1. Do the differences between common law and equitable tracing make any sense nowadays?

Suggested Answer

There have always been historical differences between common law and equity as described in Chapter 1, so it is not surprising that there are different rules and procedures for common law and equitable tracing. See 16.1 and 16.2. Common law, being older, originally concentrated on the recovery of a physical object, such as a bag of gold. Equity allowed recovery of any kind of property, including intangible property.

Despite this, the distinction between common law and equity has become blurred. *Taylor v Plumer* 3 M & S 562 accepted that it was possible to trace at common law, even if the property changed its form. Later, it was even accepted, in *Banque Belge pour L'Etranger v Hambrouck* [1921] 1 KB 32, that it was possible to trace money into a bank account. This is despite the fact that one sum of money is indistinguishable from another sum of money and that money in a bank account has no physical existence. It is just a debt that the bank owes to the customer. At that point though, common law hesitated and would not allow tracing, when the property sought had been mixed with other property.

Both types of tracing allow the claimant to take an increase of value in their property. Common law allowed this in *Jones (FC) & Sons v Jones* [1996] 3 WLR 703 and equity and finally allowed this in *Foskett v McKeown* [2001] 1 AC 102 (See 16.3.6). Both systems base this conclusion on a theory of property rights. If you use my property to make money, that profit is mine.

Both common law and equity allow the bone fide purchaser for value without notice to defeat a tracing claim. The rule is explained by Lord Millett in *Foskett v McKeown* [2001] 1 AC 102 (See 16.4,1), but also appears in the common law case *Banque Belge pour L'Etranger v Hambrouck* [1921] 1 KB 32 (See 16.3.2).

Despite these similarities, some fundamental differences remain. Only equity allows tracing into a mixed fund and only in equity is a fiduciary relationship required before tracing is permitted: *Re Diplock* [1948] Ch 465 (See 16.3.1).

Academic writers, led by Professor Birks, have explained that tracing is just about evidence and the ability to identify property. Therefore, the same rules should apply and there should not be both common law and equitable tracing. The problem of whether equity or common law should apply only arises when deciding upon the remedy. These ideas were endorsed by the House of Lords in *Foskett v McKeown* [2001] 1 AC 102, but the House felt unable to apply these principles and change the law in that particular case.

FURTHER READING: G. Virgo ‘Vindicating vindication: *Foskett v McKeown* reviewed’ in New Perspectives in Property Law, Obligations and Restitution, Editor A.S. Hudson (2003 London, Cavendish).
P. Millett ‘Tracing as the Proceeds of Fraud’ (1991) 107 LQR 71.

2. Is the rule in *Clayton’s Case* a rule of law or just a rule of convenience?

Suggested Answer
See 16.3.6
The original *Clayton’s Case, Devaynes v Noble* (1816) 1 Mer 572, [1814-1832] ER Rep 1, concerned the collapse of Barings Bank and whether customers could recover money that had been in their bank accounts. So originally, the rule did not have much to do with tracing, but since that case, it has generally been applied when two or more rival claimants trace into the same bank account. The operation of this rule can seem unfair. Just because your money was stolen and paid into the account on 1 June, why should it be assumed that it is your money leaving the account when a debit is made on 3 June? However, the whole concept of tracing money is a little strange, as money has no physical existence in a bank account and one sum of £1000 is indistinguishable from another sum of £1000. Be that as it may, the idea of tracing money into a bank account has long been accepted (*Banque Belge pour L’Etranger v Hambrouck* [1921] 1 KB 32) and the rule in *Clayton’s Case* is often applied.

Barlow Clowes International Ltd v Vaughan [1992] 4 All ER 22 sought to limit this rule, by applying a different approach to a common pool of investors. The court prefers to share out what was left in proportion to what had been taken from each investor. The Court of Appeal endorsed the rule in *Clayton's Case*, but only for active current accounts. Oliver LJ explained this at 33: "None the less the decisions of this Court, in my judgment, establish and recognise a general rule of practice that *Clayton's Case* is to be applied when several beneficiaries’ moneys have been blended in one bank account and there is a deficiency." Thereby future courts are invited to depart from this rule in all other situations.

