I

SINCLAIR v. *BROUGHAM*[1]

THE case of *Sinclair* v. *Brougham*[2] has been generally regarded as an authority of first-rate importance. I think it has been properly so regarded, though my reasons for so thinking may not altogether agree with the reasons emphasized by some lawyers. I regard the case as primarily significant as embodying the leading principles on which the Court acts in exercising its equitable jurisdiction to give relief in order to prevent unjust enrichment, or to achieve restitution, if we accept the useful term which has been employed in the recently published American Restatement of the Law of Restitution. The word itself is only an echo of language which will be found in English judgments, indeed, in this very case of *Sinclair* v. *Brougham*. The case shows how the Court can do justice by applying equitable principles where the common law would have been powerless. But since every Court is now bound in the same proceeding to apply either law or equity or both as the circumstances may require, the distinction between law and equity is now only important in the sense that the differences of method and rules must be observed. In the case we are considering a company had borrowed money for purposes for which it was *ultra vires* for it to borrow.

[1] An address to the Cambridge University Law Society, 26 November 1937. Published in 6 *Cambridge Law Journal* (1938), 305–326.
[2] [1914] A.C. 398.

There could in law be no claim for money lent and no claim in law for the repayment on the ground of quasi-contract or, to use the now obsolete phrase, contract "implied in law", because to allow such a claim as a merely money claim would be to sanction an evasion of the public policy forbidding *ultra vires* borrowing by companies. Further, as the money lent or its products could not be identified in the company's possessions, a claim in law could not be maintained. But the powers of the Court were not exhausted. The problem was further complicated by the conflicting claims of the shareholders. The moneys lent had become inextricably mingled with other moneys in the course of myriad transactions. The Court solved the difficulty by a sort of rough justice, in the form of a tracing order, so as (in the words of Lord Dunedin, at p. 437) "to give full effect to the doctrine of *ultra vires*—for the person receiving is not ordered to pay as a debt the equivalent of what he originally got, but ordered merely to surrender what he still has as a superfluity, an enrichment which, but for the original reception of the money, he would have been without". As I read the judgments, if the money borrowed had been either in the original form or its products, still capable of identification, the claim would have been properly brought as a claim in law. The aid of equitable principles had to be invoked because the identification had become impossible. It might also have been necessary to invoke the aid of equity on account of the company's insolvency to give the claimant the benefit of an equitable charge on the identifiable property or its products in the company's possession. The importance of the case is that it demonstrates a category of claims distinct from contract, or tort, or trust (express or resulting), the essential principle of which is that the defendant should not be unjustly enriched at the expense of the plaintiff. The test of recovery is not the loss to the plaintiff, but the gain to the defendant, though in general the loss fixes a limit. Emphasis is to be placed on the word "unjustly". There are many positions in which a defendant may be enriched at the expense of the plaintiff and yet it may not be unjust for him to retain that benefit. It is, therefore, important not merely to recognize the existence of this separate head in the law (in which word I include law and equity), but to enumerate, to classify and to distinguish as the American Restatement of the Law of Restitution has sought to do, the different positions which may arise, bringing into one conspectus both legal and equitable rights and remedies. The fundamental principle may also be stated in the words of Lord Parker (at p. 444), which are capable of being applied beyond the special facts of the case he was dealing with. "The equity lay in this that it would be unconscionable for the society to retain the amount by which its assets had been increased by and in fact still represented the borrowed money." This language may be compared with Baron Parke's expression in *Kelly* v. *Solari* (1841) 9 M. & W. 54 when speaking merely as a common lawyer of the right to recover money paid by mistake "it is against conscience to retain it" (at p. 58), which is explained by Lord Sumner as depending on the fact that the payer had no intention in such a case to enrich the payee. Whether the remedy given is legal or equitable or both, the underlying principle is the same. In this particular case, Lord Parker points out at the outset that it was already settled law that an *ultra vires* borrowing by a society does not give rise to indebtedness either at law or equity on the part of the society. But that forms merely the starting-point for the inquiry how justice may be done and unjust enrichment prevented. Incidentally that may be, as it was in this case, a very different thing, when looked at from the plaintiff's point of view, from complete restoration to him. The governing consideration is the superfluity in the defendant, which may differ from the expense to the plaintiff.

