment of £150. In pursuance of this Sherring and Zachariah joined in a further Indenture of 26<sup>th</sup> September, 1809, which appears to have taken no notice of the earlier annuity but was expressed to be made on similar security. Both these annuities were paid until the middle of 1811 but then ceased, save that Dearle subsequently caused one of the sureties to be arrested to enforce payment of 1<sup>3</sup>/<sub>4</sub> years' instalments.

38. Notwithstanding the earlier equitable assignments, of which the executors of the Will (that is to say the legal estate holders) had no notice, Zachariah in 1812 advertised his life interest in the original annuity of £93 as an unencumbered interest. This led to negotiations with one, Hall, who, after due enquiries of the executors by his solicitor into the validity of the fund and the title thereto, purchased the annuity for £711 : 3s : 6d. on 20<sup>th</sup> March 1812.

39. The prior assignments to Dearle and Sherring first came to the notice of the executors on 17<sup>th</sup> October, 1812, and they thenceforth refused to make further payments to any of the claimants until their rights should be ascertained. Dearle and Sherring then filed their bill against Hall for payment of their respective annuities, and sought to restrain the executors from paying any part of the original £93 annuity to any person other than the plaintiffs.

40. The plaintiffs relied on the priority in time of the execution of the Indentures under which they had acquired their interests. The defendant argued that by giving the first notice of his interest to the executors, in whom the legal estate to the residue of Peter Brown's estate (out of which the annuities were paid) was vested, he had done all he could to make his title to the interest he claimed complete, whereas, by omitting to give notice of their encumbrances, the plaintiffs had acquired an imperfect title and had thus enabled Zachariah to commit the fraud of which Hall complained.

41. It is important to ascertain, as far as possible, from the two Reports of the Case which are available, if the rule in Dearle v. Hall still survives, almost a century and three-quarters later, and its precise nature, before considering whether it is truly applicable to the circumstances of the instant case. Mr. Harris submits in Parts IX and III of his skeleton and supplemental skeleton arguments respectively, that the rule does not apply because the circumstances here are different, as shown by the authorities he cited.

42. That the decision is still regarded by authoritative courts as giving rise to a rule is shown by the following extracts from relatively recent decisions. In B.S.Lyle v. Rosher (*infra*) Lord Morton of Henryton, described it as 'the well-known rule in Dearle v. Hall.' Fifteen years later, in Warner Bros Records Inc. v. Rollgreen Ltd, Roderick David Stewart (—the pop star Rod Stewart), Mercury Inc & Phonogram Inc. [1975] 2 AER 105 at page 110, Lord Denning said:

“We were also referred to Dearle v. Hall, which gave rise to *the rule in Dearle v. Hall*.”

I do not, however, need to delve into the facts of that case, for Roskill L.J. regarded Dearle v. Hall as ‘a long way, indeed, from the present.’

43. The third case is United Bank of Kuwait v. Sahib & Others [1997] 1 Ch. 107 in which Chadwick J, after stating that to extend the rule to the facts of that case would be to lose sight of its purpose, continued at page 119:

“*The rule* is based on the inequity of allowing an assignee, who has taken no steps (by giving notice to the trustees to whom inquiry might be made) to protect subsequent assignees against the possibility of fraud on the part of the assignor, from setting up his prior assignment against those who have been deceived.”

44. Fourthly, in Pfeiffer G.m.b.H v. Arbuthnot Factors Ltd [1988] 1 W.L.R 150 Phillips J., as he then was, (who subsequently delivered a concurring judgment in the Sahib case, in which, curiously, no reference was made to Pfeiffer) to which both Counsel referred, applied *the rule* in Dearle v. Hall in a situation involving the equitable assignment of debts due to it by its sub-purchasers by a bulk importer of wine. I will revert to this case later.

45. Fifthly, Compaq Computer Ltd. Abercorn Group Ltd, Kellock Ltd, Adamson & Bairstow [1993] BCLC 602, the last case on Mr. Harris’ list, from which he extensively quoted, and in which all the foregoing authorities (save the Kuwait Bank case) were cited, Mummery J. (as he then was) said at page 17 of the Report submitted:

“I deal first with the arguments on *the rule in Dearle v. Hall*. It was accepted by Compaq that, if the rule did apply, Kellock would enjoy priority. Two arguments were advanced on behalf of Compaq as to why the rule in *Dearle v. Hall* did not apply.”

46. Regarding the true nature of the rule, this has exercised the Courts on many occasions: as Lord Macnaghten said in Ward v. Duncombe [1893] AC 369 at page 391:

“The learned counsel for the appellants invited your Lordships to define exactly the principle on which the doctrine of notice as established by the rule in *Dearle v. Hall* depends. Speaking for myself, I think that would be a very hard task. I am not sure that the doctrine rests upon any very satisfactory principle.”

Both this sentence, and that to which Lord Denning referred as a criticism of the Dearle v. Hall (*infra*) were strongly relied on by Mr. Harris

47. The facts in Ward v. Duncombe were that the settlor left leasehold property to his executors on trust for sale, and a portion of the surplus rents, which was to devolve upon his son and then his granddaughter, formed her marriage settlement. This share was assigned to Frederick Wyatt on certain trusts. One of the executors had notice of this assignment and the other did not. By two indentures, made eleven and twelve years later years later respectively, advances of £300 and £200 were obtained from an insurance company on the security of the granddaughter’s share. On an action for the administration of the estate of the original testator questions arose as to the priority of the encumbrances on the granddaughter’s share thereunder.

48. At first instance Stirling J. allowed the claim of the trustees of the marriage settlement as against the directors of the insurance company which held the mortgages over the security, *despite* the fact that the company had received no notice of the prior assignment, in one instance because the executor had no knowledge of the assignment and the other had prevaricated when enquiries were made. This decision was upheld on appeal and on second appeal to the House of Lords.

49. As Mr. Edwards said, it is important to understand the underlying reasons as to why the rule came into existence. The Lord Chancellor and Lord Macnaghten were *ad idem* that where there are successive assignments of an equitable interest and the second or

subsequent assignee has no notice of an earlier assignment, priority depends simply and solely on priority of notice. The reason for this was that if a prior (not primary) encumbrancer who had given no notice was preferred it would facilitate fraud by the *cestui que trust*, and cause loss to those who might have used every precaution to ensure that the title they were taking was valid and had done everything they could to make that title secure.

50. In his Speech Lord Herschell L.C. was impressed by the fact that in Dearle v. Hall Lord Lyndhurst had followed the principle of Ryall v. Rowles [1750] 27 English Reports 1074, which was a case in bankruptcy, but which was expressly stated to be of general application namely:

“.....if you leave another in apparent possession of personal property, you enable him to gain false credit and must take the consequences.....”

He then cited the former Lord Chancellor who had stated (38 E.R page 494):

“Sir Thomas Plumer [M.R.] was of the opinion that the plaintiffs had no right to the assistance of a court of equity to enforce their claim to the property as against the Defendant *Hall*, and that having neglected to give the trustees notice of their assignments, and having enabled *Z.Brown* to commit this fraud, they could not come into this court to avail themselves of the priority of their assignments in point of time, in order to defeat the right of a person who had acted as *Hall* had acted, and who, if the prior assignments were to prevail against him, would necessarily sustain a great loss. *In that opinion I concur.*” My italics.

51. Lord Macnaghten concurred with this reasoning, in similar language, and also [at page 389] approved another principle on which the Master of the Rolls had acted in Dearle v. Hall namely that:

“...a party, till he gave notice to the trustees, had not done everything that was necessary to complete his title. I fully agree with this principle. In a case of this sort it is necessary that a party claiming advantage from his title should do everything that is requisite to complete that title before he sets up a claim in respect of it.”

