Neutral Citation Number: [2023] EWHC 121 (Ch)

Claim No.: PT-2022-000059

IN THE HIGH COURT OF JUSTICE

BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES

PROPERTY, TRUSTS AND PROBATE LIST (ChD)

Rolls Building
7 Rolls Buildings
Fetter Lane
London
EC4A 1NL

Date: 6 February 2023

Before :

DEPUTY MASTER DRAY

- -

Between :

MICHAEL LEON

Claimant

- and –

(1) KENSINGTON MORTGAGE COMPANY LIMITED

(2) THE MAYOR AND BURGESSES OF THE CITY OF WESTMINSTER **Defendants**

- -
- -

Niraj Modha (instructed by Anthony Gold Solicitors LLP) for the **Claimant**
Clifford Payton (instructed by TLT LLP) for the **First Defendant**
Gerard van Tonder (instructed by Bi-Borough Shared Legal Services) for the **Second Defendant**

Hearing date: 12 December 2022

Further written submissions received on 20, 22 & 30 December 2022

- - - - - - - - - - - - - - - - - - - -

Approved Judgment

This judgment was handed down remotely by circulation to the parties or their representatives by email and by release to the National Archives.
The date and time for hand-down is deemed to be 10.30am on 6 February 2023.

DEPUTY MASTER DRAY:

Introduction

1. Somewhat simplified, the root issues in this case are:
   (1) Where A and B are co-debtors and the creditor C holds security over A's property in respect of the debt, if A is dissolved and the Crown disclaims the property, is B (upon later payment of the debt in full to C) entitled to be subrogated to C's security?
   (2) If 'yes' to (1), where following such dissolution and disclaimer C has been granted a vesting order in respect of A's property, if B is entitled to be subrogated to the property so vested, i.e. does that property constitute C's security?

2. For the reasons given below I answer both questions in the affirmative.

The background

3. Frinton Limited (**Frinton**) was a company incorporated on 28.4.1999 and owned or controlled by the Claimant, Mr Leon, or his wife. All its shares were held by him or on his behalf. He was at one time a director of Frinton.

4. On 21.10.2002 Frinton and Mr Leon jointly entered into a loan agreement with IGroup Mortgages Limited whereby the lender loaned them the sum of £472,500 (the **Loan**). The term of the Loan was 25 years. The Loan carried interest payable monthly at 0.75% over base rate. The liability of Frinton and Mr Leon for the Loan was joint and several; they were co-debtors.

5. The Loan was secured by a contemporaneous charge by way of legal mortgage (the **Mortgage**). The property charged was 86 Flanders Road, London W4 1NG.

6. In the Mortgage Frinton was identified as the mortgagor and Mr Leon as the co-mortgagor. In addition to the charge effected by Frinton, the Mortgage provided that Mr Leon charged any right or interest which he had in the subject property or its proceeds of sale which was not charged by Frinton.

7. Condition 11 of the Mortgage provided that conditions 4-10 thereof applied to Mr Leon in the same way that they applied to the mortgagor. Condition 4 was that the mortgagor must keep to the terms of any lease under which the property was held.

8. In 2007 Frinton took an assignment of a lease (the **Lease**) of the basement floor flat at 122a Westbourne Terrace, London W2 6QJ (the **Property**). The Lease was granted by the freeholder, the Second Defendant (**Westminster**), and is for a term of 125 years from 10.10.1988. It is registered at HMLR under title no. NGL713746 (the **Title**).

9. On 26.3.2007 Frinton, Mr Leon and GE Money Mortgages Limited (as IGroup Mortgages Limited was then known) (**GE Money**) entered a deed of substituted security (the **Deed**). By the Deed the Lease was substituted as security for the Mortgage in place of the property at 86 Flanders Road, on the terms of the Mortgage.

10. The effect of the Deed was to charge the Lease held by Frinton in favour of GE Money. So far as Mr Leon was concerned, he had no right or interest in the Lease and hence the further charge expressed to be made by him (see paragraph 6 above) had no bite; it would have bitten only if he had any such right or interest (which he did not). However, he remained bound by the Mortgage conditions.

11. The charge in favour of GE Money (the **Charge**) was registered against the Title with effect from 27.3.2007.

12. On 17.2.2009 Frinton was dissolved because of its failure to comply with its statutory filing requirements. No application for its restoration was made within the 6 year period set by s.1024 of the Companies Act 2006 (the **2006 Act**).