The facts of *Sinclair* v. *Brougham* were simple. The Birkbeck Building Society had no power to carry on a banking business. It did so, along with its legitimate business as a building society, and accepted large sums from depositors for the banking business. Thus there was borrowing which was *ultra vires*. Heavy losses were incurred and the society went into liquidation. Its assets were insufficient to meet the claims of the outside creditors, and to repay the shareholders and the depositors. It was conceded that the outside creditors came first. As to the depositors, as I have already said, their Lordships held they could not on the facts of the case claim to rank in law or equity as ordinary creditors. A conflict of claims arose as between shareholders and depositors. One possible view was that the shareholders were entitled in the liquidation to share in all the assets remaining after outside claims enforceable at law were paid, which would have given them five times the amounts of their subscriptions. But the assets beyond question represented in some part the sums which had been paid to the society by the depositors. These were many times larger in total amount than the share capital paid up by the shareholders. The House of Lords held that it would be unconscionable that the shareholders should be enriched at the expense of the depositors. As all the funds had been inextricably mingled together in the actual transactions of the society, it was impossible to identify in the assets found on liquidation in the society's possession what represented contributions which had come from the shareholders and what represented sums paid by depositors. Neither shareholders nor depositors could claim priority, as both sets of persons must equally be deemed to have been cognizant that the funds were being utilized to carry on the *ultra vires* business. It was held that justice could best be done by a rough sort of tracing order, which took the form of dividing up the assets which remained after paying outside creditors and preferred shareholders among all the claimants, shareholders and depositors, *pari passu*, in the proportions of the sums which they had severally contributed. If the net assets had been sufficient to repay all these claimants, the matter would have been simple. But there had been a loss. That loss, it was held, should be borne equally by those whose equities *inter se* were equal. The House of Lords reversed the Court of Appeal, who by a majority, Fletcher Moulton L.J. dissenting, had held that the shareholders were entitled to repayment in full. The decision of the Court of Appeal was clearly illogical, though apparently based on authority binding that Court. Logically the shareholders if entitled to priority would have been entitled to divide up all the remaining assets of the society. Fletcher Moulton L.J. held that the depositors were entitled to priority over the shareholders. The House of Lords, while agreeing with his reasoning up to a point, held that there was no ground for giving priority to depositors over shareholders, or shareholders over depositors.

There were four speeches delivered in the case in the House of Lords, two by equity lawyers, Lord Haldane (with whom Lord Atkinson agreed) and Lord Parker, one by Lord Dunedin, one by Lord Sumner. I shall deal first with the constructive portions of these judgments, in which the conclusion arrived at is justified. I shall later refer to the negative or critical portions, in which they deal with the matter, for them already a *chose jugée*, viz. that in the facts of the case there was not a debt either at law or in equity.