52. The Lord Chancellor and Lord Macnaghten were also *ad idem* in concluding that Lord Lyndhurst had relied on the much earlier case of Ryall v. Rowles in affirming the decision of the Master of the Rolls. Indeed at page 392, Lord Macnaghten says:

“Much of the reasoning in *Dearle v. Hall* is founded on *Ryall v. Rowles.*”

This is borne out by the following extract from Lord Lyndhurst in Dearle v.Hall at page 494:

“Where personal property is assigned, delivery is necessary to complete the transaction, not as between the vendor and the vendee, but as to third persons, in order that they may not be deceived by apparent possession and ownership remaining in a person who, in fact, is not the owner. This doctrine is not confined to chattels in possession, but extends to *choses in action*, bonds &c. : in *Ryall v. Rowles* it is expressly applied to bonds, simple contract debts, and other *choses in action*. It is true that *Ryall v. Rowles* was a case in bankruptcy but [there is then a reference to the eminent jurists who sat on that Court] [they] ‘did not confine themselves to the case of bankruptcy, but stated grounds of judgment which are of general application.’”

52. While it is perfectly true that at page 378 Lord Herschell stated that:

“Those opinions’ [of the Judges in *Ryall v. Rowles*] ‘do not appear, as the law is now settled, to be of such general application as was thought by Lord Lyndhurst.’”

he then continued:

“...the importance attached to them throws light upon the considerations which led to the judgments in the cases before Sir T. Plumer and Lord Lyndhurst.”

53. It follows from the foregoing and from Mr. Edwards’ emphasis on the passage from Lord Herschell’s Speech at page 377 of Ward v. Duncombe, that, despite its length and antiquity, it is necessary to analyse the decision in Ryall v. Rowles. In that case a trader had taken a loan from two brothers of £1,500, against the security of a mortgage over his dwelling house, coppers and utensils. He then mortgaged the utensils, stock-in-trade, debts and profits, for securing another loan from his partner, Stephens, and again to Sir James Reynel of a seventh part of his moiety. The trader then made another mortgage of the same to one, Skip, and a fifth mortgage of the realty to Stephens in return for £2,000, which Stephens paid to Baugh, to whom it had been assigned by the original mortgage, one Stone.

54. The final disposition made by the trader was to effect a sixth mortgage of his moiety to his son, George, in consideration for a further loan. Notwithstanding all these several mortgages, which had taken place between 1732 and 1738, the trader, William Harvest, had remained in possession of the utensils and stock-in-trade as his own, altered and received the debts due to the partnership without any control from the creditors, until 1740 when he was declared bankrupt.

55. Ryall v. Rowles, therefore, involved a medley of mortgages, pledges and securities, and it is not entirely clear from the Report as to which items were the subject of the successive mortgages. It is, however, clear, as is recognised by Lord Macnaghten in Ward v. Duncombe at page 384, that the very strong Court which decided Ryall v. Rowles was primarily concerned with the construction of the relevant bankruptcy statute then in force—for instance the Chief Justice refers to the use of the preamble in its construction and the Solicitor General, who appeared for the assignees, refers to ‘the act now in construction.’

56. It is also, in my view, clear that the purpose of the action was to achieve equal distribution amongst creditors, and to prevent undue priority between them and the mortgagees. It was submitted that to allow a trader to remain in possession of his goods and chattels would allow him to gain false and delusive credit by the appearance of substance to mislead those who dealt with him. This aspect formed an important part of Mr. Edwards’ submission that to allow another person to remain in apparent possession of personal property is tantamount to an invitation to obtain false credit.

57. The question for the Court to determine in Ryall v. Rowles was whether the phrase ‘goods and chattels’ in the Act included *choses in action*. The Lord Chancellor said at page 1088:

“...where the vendee or assignee leaves such goods in possession of the bankrupt as owner, he confides as much in the general credit of the bankrupt as that creditor who has only taken his bond or note.....Traders instead of absolute sales would then make such mortgages: and there would be a great opportunity; for traders might mortgage over and over again, as this case is a pregnant instance.”

Consequently he held:

“*Choses in action* are properly within the description of goods and chattels within this clause; and I will only add one argument, for the sake of which I mention it, which is, that this construction is strongly warranted by the next preceding clause relating to bankrupts, who by fraud make themselves accountants to the king to defeat to defeat their private creditors; which plainly shows, that the words *goods and chattels* take in *choses in action*.”

58. What then is a *chose in action*? According to Wharton’s Law-Lexicon:

“A *Chose in action*, otherwise called a *chose in suspense*, is a thing of which a man has not the possession or actual enjoyment, but has a right to demand, by action or other proceeding.”

Mr. Edwards strongly relied on the passage to which I referred in paragraph 50 (*supra*) at pages 377 and 378 of the Report in Ward v. Duncombe, of which he sets out an extract at page 5 of his skeleton argument. The rest of the passage in the Speech of Lord Herschell L.C is as follows:

“.....the leading consideration which induced the Court’ [in Dearle v. Hall] ‘to lay down the rule that he who gives notice has a better equitable right than a prior encumbrancer who has given no notice was this, that any other decision would facilitate fraud by the *cestui que trust* and cause loss to those who might have used every precaution that was possible to ascertain, before parting with their money, that the title they were taking was a valid one, and who might have done everything they could to render that title secure.....the point upon which stress was laid was this, that the party giving notice had taken the property out of the apparent ownership and possession of the *cestui que trust*. This is indicated by the importance attached to the opinions of the judges in Ryall v. Rowles.

59. Mr. Edwards submitted, and this is an integral part of his submissions, that that is the very thing that happened in the instant case—that by leaving Kells in possession of the money in its account and failing to give the Bank notice of his interest, Mr Hammerschmidt enabled the fraudsters to do what they did. Mr. Harris, however, submitted that whereas in Dearle v. Hall there were successive assignments of the same beneficial interest, this is not so in the instant case. He, equally strongly, relied on this passage in Ward v. Duncombe, at page 394, in support of his contention that the rule is not to be extended beyond its original scope, as follows:

“I have made these observations, not for the purpose of impugning the authority of the rule in *Dearle v Hall*. The rule is settled law. But it seems to me that when your Lordships are asked to extend the rule to a case not already covered by authority, it is proper to inquire into the principles upon which the rule is said to be founded. For the reasons which I have already given, I do not think those principles are so clear or so convincing that the rule ought to be extended to a new case”.

60. Moreover, said Mr. Harris, this was made crystal clear by Viscount Kilmuir L.C in B.S.Lyle Ltd v. Rosher [1959] 1 WLR 8. The facts of that case were that in 1933 the bankrupt and his father had executed a deed of appointment and release in respect of re-settlement funds, over which they had power of appointment, and had transferred to Lloyd’s certain investments. This was done in order to comply with the conditions of admission so as to enable the bankrupt to be admitted as a member of Lloyd’s.

61. In 1953 the bankrupt borrowed a substantial sum from the plaintiffs/appellants, and later created two charges over the funds deposited in Lloyd’s to stave off proceedings. He was not entitled to use those funds himself or create any charge over them for his debts. Lloyd’s informed the appellants that they had no notice of any other charge over the funds, specifically the interests of the trustees, which had been preserved under the original deed of appointment. The bankrupt had no beneficial interest in the funds held by Lloyd’s. The question for decision was whether the charges created in favour of the appellants ranked in priority to the interests of the settlement trustees.