FURTHER READING: M.Pawlowski ‘The Demise of the rule in Clayton’s case’ [2003] Conveyancer 339.

3. Should a tracing claimant be able to claim part of the increased value of a mixed fund?

Suggested Answer
See 16.3.7
This is really a question about whether the decision in *Foskett v McKeown* [2001] 1 AC 102 is correct. Should a tracing claimant be able to claim a proportionate part of the increased value of a mixed fund? The principle that this was possible was recognised some time before in *Re Tilley’s Will Trusts* [1967] Ch 1179. This was explained by Ungoed-Thomas at 1189: "where the asset is purchased by a trustee in

part out of his own money and in part out of the trust money [the claimant] may, if he wishes, require the asset to be treated as trust property with regard to that proportion of it which the trust moneys contributed to its purchase." There was, however, a finding of fact in that case that the defendant had not used the beneficiaries' property to make their profits.
Therefore the claimants were not entitled to any share of those profits, but just to a return of the money originally taken from them. In *Foskett v McKeown*, the majority thought that the defendant had used claimants' property to secure their profit. Some of the investors' money had been used to pay insurance premiums, so part of the insurance pay-out belonged to them. The judgments asserted the importance of property rights. If you use my property to make a profit, you have to return that profit together with my property. In contrast, the dissenting judges did not think that the property of the claimants had been used to obtain a profit. So the claimants were only entitled to the return of their property and not to share in the profits, here the insurance pay-out.

The decision of the majority is controversial, because it seems to go beyond mere restitution, restoring what the claimant has lost. The judges were insistent that it is not wrong for the claimants to enjoy "a windfall" or to secure the "winning lottery ticket", when someone else had taken their property and used it to make a profit.

FURTHER READING: G. Virgo 'Vindicating vindication: *Foskett v McKeown* reviewed' in New Perspectives in Property Law, Obligations and Restitution, Editor A.S. Hudson (2003 London, Cavendish).

4. Should innocent volunteers, who have done no wrong, be forced to hand back trust property?

Suggested Answer
See 16.4
The classic explanation of how volunteers should be treated can be found in *Re Diplock* [1948] Ch. 465. Charities had mistakenly been given the money by a trust, which they had to return to the beneficiaries of that trust. That equity will not assist a volunteer is a basic principle of this area of law and can be found amongst the equitable maxims in Chapter 1, at 1.12. If someone has given no consideration, there is not a binding contract and a promise is unenforceable. The same principle is also encountered at 7.4.1, where if there is a voluntary transfer to another, that other must return the property on the basis of resulting trust. The logic behind this is that they have done nothing in return for the gift and therefore have no right to keep it. There seems to be a hard-nosed business principle behind this, if someone has got something for nothing, why should it be unfair to have to return it to the rightful owner? A good example is the children in *Foskett v McKeown* [2001] 1 AC 102. They had done nothing in return for the insurance pay-out, whereas the investors had had their property stolen by the father of the children. The investors had the more deserving claim.

In tracing, the rule is not always as harsh as it might seem. In *Re Diplock* [1948] Ch. 465, some of the defendants had innocently mixed the trust money with their own.

They did not have to return the whole fund, but could keep the proportion that represented their own money. Only wrongdoers, defendants who knew that they had taken trust money, are bound to return their own money as well: *In re Hallett's Estate* (1879-80) LR 13 Ch.D 696. *Re Diplock* did not demand the return of money from volunteers where it was impossible to do so. In that case, the money had been used to build hospitals. This change of position defence seemed to be endorsed in *Lipkin Gorman v Karpnale* [1991] 2 AC 548, but rejected in *Foskett v McKeown.*
Whether this defence is allowed, ina tracing claim is therefore debatable, but if we return to *Diplock*, equity always has discretion on what remedy it awards and the judges may choose not to enforce the tracing claim.