Of the four speeches, I have found those of Lord Parker and Lord Dunedin most illuminating. I shall primarily examine their reasoning, adding at times parallelisms from their colleagues, though the reasoning of all the Lords agrees in substance. I find in the speeches of Lord Parker and Lord Dunedin references more or less complete to almost every main principle of unjust enrichment or restitution, which latter term is actually used by Lord Dunedin. The most obvious and common claim in a case of unjust enrichment is in debt, but that is put aside as inapplicable in the facts of the case. I shall reserve that aspect for discussion later. But I may here observe that an action at law is recognized by the Lords to be competent even in cases of *ultra vires* loans, so long as the money lent or its products are identifiable. This is based on the doctrine of *Taylor* v. *Plumer* (1815) 3 M. & S. 562, an aspect which is more fully dealt with by Lord Haldane. When, however, identification ceases to be possible at law, then equity can still carry the matter farther, for instance, it can apply the principle of *Hallett's Case* (1880) 13 Ch.D. 696. In thus proceeding, equity imposes what has been usefully called a constructive trust, to distinguish it from an express or resulting trust. In an express or resulting trust there is an actual intention of the settlor to create a trust, the intention being either expressed or to be inferred from the facts of the case. Cases of that character where the trust depends on the intention of the settlor to create it are distinguishable from those trusts or rather quasi-trusts which are imposed by the Court in order to prevent unjust enrichment, and which are called constructive trusts because they do not arise from the intention of a settlor, but are declared by the Court *ab extra*, irrespective of actual intention. But there are cases in which equity cannot find a constructive trust of the property, because that property represents in part only the property which is the subject of the unjust enrichment. It is the product not of that property by itself, but of that property combined with the defendant's own property or with that of a third person. Equity in such cases gives a partial right, which has been called an equitable lien, on the total property to the extent that the total property represents the plaintiff's property. Lord Parker in one passage speaks of all these rights as being themselves a species of property which equity has created. In such cases there cannot in general be equitable property unless there is legal property in the defendant, only the equitable property being in the plaintiff, whereas in the *Taylor* v. *Plumer* type of case, the legal property remains in the plaintiff. When the property has passed in law to the defendant, the plaintiff can only claim as beneficial owner in equity of the property, claiming either on the ground of a constructive trust when the whole property is the product of the plaintiff's property, or on the ground of an equitable lien when the property is only in part the product of the plaintiff's property. The extent to which the Court may carry this equity is strikingly illustrated by the tracing order in *Sinclair* v. *Brougham*, where the properties of two sets of claimants had, as already stated, become inextricably mingled as the result of an immense number of separate transactions over many years, so that only the roughest apportionment of the residual property could be attempted. But in effect each individual claimant was given an equitable lien in his proper proportion. Lord Sumner seeks to illustrate what was done by the analogy of a familiar case at common law where material chattels, bales of cotton, belonging to different owners, had become mixed up in a ship's hold as the result of a maritime casualty, and had become incapable of identification because the marks indicating ownership had become obliterated. The Court held in that case that the several shippers or consignees were tenants in common of the indiscriminate bulk. It is a similar principle which equity applies in the more esoteric atmosphere of financial transactions. But the point here to be noted is that equity does not stop where law must do. It will follow the plaintiff's property up to the ultimate limit of its identification in any form or in any amalgam, even into the hands of third persons, so long as they are not purchasers for value without notice, and even as against persons who have no higher title in equity than the original transferee, such as his ordinary creditors or his trustee in bankruptcy. I may here note the third or alternative form of relief which may in proper cases be given, that is, where a person's money has been used to discharge the obligations of the recipient, but where the person can have no direct recovery as for a debt. An illustration of such a case is where money has been borrowed *ultra vires*. This third method is also noted by the Lords in *Sinclair* v. *Brougham*, and is described as subrogation. The *ultra vires* lender (if he may be so called) is put to stand in the shoes of the borrower's creditor, at least as regards the personal debt. In that way, it is said, the *ultra vires* borrower's total indebtedness is not increased, but unjust enrichment is at least in part obviated. Lord Parker put another case somewhat analogous, namely, where money borrowed to the lender's knowledge for an illegitimate purpose has been in fact used for a legitimate purpose in whole, or in part, and he indicates his view that such money would be recoverable as a debt though the borrowing was *ultra vires*. It was strongly urged in *Sinclair* v. *Brougham* that in the facts of that case subrogation was the utmost and only remedy that equity could give. It would have assuredly been futile since in the inextricable flood of transactions no depositor could have shown that his money had been used to pay any particular debt of the society. But no such limitation on the powers of the Court in equity was admitted. Lord Dunedin is particularly instructive on this aspect. After adducing parallels from Roman law and from Pothier, he went on to say (at p. 435): "I have made these citations to show that other great systems of law have not been unable to solve the problem arising where the equity of restitution comes in contact with the doctrine of nullity of contract. Is English equity to retire defeated from the task which other systems of equity have conquered? Let us for a moment examine what the argument on the other side is. There being no contract, it is impossible, it is said, to have any obligation on the part of the society to restore what it has taken from the depositors. The only right of the depositors is a right to vindicate property, or, in other words, when you have a *ius in re* you can enforce it; but if the thing has so disappeared that a *ius in re* is no longer to be found (and this must practically always be so in the case of money), then your remedy is gone. The sole relief which equity can give is that if you can show that your money has paid a just debt, in that case you shall have action. This comes to this, that having got hold of property which does not belong to you, if only you are wise or lucky enough to change its form you may enjoy the proceeds unmolested. Such a plea on the face of it seems only worthy of the Pharisee who shook himself free of his natural obligations by saying Corban. In the words of technical equity it is unconscionable." A little later (at p. 436) he proceeds: "But further, the whole strength of this argument lies in the idea that the *ius in re* represents the depositors' only right: that there can be no obligation on the other side at all. It is here that I think the importance of the action for money had and received comes in. That cannot be founded on a *ius in re*, for you cannot have a *ius in re* in currency. It shows that both an action founded on a *ius in re*, such as an action to get back a specific chattel, and an action for money had and received are just different forms of working out the higher equity that no one has a right to keep either property or the proceeds of property which does not belong