62. The appellants contended that the case was one of competing equitable interests in which priority was to be decided by an application of the rule in Dearle v.Hall. The Law Lords unanimously rejected this contention on the ground that the bankrupt had no beneficial interest in the Lloyd’s’ funds, Lord Cohen saying at page 23 that this fact was in his opinion fatal to the appellants’ submission that the doctrine in Dearle v. Hall applied. Mr. Harris

drew particular attention to the passage from Lord Kilmuir at page 14, see paragraph 78 (*post*).

63. In response to this line of argument Mr. Edwards said that by no stretch of the imagination could Lyle v. Rosher be regarded as an authority on the applicability or non-applicability of the rule, because, as Lord Morton demonstrated, it was not a case of priorities at all. He said, at page 16, and I underline the relevant portion of his Speech:

“That rule applies where there is a debtor, or fundholder, and an individual who, having a beneficial interest in the debt or fund, executes two or more successive equitable assignments of, or charges on, that interest in favour of different persons. In these circumstances questions of priority arise. But no question of priority can arise in the present case, where the bankrupt has merely executed two wholly ineffective charges, both in favour of the same party.”

64. The next case cited by both Counsel was Hill v. Peters [1918] 2 Ch 273 which was extensively referred to in Lyle v. Rosher. In that case a firm of solicitors who were trustees for a Mr. & Mrs. Peters of an equitable interest in personalty, namely the purchase price received by them in respect of the sale of the Peters’ property, in breach of trust and in fraud of their *cestuis que trust*, and for their own purposes, without disclosing the existence of the trust, had purported to assign the interest by way of mortgage to another client, Mrs Gwyn, who had died in 1911. Afterwards, in further breach of trust, they handed over to Mrs. Gwyn’s executors, the mortgage deed which had formed the security for an advance the solicitors had made to another client, a Mr. Gotto, in September, 1897, on the security of his share in the residuary estate of his father.

65. In 1917 Mrs. Gwyn’s executors gave notice to the surviving trustee of the will of Mr. Gotto senior, and in 1918 they sought a declaration that the notice they had given regarding the £4000 raised from Mrs. Gwyn entitled them to priority over the £2,000, which was still outstanding from the money advanced out of the purchase money due to the Peters’ under the rule in Dearle v. Hall. They claimed that the Peters’ should have given notice of the declaration of trust which the solicitors had made in respect of the £4,000 originally advanced from the money due to Mr. & Mrs. Peters in 1907.

66. In addressing this aspect of the executors’ case Eve J. said at page 279:

“In my opinion the declaration of trust’ [in respect of the Peters’ interest] ‘was not an assignment or transfer, but the creation of the relationship of trustee and *cestui que trust* as between Mr & Mrs. Peters and’ [the solicitors].’

Further on he said:

“I cannot see any reason whatever for so extending the doctrine of Dearle v Hall. I respectfully indorse the observations of Lord Macnaghten in Ward v. Duncombe as to the undesirability of doing anything to extend that doctrine to cases which are not already covered by it.”

67. In dealing with this case Mr. Edwards’ pointed to the fact that in Lyle v. Rosher, Lord Morton, after considering the Scottish case of Redfearn v Somervail [1813] 1 Dow 50, (which he found ‘of no assistance at all’) said at page 17:

“As the Court of Appeal correctly observed, the interests now claimed by the appellants were never in fact capable of being created by the bankrupt, ‘even in breach of trust’. That fact, in my opinion, completely distinguishes this case from Redfearn v. Somervail.”

Then, and Mr. Edwards laid particular emphasis on the next sentence:

“For these reasons the appellants’ case fails *in limine*’—

—in other words ‘at the outset’, or, to put it colloquially, the appellant’s case did not even get to first base—Why? Because, as Mr. Edwards in effect said, and as Lord Morton had earlier said, Lyle v. Rosher was not a case of priorities at all.

68. Finally, as regards this case, Mr. Edwards drew attention to these words of Lord Cohen at page 24:

“.....there was no room for the application of the rule in *Dearle v Hall*. For this reason, while not dissenting from the observations of Eve J.’ [in Hill v.Peters], ‘I prefer to base my opinion that the appeal should be dismissed solely on the ground I have stated’

which, he said, could hardly be treated as a ringing endorsement of Hill v.Peters, or, indeed, of the Plaintiff’s submissions, inasmuch as at least two of the leading cases cited not only held that Dearle v. Hall had no application, but that the issue of priorities had never arisen in either of them.

69. Mr. Edwards then demonstrated that the rule in Dearle v. Hall, notwithstanding that it involved the priority of equitable interests, had been applied in many common law jurisdictions. For instance in Australia Mutual Providence Society v. Gregory [1908] HCA 7; 5 C.L.R 615, the question at issue was whether the interest of the trustee in bankruptcy in the estate of a bankrupt, which had been placed under sequestration in Natal, took priority over successive assignments for valuable consideration by the bankrupt of his interest under the deceased’s will, which included land in Tasmania, to the appellants and others.

70. It seems to me that this case is of little assistance, for although the applicability of the rule in Dearle v. Hall was canvassed, this was only on the hypothetical basis that the trustee’s interest by virtue of the sequestration was fell into the category of a moveable and not an immoveable. The Court, consisting of Griffiths C.J , Barton and Isaacs J.J, took the view that the interest which the trustee had acquired was in immoveable property in Tasmania, and was therefore an immoveable. The result of that conclusion is succinctly stated by Barton J. at page 6:

“For these reasons I am of opinion that G.W.Gregory’s Tasmanian interest was at the time of the Natal adjudication an immoveable, and, therefore, the Natal adjudication and the appointment of Mr. Green as trustee did not operate to vest the interest in that respondent.”

He then states why the Court went on to consider the rule in Dearle v. Hall:

“But in view of possible further proceedings it is perhaps desirable that we should give an opinion on the second question debated at the bar, *which can be dealt with on the assumption that G.W.Gregory’s interest is a moveable.*” [My Italics].

71. It was accepted that the Tasmanian assignees gave notice of their separate interests to the trustees of the deceased’s will on 17<sup>th</sup> February and 16<sup>th</sup> October, 1905, respectively, but the trustee in bankruptcy did not do so until 6<sup>th</sup> November. Under private international law the assignment of a bankrupt’s property to the trustee, as the representative of his creditors, operated as an assignment of his moveables wherever situated, but not of his immoveables. Thus, the interest being in immoveable property, there was no assignment.

72. Consequently, Barton J. stated, in the paragraph of his judgment to which Mr. Edwards referred:

“...the reasoning of the Master of the Rolls in *Dearle v. Hall* applies as fully and as forcibly to an assignee in bankruptcy (or in insolvency) as to an assignee for valuable consideration.”

and in the result, at page 8, he said:

“.....I am of opinion that, *on the assumption stated*, the claim of the trustee in the Natal insolvency is postponed to those of the several assignees, for valuable consideration and without notice of the insolvency, who anticipated him by giving prior notice to the trustees under the will of James Gregory.”

73. Isaacs J. concluded his judgment by saying (page 13):

“On the ground also that the principle of *Dearle v. Hall* would apply if the bankrupt’s interest were a moveable, notwithstanding a Natal assignment in bankruptcy, I am of the opinion the appeal should be allowed.”

While therefore in the case of Australia Mutual Providence Society v. Gregory the rule in Dearle v. Hall would have applied, because of the priority of the notice by the assignees, and the requirement of successive assignees of the same, or similar, interest was satisfied, in my judgment those parts of the judgments of the Court which dealt with the rule are *obiter dicta*.

74. Mr. Edwards’ next case is the appeal to the Privy Council in Colonial Mutual General Insurance Co Ltd v. ANZ Bank (New Zealand) Ltd [1995]. This concerned the priority of equitable interests in the proceeds of an insurance policy between the Respondent Bank, as second mortgagee of a house which was destroyed by fire on 25<sup>th</sup> February, 1988. The first mortgagees had exercised their power of sale and had recovered their debt from the proceeds. The policy had been effected by the appellants in the name of the mortgagor who was, wrongly, paid out by the insurers. The Bank claimed the proceeds of the policy from the insurers, as it had notified them of its interest prior to the fire. The Board applied the rule in Dearle v. Hall and held that the Bank’s equitable interest took priority over that of the appellants.

75. In the Compaq case (*supra*), the plaintiffs sold computers to Abercorn under a dealership agreement which included a Romalpa clause (so named after the case of Aluminium Industrie Vaassen BV v. Romalpa Aluminium Ltd [1976] 2 AER 552). This said that the title to and/or the property in the goods and materials supplied would not pass to Abercorn until the price and any other sums owing had been paid to Compaq. Abercorn sold Compaq products to purchasers under agreements which also included a Romalpa clause. It then made a discount agreement with Kellock, the terms of which included, *inter alia*, the assignment of invoices which it had raised to Kellock, subject to notice to its debtors, and later assigned to Kellock for value debts owing to it for Compaq products. Finally, Abercorn executed two debentures in favour of Kellock con-ferring on Kellock charges on its book and other debts, and also over its undertaking, property and assets.

76. A number of facts were agreed between the parties for the purposes of the trial on five points of law, three of which related to priorities between Kellock and Compaq. Leaving aside for the moment the issues relating to section 395 of the Companies Act 1985 and sections 136(1) and 137(1) of the Law of Property Act 1925, which arose in the course of Mummery J.’s judgment, he followed Phillips J. in the Pfeiffer case (*supra* and *infra*) and held that Kellock’s interests took priority over those of Compaq, notwithstanding that Compaq had effectively retained legal and beneficial title in unsold Compaq products.

77. Mr. Harris submitted that the Compaq case was additional, and, indeed, recent authority in support of his contention that the rule in Dearle v. Hall applied only in the case of successive equitable assignments in favour of different persons, and not where there were competing assignments of two or more equitable interests in one fund. This is evident from

the passage from Lord Morton’s speech in Lyle v. Rosher which I cited at paragraph 63 (*supra*) and which Mummery J. cited at page 14 of Compaq.

78. Neither, Mr. Harris continued, could it apply where the assignor (here Kells) never had any beneficial interest in the fund which he purported to assign or charge. Again a passage from the Speech of Lord Kilmuir L.C. in Lyle v. Rosher is referred to by Mummery J. at page 14:

“I do not know of a case where the doctrine has been applied without there being someone who had at one time a beneficial interest.....I am certainly not disposed to extend the doctrine.”

79. The one consistent thread that runs through the decisions cited in argument is that the rule can not be extended to cover other situations. In Warner Bros Records Inc v. Rollgreen Ltd (*supra*) Sir John Pennycuik said:

“The court’ [in Dearle v. Hall] ‘was there concerned with a trust fund where trustees were directly accountable to all persons having an interest in the trust fund, whether original or derivative. The question at issue was the priority as between various assignees of original interests....the judgment in that case contains valuable statements of principle which have been cited by Lord Denning MR.....”

At page 110f Lord Denning refers to the criticism of the rule by Lord Macnaghten in Ward v. Duncombe at page 393,

80. The passage to which Lord Denning was referring is as follows:

“But the rule in Dearle v. Hall, founded in great measure on the bankruptcy law as it existed sixty years ago, remains unaltered, and it is beyond the power of any Court to alter it.’[*paragraph*] ‘I am inclined to think that the rule in Dearle v. Hall has on the whole produced at least as much injustice as it has prevented.”

81. Although the facts in Pfeiffer (*supra*) bear little resemblance to the instant case, the judgment of Phillips J. as to the priority of equitable interests is of considerable assistance, and, as I have noted above, it was followed by Mummery J. in Compaq. In that case an English importer of wine in bulk from Germany which, in turn, sold wine on to sub-purchasers, assigned to the defendant company debts owed to it by the sub-purchasers, who duly paid them to the defendant.

82. An essential feature of the case was that notice of the assignment of the debts which were sold to the defendant was given to the debtors, i.e the sub-purchasers, by the importers and by the defendant. As there was a title reservation clause in favour of the German plaintiff company it claimed that the defendant’s title to those debts was subordinate to its claims as beneficial owner of the proceeds of sale due from the English importer to the German plaintiff.

83. Mr. Harris of course says that, given the clear judicial authority which is discernible in all the cases which have been cited on the point, that the rule in Dearle v. Hall should not be extended, Pfeiffer can have no application here because it did not involve two or more successive assignments of an equitable interest. In other words the Dearle v. Hall exception to the first in time rule only applies to successive assignments and not to competing priorities of an interest e.g. under a trust, and a subsequent assignment of that interest.

84. In the Pfeiffer case two preliminary issues of law were submitted to the Court for decision, of which only the second, namely:

“Whether or not the defendant’[had] ‘priority over the alleged rights of the plaintiff by virtue of the factoring agreement made between the defendant and Springfield Wine Importers Ltd. and any assignments made pursuant thereto.”

is relevant here. After considering section 136(1) of the Law of Property Act 1925 Phillips J. held that that section enabled the assignee of a debt or chose in action to acquire a legal title to it that had all the advantages of a legal title, but, so far as priorities are concerned, his position was no better than if the assignment had been made prior to the Act.

85. No similar statutory provision in Guernsey has been brought to my attention, and therefore in my view the consequence is the same as that stated by Phillips J. at page 162F, namely:

“...that, even if the assignment is effected for value without notice of a prior equity, priorities fall to be determined as if the assignment had been effected in equity, not in law.”

he continued, at page 163C:

“Under the rule priority depends upon the order in which notice of the interest created by the dealing is given to the person affected by it, i.e. in the case of assignments of a debt, the debtor.”

86. I accept for the purposes of this case Mr. Edwards’ submission that the rule in Dearle v. Hall would apply in Guernsey in the same way as it does in England provided that the conditions judicially laid down for its application are satisfied. Those conditions are, as formulated by Lord Kilmuir L.C. in the most authoritative decision on this question in the last century:

“For the application of the doctrine there are at least four requirements, namely: a fundholder, someone who has, or has had, a beneficial interest, assignee No.1 and assignee No. 2.”

87. Accordingly, in the oft-cited words of Lord Macnaghten in Ward v. Duncombe ‘priority in such a case’[would depend] ‘simply and solely on priority of notice’. This was reiterated by Phillips J. in Pfeiffer as I have just demonstrated and followed by Mummery J. in Compaq, for he said at the top of page 15 of that no bare trust of the proceeds of sale was created in favour of Compaq, but that there was an equitable assignment by Abercorn to Compaq of the proceeds of the sales of Compaq’s products to Abercorn’s customers.

88. At the beginning of that passage Mummery J. ‘assumes’ that there is a distinction between the creation of a trust and an equitable assignment. In my judgment there is such a distinction. It is common ground in the instant case that Mr. Hammerschmidt is the beneficiary under constructive trusts of the monies he admittedly deposited in the Kells Account with Barclays in late 1997 and early 1998. It follows, again in my judgment, and in accordance with the decisions I have reviewed herein, that those transactions are not assignments but trusts which were created and in which Mr. Hammerschmidt had acquired equitable interests.

89. In paragraphs 3 and 6 of Mr. Shepherd’s Skeleton argument (which reflects, although it is not identical to, paragraphs 9.1 and 9.2 of the Defence in this respect) it is expressly stated that Barclays took equitable assignments of the balances of the respective currency deposit accounts into which the money initially deposited by Mr. Hammerschmidt had been transferred by it. These monies then formed the basis for the guarantees provided by Kells as security for the loans to Ivyside under the Security Agreements.

90. In the present case there were not successive assignments of the equitable interests, but two instances of the creation of a trust, followed in each case by an equitable assignment of the monies standing to the credit of Kells in the relevant Bank account. Accordingly, the test formulated by Lord Kilmuir for the application of the doctrine is not satisfied, for there

was no Assignee No. 1. It follows from the authorities, in my judgment, that the rule in Dearle v. Hall does not apply here.

91. Mr. Harris has submitted that there is a second reason why, according to the authorities, the rule does not apply. It is accepted in the Defence the two amounts that Mr. Hammerschmidt initially deposited with the Bank were placed in account No. 43713233. I have already traced the passage of the sums invested from and into the various accounts maintained by Kells in the Bank 9 see paragraphs 17, 21 to 23 and 28-31 hereof). In view of the conclusion expressed in the preceding paragraph it is not essential to reach a decision on this sub-issue (if I may so refer to it). However in order to see this part of the argument in its proper perspective, I find it convenient to recapitulate the basic facts as they have been agreed for this purpose.

92. As has been seen, on 8<sup>th</sup> January, 1998, Barclays and Ivyside concluded a loan agreement (see paragraph 21.3 of the Defence) pursuant to which the Bank advanced DM 4,750,000 to Ivyside on 15<sup>th</sup> January, 1998. On 20<sup>th</sup> January, following the loan Agreement, Barclays, Ivyside and Kells entered into the First Security Agreement, whereby, *inter alia*, Kells assigned to the Bank the amount of DM 4,999,865.88 as specified in the Schedule. This exceeded the sum advanced to Ivyside in accordance with the letter of 8<sup>th</sup> January, 1998, see paragraph 21.3 of the Defence.

93. Mr. Harris advances the same submissions in respect of the deposit of DM 9,399,981.94 into account No. 43713233, in which Mr. Hammerschmidt had a beneficial interest under a constructive trust, and of which Barclays took an equitable assignment pursuant to the Second Security Agreement of 9<sup>th</sup> April, 1998. The sequence of events was that, following the deposit of DM 9,400,000 on 27<sup>th</sup> February, the Bank transferred DM 9,399,981.92 into Kells' currency deposit account 6130514 where it remained until 26<sup>th</sup> March, 1999, earning interest as stated in paragraph 28.2 of the Defence.

94. Barclays then provided a second loan to Ivyside under the second loan agreement of 3<sup>rd</sup> March. On 9<sup>th</sup> April, 1998, the same parties executed the Second Security Agreement whereby Kells granted to the Bank a security interest in its favour over all sums of money standing to the credit of account No 6130514 as stated in Schedule 3. No point has been taken by either side as to the differing form of the Second Security Agreement from the First such agreement. I am satisfied in substance they were the same, and that Kells thereby effected an equitable assignment to the Bank of the balance in that account.

95. The Defence having accepted, for the purposes of this preliminary point, that pursuant to the First Security Agreement, the Bank took an equitable assignment of the balance in currency treasury deposit account No. 6130514 (into which, as stated in paragraph 21.2 of the Defence, the balance in Account 6129918 had been transferred), who, then, was the assignor? Mr. Harris submits that this has to be Kells, since it is so described in the Agreement of 20<sup>th</sup> January, which is itself called 'This Assignment'. He then poses the question: did the Assignor have a beneficial interest in the Account 6129918, or in 6130514?

96. In Clause 2 of the Agreement the Assignor is, loosely, described as Beneficial Owner, but Mr. Harris submits, that is not the reality, for in paragraph 30 of the Cause it is stated that the three amounts paid in by the Plaintiff into Kells' Deutschmark Account No. 43713233, were 'from the moment they were paid in' held by Kells on constructive trust for Mr. Hammerschmidt *as beneficial owner of the same.* The Defence have not sought to get away from this position, since, for the present purposes the truth of paragraph 30 of the Cause is assumed.

97. In Mr. Harris' submission Kells had no beneficial interest in the funds in accounts No. 6129918 or 6130514, either when the Bank took its equitable assignments or at any other time. In addition to the passage I have cited from Lord Kilmuir on this point, he drew attention to the following extracts from Speeches of Lord Keith of Avonholm, at page 25:

“I understand that the others of your Lordships take the view that *Dearle v. Hall* has never been applied to a case where the assignor never had a beneficial interest in the thing assigned, and that the rule in *Dearle v. Hall* should not be extended to cover such a case.”

And to that of Lord Cohen, at page 23:

“Now I know of no case where the rule in *Dearle v. Hall* has been applied where the creator of the incumbrances never had any beneficial interest in the fund. Nor were counsel able to direct our attention to any such case.

98. How, therefore, Mr. Harris says could Kells create in favour of Barclays, an equitable or beneficial interest that it did not have? Although Kells held the legal title and was the Assignor, contrary to that which is stated therein, it did not have a beneficial interest in the money in the account. However, as I have just indicated, in view of my decision that one of the essential ingredients for the application of the rule in *Dearle v. Hall*, namely the requirement of successive assignments, is not present in this case, it is unnecessary for me to decide this point.

99. I therefore turn to address the second, and equally important, issue of whether the Bank, when it acquired its legal interest in the funds concerned, was in each instance a *bona fide* purchaser for value without notice of Mr. Hammerschmidt’s prior interest. As regards the issue of priority, between an equitable and a legal interest, I am content to adopt a passage from Millett J.’s Judgment in *Macmillan Incorporated v. Bishopsgate Investment Trust PLC, Shearson Lehman Bros. Holdings PLC, Swiss Volksbank, Morgan Stanley, Crédit Suisse, Prudential Securities Inc., Paine Webber Inc and Advest Inc. [1995] 1 WLR 981*.

100. The passage in question is at page 1000A & B, and is as follows:

“Where both interests are equitable—or both legal, for that matter—the basic rule is that the two interests rank in the order of their creation. In the case of equitable interests the order of priority may be reversed in special circumstances, but ‘where the equities are equal, the first in time prevails’[subject as appears in this judgment to the rule in *Dearle v. Hall* if it is applicable]..... Where, however, the first is equitable and the second is legal the position is different. A bona fide purchaser for value who obtains the legal estate at the time of his purchase without notice actual or constructive of a prior equitable right is entitled to priority in equity as well as at law: see *Pilcher v. Rawlins* (1872) L.R 7 Ch. App.259. But he must have obtained the legal estate, and the question of notice is normally tested at the time when he obtained it.”

101. The next issue to determine is: was Barclays a purchaser for value when it acquired its interest in the sum standing to the credit of Kells respective accounts? The Bank’s case is that when it made the two advances to Ivyside they represented value in each case, inasmuch as they formed valuable consideration for the assignments which it took from Kells under the two Security Agreements.

102. Mr. Edwards referred to paragraph 29 of his main Skeleton argument, in which a passage from the judgment of Buckley L.J. in *Inland Revenue Commissioners v. Gribble (supra)* is set out *in extenso*. Mr Edwards did not emphasise that that was a dissenting judgment, and that the majority of the Court of Appeal adopted a different meaning of the word ‘purchaser’. They up-held Horridge J. at first instance [1913] 1 KB 224 who had stated the problem thus:

“On behalf of the Crown it was contended that the word ‘purchased’ in this section meant purchased in a popular sense and either in the sense of being bought for money or at any rate for money’s worth; whilst on the other hand it was contended on

behalf of the respondents that purchase had a well-known meaning in English law and meant acquisition of any property otherwise than by descent, or at least that it included any acquisition of property for valuable consideration.”

103. The facts of I.R.C. v. Gribble were that the Commissioners, under the provisions of section 13 of the Finance Act (1909—10) Act 1910, had raised an assessment to reversion duty on the benefit accruing to trustees lease of a house which had expired in 1910. They claimed exemption under section 14(1), the relevant part of which provided:

“Where, in the case of a reversion to a lease purchased before’ [30<sup>th</sup> April 1909] ‘the lease on which the reversion is expectant determines within forty years of the date of the purchase, no reversion duty shall be charged.....on the determination of the lease: Provided that.....”

At page 220 of the Report Kennedy L.J said:

“.....it is our duty.....to say that ‘purchased’ in the first line of this subsection and ‘purchase’ in the fourth line mean that which .....everybody to-day means by the words ‘purchased’ and ‘purchase’ in the ordinary language of life. ‘Purchase’ means ‘buy’.”

And at page 221:

“But I think ‘purchase’ in the ordinary sense in the absence of any context to qualify it does mean ‘buy’.

104. Had it not been for two earlier cases which Mr.Edwards cited on this question, I think he might have had difficulty in overcoming this very definite, authoritative and restrictive interpretation of ‘purchase’ (which term would obviously include ‘purchaser’). It will be seen that that construction was of a word used in a statute dealing especially with tax and revenue. These two authorities in my view demonstrate the criteria by which the Courts will decide this frequently used phrase ‘purchaser for value’ (other than in a specialised statute) namely Taylor v. Blakelock [ 1886] 32 Ch.D 560 and Thomson v. Clydesdale Bank Ltd [1893] AC 282 at Tabs 10 and 11 of Mr. Edwards’ Bundle.

105. As to the first, I am content to adopt very largely the summary of the facts at paragraph 31 of the Defendant’s Skeleton argument. The fraudulent trustee had invested £5,000 from money in the estate of one, Gyhon deceased, in Metropolitan 3 ½ % Stock in his own name. He then embezzled money from the Pearson marriage settlement, of which he was a co-trustee with the Rev. Blakelock, and later paid for Caledonian Railway Stock from part of the proceeds of sale of the Metropolitan Stock. He placed the Caledonian Stock in his firm’s name, and later transferred it into his and Blakelock’s joint names.

106. On his death insolvent seven years later Blakelock, as surviving trustee of the Pearson settlement, had the Caledonian Stock registered in his own name, whereupon Taylor, the surviving trustee of the Gyhon estate, sued for a declaration that it belonged to that estate. A very strong factor which weighed with Bacon V-C and, later Cotton and Bowen L.J.J., was that not only did Blakelock have no notice of the fraud, but that the correspondence and other evidence showed that he was entirely innocent. As in that case, this case is, in the words of Bacon V-C, to which Mr. Edwards drew attention:

“.....one of those painful cases in which, as between two innocent persons, a loss having been sustained, the Court is to decide upon whom that loss should fall.”

107. The Court of Appeal held that Blakelock was a purchaser for value without notice of the fraud. The following passage from the judgment of Bowen L.J. at pages 569-70 of the Report, which Mr. Edwards cited, epitomises the meaning of the phrase ‘purchaser for value’:

“No doubt if [Blakelock] ‘ had notice, then his legal title would disappear, would be invalidated. If he was a volunteer he could not stand in a better position than the person who conveyed to him.; but if he is not a volunteer, upon what principle can you take away his property?”

That really reduces it to the simple question of what is the meaning of the term ‘purchaser for value’ in such cases. “A purchaser for value’ is a well-known expression to the law. By the common law of this country the payment of an existing debt is a payment for valuable consideration.”

108. At page 568 Cotton L.J., in a passage cited at paragraph 32 of the same Skeleton argument, demonstrated that by accepting the Caledonian Stock in his own name Blakelock had parted with the right to sue Carter (the fraudulent trustee). In doing so he had given valuable consideration for having the stock vested in his sole name, and was thus a purchaser of it for value. The action was accordingly dismissed.

109. Thomson v. Clydesdale Bank Ltd was possibly closer to the present case. There a stockbroker employed by the appellants as trustees of one Thomas Dunlop deceased to sell 50 shares in the Commercial Bank of Scotland received a cheque for the money, but dishonestly paid it into his own current account with the respondent Bank, which was substantially overdrawn. He then absconded. The trustees claimed they were entitled to follow the proceeds of the cheque and be repaid by the respondent Bank, and the Bank claimed that it was entitled to retain those proceeds in discharge of the debt due to it on the overdraft. At page 290 of the Report Lord Watson said:

“[The broker’s conduct] ‘was an undoubted fraud upon the appellants; but, in my opinion the broker’s fraud is of no relevancy in this case, unless it is coupled with bad faith on the part of the respondents. The onus of proving that they acted *in malâ fide* rests with the appellants..”

110. As a result of considering these two nineteenth century cases, I have arrived at the conclusion that it would be wrong to apply the narrow and restricted meaning to the word ‘purchaser’ which the majority of the Court of Appeal did in Inland Revenue Commissioners v. Gribble. That decision depended on the particular wording of the Finance Act and as to whether an exemption granted in a taxing statute to a specified set of circumstances applied to the case in question.

111. I do not consider there is any warrant for extending the construction of a specialised phrase in a revenue statute to the much wider circumstances obtaining in the commercial world of Guernsey. The purpose of that Act, as stated in the preamble, was:

“.....to grant certain Duties of Customs and Inland Revenue (including Excise), to alter other Duties, and to amend the Law relating to Customs and Inland Revenue (including Excise), and to make other financial provisions..”

affords further support for this conclusion.

112. It follows that, in my judgment the words of Bowen L.J. which I have set out in paragraph 107 (*supra*) govern the transactions carried out by the Bank in this case. I therefore hold that when the Bank made the advances and took its equitable assignments of the amounts standing to Kells’ credit in the relevant currency treasury accounts, it was a purchaser of those interests for valuable consideration, and therefore for value.

113. This leaves for determination the issue of notice, for, as Bowen L.J. observed, if the respondent had notice, then his legal title would disappear—would be invalidated. At the conclusion of its main Skeleton argument the Defendant emphasises that when it entered into the respective Security Agree-ments it had no notice of Mr. Hammerschmidt’s equitable interests under the constructive trusts.

114. I should record at this stage that, while I have noted (at paragraph 21 hereof) that in paragraphs 6.1 and 6.2 of the Defence it is admitted that at least two of the payments in to the accounts were either made by Mr. Hammerschmidt or on his behalf, I do not think, in deciding the preliminary issue, I can legitimately take these admissions into account. As I understand the position, my task is to decide the issues of priorities within the four corners of the second paragraph of the Consent Order of the 3<sup>rd</sup> September, 2004.

115. Further on the issue of notice, the Defendant says that when it purchased the (equitable) interests, it did not have notice of those of the Plaintiff. The paragraph continues:

“The fact that at the time it enforced its securities’ [the Bank] ‘had acquired notice is of no relevance. By that time the equities had already been determined.”

Any other conclusion, so the argument goes, would result in serious implications for the lending industry, and, in graphic language, would lay lenders open to the risk of a lurking third party being able to trump the lender’s security. These submissions are reiterated and amplified in paragraphs 6 *et. seq.* of the Defendant’s replying submissions, which introduces the doctrine of *tabula in naufragio*. I will consider this aspect shortly.

116. Mr. Harris, however, strongly submits that the 9<sup>th</sup> April, 1999, is the relevant date for determining the issue of notice, which was when Barclays acquired the legal estate in the sums in Kells’ account. Accordingly the letter from the German lawyers, Boesebeck Droste, of 9<sup>th</sup> February, 1999, having stated Mr. Hammerschmidt’s prior interests with crystal clarity, provided ample notice thereof. It followed, he said, that the only possible conclusion was that when Barclays acquired its legal interests on 9<sup>th</sup> April, 1999, it could not be regarded as a purchaser for value without notice as claimed by Mr. Edwards.

117. In response to this line of argument Mr. Edwards submitted that the Court had to look at the dates when the Bank’s *equitable* interests were created, namely the 20<sup>th</sup> January and the 9<sup>th</sup> April, 1998, under the two Security Agreements, when, as he maintained, the Bank had no notice of Mr. Hammerschmidt’s beneficial interests. For this proposition he relied on the early authority of Dodds v. Hills [1865] 2 H & M 424 with which I will now deal.

118. The facts of Dodds v. Hills can be shortly stated. Hills was the sole trustee of certain shares settled on Mrs. Dodds. He obtained a series of advances, beginning in 1857, from one, Smith, the secretary of a local club (from whose funds the advances predominantly came) and, as security, dishonestly executed a transfer of those shares to Smith. On 7<sup>th</sup> June, 1863, Hills absconded and on 30<sup>th</sup> June was declared bankrupt. On 14<sup>th</sup> June Mr. and Mrs. Dodds informed Smith of the trust. On 19<sup>th</sup> June Smith sent the share certificate to the company secretary for registration.

119. Mr. Edwards laid strong emphasis on this passage from the judgment of Page Wood V—C:

“When this arrangement was made’ [in 1857] ‘ Smith had no notice of the trust; and after having received notice, he registered the transfer. At the time of the transfer he acquired the power to register himself as the owner of the shares. Hills could not displace the equity thus acquired, nor was anything further necessary to be done on his part to complete the transaction. Although it is true that, as between him and the company, Smith did not become the owner until after registration, nothing but his own act was necessary to make him complete master of the shares.”

As in Taylor v. Blakelock, a factor which carried some weight with Page Wood V—C was that when he acquired the equitable interest Smith was entirely innocent, for he continued:

“Some suggestion was made that the Defendant was guilty of negligence, such as to

fix him from the outset with notice of the trust. But there is no evidence of any negligence. ....there was nothing to raise a legitimate suspicion in anyone’s mind.”

120. Mr. Edwards stressed that as recently as 1995 in Macmillan Incorporated v. Bishopsgate (*supra*) Dodds v. Hills was regarded as still good law.

It followed that the critical moment for notice was when the equitable interest was obtained, or, here, assigned. This, said Mr. Edwards, is clearly shown by this extract from Millett J. at page 1004 F—G:

“As between the transferee on the one hand and the transferor and those claiming under him on the other, this rather than the time when the transferee actually obtains the legal title is to my mind the appropriate time for the question of notice to be tested.....As the facts of the present case show, modern commercial lending frequently involves substitution of security, and this makes registration inconvenient and commercially unattractive.”

Mr. Edwards particularly drew to my attention the concluding words on that page that to expose the creditor (the Bank in this case) in addition to the other risks, to the ‘further risk of being bound by an adverse claim of which he had no notice when he advanced his money, and from which he would have been free if he had obtained registration, is in my judgment commercially unacceptable’.

121. To this argument Mr. Harris responded that, as the Policy Letter of 28<sup>th</sup> August, 1992, shows, the Security Interests (Guernsey) Law 1993 was specifically designed to protect people like Mr. Hammerschmidt, who in good faith, deposited his money in a reputable and internationally known Bank. It was of equal, if not greater, importance, Mr. Harris submitted, that investors should have confidence in the integrity of such institutions, and in particular, to know that if the Bank became aware of a fraud, it would take steps to protect the beneficial owners of funds and intangible property, and far more unacceptable if they did not do so.

122. What was Mr. Hammerschmidt to do to protect his interests if that integrity did not exist? It was impossible to give notice to the world at large but immediately he knew of the arrest of two of Ivyside’s directors he caused Boesebeck Droste to write to the Bank in terms which included the following:

“The purpose of this letter is to put you on notice and strongly urge you to refrain from disposing of any money presently standing to the credit of the above named [meaning Kells] ‘account.’”

123. What, on the other hand, did Barclays do? At most it had acquired an equitable interest in each case when it took its assignments under the First and Second Security Agreements of 20<sup>th</sup> January and 9<sup>th</sup> April, 1998. Mr. Harris urged that at those dates the Bank took *subject to* Mr. Hammerschmidt’s rights, as is pleaded at paragraph 2(d) of the Cause. The order of events was of huge importance in this case. He said that when it acquired the legal title Barclays were on notice—Boesebeck Droste’s letter of the 9<sup>th</sup> February, seeking, *inter alia*, full repayment of the funds invested by their client, *insofar as they are still in possession in Barclays Bank Plc*, made all the difference.

124. It is, of course, undisputed that the funds were at that moment in time still in possession of Barclays Plc—inasmuch as they represented the balance in the Accounts in Kells’ name which were maintained at the Bank. Did the Bank either then or at any antecedent or subsequent time, check the source of the funds, inasmuch as it must have been aware of the Law, since that was the statute enabling it to take the securities in the first place, and especially section 14(1)(d) thereof, and thus of the policy behind its enactment, as set out in the Policy Letter of August 1992? That policy was to protect investors by preventing people, especially Banks, from assigning, or giving a valid security over, or from causing the assignment or the giving of security over, something which did not belong to the assignor.

125. The answer, said Mr. Harris was emphatically in the negative. By a series of self-serving measures, which were, as alleged in paragraph 36 of the Cause, not only unconscionable but entirely inconsistent with its obligations towards depositors. When the respective loans were due for renewal in March, 1999, Barclays took the steps which are described, in Paragraphs 47.1 to 47.5 of the Defence. It issued formal demands for repayment of the monies due under the Security Agreements, from the principal debtor and the guarantor respectively, in the two letters of 26<sup>th</sup> March.

126. Barclays then, on 9<sup>th</sup> April, 1999, debited Kells' call account No. 88183777 (into which the sums in Account numbered 6130514 had been transferred—see paragraphs 21.2 and 28.2 of the Defence) with DM 5,006,540.70 and DM 9,413,046.70, being the principal and interest due under the respective loan agreements and then to transferred these amounts to itself, thus acquiring the legal title to those balances.

127. Mr. Harris challenged the correctness of the final paragraph of the Defendants' first Skeleton argument, of which I have set out an extract at paragraph 115 hereof. How could the acquisition of the legal interest in the currency deposit accounts by the Bank, when admittedly it had by then two months' notice (at least) of Mr. Hammerschmidt's equitable interest, relate back, as it were, in one instance a year, and in the other well over a year, to its acquisition of the equitable assignments when, for the purposes of this preliminary point, it had had no notice?

128. There were two essential distinctions, Mr. Harris submitted, between Dodds v. Hills and Macmillan Incorporated v. Bishopsgate on the one hand and the Bank's conduct in this case on the other. Mr. Edwards had made much of the fact that in the former case Smith took the legal title to the shares some five days *after* notice had been given to the plaintiff. But, said Mr. Harris, there no act other than Smith's act in registering himself had been necessary for him to acquire the legal title in Dodds v. Hills. As Millett J. said the *ratio* of that case was that Smith had been able to obtain the legal interest of the shares (and Millett J. emphasised this phrase) *without recourse to the legal owner*.

129. Here there was all the difference, as several acts other than by the security holder had occurred: for instance the defaults by Ivyside, and the non-compliance with the Bank's letters of 26<sup>th</sup> March, 1999, by Kells as guarantor, and, unlike Dodds' case the Bank had had to have recourse to the legal owner of the monies, meaning Kells. It could not become the legal owner of the monies from Day 1 as had happened in respect of Smith, let alone the fact that five days' lapse from the giving of the notice to the acquisition was hardly comparable to the periods just stated in paragraph 127 hereof.

130. Turning to Macmillan Incorporated v. Bishopsgate Mr. Harris argued that, given that his client was the *cestui que trust* under a constructive trust Kells, having committed breaches of trust by entering into the two Security Agreements and effecting the equitable assignments to Barclays, then committed further breaches of trust by its activities in March and April of 1999. Thus their conduct was directly contrary to this passage from Millett J. at page 1003C—D:

“.....the doctrine has never been applied where the owner of a later equitable interest acquires the legal estate from a person who commits a breach of trust by conveying it to him.”

Moreover, it is stated in Underhill & Hayton's Law Relating to Trusts and Trustees 16<sup>th</sup> Edition at page 1002:

“The *bona fide* purchaser of an equitable interest without notice of an express trust, cannot defend his position by subsequently, and after notice, getting in an outstanding legal estate *from the trustee*, for by doing so he would be guilty of taking part in a new breach of trust.”

131. My principal reservation regarding this portion of Millett J’s judgment is that he was dealing with the doctrine of *tabula in naufragio*, a species of tacking, the historical passage of which he had traced on the preceding page, and to which Page Wood V—C had referred in Dobbs v. Hills. This doctrine was introduced into the scales of the written submissions by paragraph 7 of the Defendant’s Skeleton argument of 1<sup>st</sup> December, 2004, and Mr.Harris devoted an entire section of his Supplemental Skeleton argument of the 22<sup>nd</sup> December in reply. Moreover, the principle stated in Underhill is in relation to an express trust, whereas the beneficial interest here was by virtue of an implied, constructive, trust.

132. *Tabula in naufragio* is the process by which a mortgagee may, by taking a further mortgage for a further advance on the same property, defeat the equitable claims of a mesne incumbrancer, that is, a person who has lent money on the property after the first but before the further mortgage. The tacking mortgagee gains this right by virtue of his title under the first mortgage, and by the operation of the rule that where the equities are equal the law shall prevail.

133. The limitations of this doctrine, and its abolition in relation to mortgages by the Law of Property Act 1925, were explained by Millett J. at page 1002. Mr. Harris has set out in some detail the reasons why he considers the doctrine cannot be applied in the instant case, and concentrates on the fact that it does not apply where the encumbrancer who gets in the legal estate as a result of a breach of trust in conveying it to him be the trustee, in this case Kells.

134. However, without disrespect to Counsel, who have both devoted much care to this question, there is a more fundamental reason why *Tabula in naufragio* is inappropriate here. The essence, as I understand it, of the doctrine was that it required the existence of an intervening equitable encumbrancer (i.e. one who intervened between the first and the third mortgages) who could, as it were be huffed by a later legal encumbrancer, provided the latter did not acquire his interest as a result of a breach of trust by the trustee. In those circumstances, in the words of Millett J. ‘the doctrine was a harsh one’ the result of which (in the example there given) ‘might be to squeeze B’ out altogether’.

135. As I understand the definition, *Tabula in naufragio* does not apply to a case where, as here, the person who later acquires the legal interest for value after having (as here) taken an equitable assignment can consolidate his two interests. Moreover in Macmillan Incorporated v. Bishopsgate at page 1004 F Millett J. says:

“It is true that Page Wood V—C based his decision on an imperfect analogy with the doctrine of tacking. ....and is best regarded as standing on an independent footing.”

136. It is important to remember that in that portion of his judgment Millett J. was dealing specifically with priorities relating to the those defendants in the Macmillan case who had either become holders of shares in a New York company known as Berlitz, or who had security interests in such shares, of which 1.9 million were held by the second defendant Shearson Lehman Bros. Holdings Plc, by way of the deposit of share certificates in London: it was thus an equitable interest. In due course the security was perfected by deposit in the Depository Trust Company, which operated the central depository system.

137. The day after the death of the late Robert Maxwell, Lehman Bros., prior to the plaintiff’s notification of its claim to the shares, were sold to Shearson Lehman, though not transferred to them until afterwards. Thus in both Dodds v. Hills and the relevant part of the Macmillan case, the Court was dealing with an equitable interest in shares in which the holder subsequently acquired the legal estate and no notice of any third party’s interest intervened between the two events.

138. It seems to me, although a deposit of shares is not involved in this case, that, unlike the imperfect analogy referred to by Millett J., that the Bank here was perfecting the

security it had previously taken, in each of the two sets of transactions, by getting in the legal estate. True, Ivyside and Kells were necessary participants in the process of getting in the legal estate, inasmuch as the appropriate letters of demand had to be sent to them, and default made, but they were purely passive participants.

139. As Millett J. said in relation to the case before him, this is a case of substitution of the security by the Bank. True again, Mr. Hammerschmidt is an innocent party who suffered by the activities of the fraudsters, but it was he, and not the Bank, that allowed the fraudsters to retain control of Kells. I find myself in agreement with Mr. Edwards that the Bank acted perfectly lawfully in following the instructions of the persons who were mandated to give, and to sign, those instructions.

140. I would therefore hold, subject to considering the effect of the Security Interests Law, that the Bank, in acquiring the legal estate to these accounts, was a purchaser for value of them without notice of the Plaintiff's prior equitable interest, because it had no such notice when executing the respective Security Agreements and taking the equitable assignments thereunder. How, then, does the 1993 Law impact on this situation?

141. Mr. Harris argues that for the limited purpose of establishing priority the Law requires the Court to disregard whatever security interest Barclays acquired and thus to treat his client's interest as having priority. I regret that I do not read Section 4(1), which is the provision dealing with priority between security in the same collateral, in this way. The collateral, under the definition of that term, means in each case the relevant treasury currency account in Kells' name. The debtor in each case was Kells. Under paragraph (d) of Section 14(1) the rights of any person (other than Kells), which would clearly also include Mr. Hammerschmidt, who had an interest in the collateral, at the time when Kells permitted the security interests to be created in that collateral are to be determined without regard to the law, meaning without regard to the order of priority stated in Section 4(1).

142. While I have taken into account Mr. Harris' submissions regarding paragraph 3.9 of the Policy Letter, I do not think it can control that which is, in my opinion, the plain meaning of section 14(1). It follows that, in answering the question posed by the Preliminary issue, I accept the Plaintiff's submissions that the rule in Dearle v. Hall does not apply in this case, and that consequently the equitable rule as to the first in time, as regards the equitable interests, would apply were it not for my conclusion on the second head of the submissions before the Court.

143. However, for the reasons herein appearing, I propose to follow the reasoning of Millett J. in Macmillan v. Bishopsgate at page 1004 G—H. Consequently I hold that the critical time for the issue of notice to be tested is when the Bank took the equitable assignments and not at the later time when it acquired the legal estate. I reject the Plaintiff's submissions to the contrary. Barclays was in my judgment a purchaser for value without notice in each instance.

144. In the result, to use the term employed for the final head of his judgment by Millett J. in the Macmillan v. Bishopsgate case, the outcome is that I answer the question in the Preliminary Issue thus:

“At the time Barclays enforced its securities under the First and Second Security Agreements, Mr Hammerschmidt's equitable interest in the subject matter of the said securities as a beneficiary under constructive trusts did not take priority over Barclays' interest in the same pursuant to its securities.”

;145. Subject to Counsel's views I propose to reserve the question of the costs hereof.

A.R.W.Hancox  
Lieutenant Bailiff  
3<sup>rd</sup> May 2005.