13. By s.1012 of the 2006 Act, on the dissolution of Frinton the Lease vested in the Crown *bona vacantia*.

14. On 23.5.2016 GE Money transferred the Charge over the Lease to the First Defendant (**KMC**). In the same month KMC was registered as the proprietor of the Charge on the Title in place of GE Money.

15. On 30.8.2016 the Crown, having then recently learned of the dissolution of Frinton, disclaimed the Lease pursuant to s.1013 of the 2006 Act.

16. By s.1014 of the 2006 Act, the consequence of the disclaimer was that the Lease was deemed not to have vested in the Crown under s.1012. By s.1015 the disclaimer operated to terminate, as from the date of the disclaimer, the rights, interests and liabilities of Frinton in the Lease but did not, except so far as was necessary to release Frinton from such liability, affect the rights or liabilities of any other person.

17. HMLR made an entry on the Title which recorded the disclaimer.

18. The open market value of the disclaimed Lease was then put around £800,000 to £1 million. Hence, even after deducting the outstanding Loan, there was roughly £370,000 to £570,000 residual equity in the Lease. I understand that, if the Lease were now sold, there would still be residual equity, i.e. a surplus (the **Surplus**).

19. Mr Leon's liability under the Mortgage was unaffected by the disclaimer of the Lease. It is common ground that he remained (and remains) liable to repay the sums secured by the Mortgage.

The previous proceedings

20. On 5.5.2017 Mr Leon brought proceedings seeking a vesting order in respect of the Lease.

(1) First instance

21. The claim was heard by Chief Master Marsh. His judgment, delivered on 11.12.2017, bears the neutral citation [2017] EWHC 3148 (Ch).

22. Mr Leon claimed that the Lease had been held by Frinton on trust for him. The Chief Master rejected that contention and it is unnecessary to say anything more about it.

23. However, the Chief Master upheld Mr Leon's claim for a vesting order under s.1017 of the 2006 Act.

24. Thereafter, on 27.7.2018 HMLR registered Mr Leon as the proprietor of the Lease in place of the erstwhile Frinton.

25. The Charge in favour of KMC remained registered against the Title.

26. The Lease which, following the disclaimer, had been in what might be described as a state of suspended animation, was thereby revived and vested in Mr Leon.

(2) First appeal

27. Matters did not end there. Westminster appealed against the decision of the Chief Master. On the appeal Arnold J (as he then was) set aside the vesting order made by the Chief Master. He held that Mr Leon was not entitled to a vesting order under the 2006 Act. His judgment, delivered on 12.11.2018, bears the neutral citation [2018] EWHC 3026 (Ch).

28. Arnold J held (paragraph [28]) that although Mr Leon would have had the right to redeem the Mortgage by paying off the debt, he did not own the equity of the redemption in the Lease. That had belonged to Frinton until its dissolution and then to the Crown until the disclaimer. Hence Mr Leon did not have an interest which entitled him to the Lease under s.1017(2)(a) of the 2006 Act.

29. Arnold J further held (paragraphs [34-37]) that, although Mr Leon was under a liability in respect of the Lease by reason of the Mortgage conditions, thereby bringing him within s.1017(2)(b) of the 2006 Act, it was not just to vest the Lease in Mr Leon in order to compensate him in respect of the disclaimer. That was because Mr Leon had not lost the Lease (it never having been his) and, as above, his liability under the Mortgage was unaffected by the disclaimer. Therefore, this gateway to a vesting order was denied by s.1017(3) of the 2006 Act.

30. It was common ground between the parties that, in those circumstances, a vesting order should be made in favour of KMC on terms that it should account as mortgagee to the person next entitled in accordance with s.105 of the Law of Property Act 1925 (the **1925 Act**), whoever that might be. The identity of such person (i.e. the person entitled to the Surplus) was not determined, although Arnold J observed (paragraphs [32] & [38]) – echoing the observations of Chief Master Marsh in paragraph [50] of his judgment – that it was far from clear that Westminster would be entitled to the Surplus if KMC sold the Lease.

31. Accordingly, by his order sealed on 7.12.2018 (the **Vesting Order**) Arnold J ordered that:
    (1) The property comprised in the Lease be vested in KMC pursuant to s.1017 of the 2006 Act for such term and upon such conditions as the said Lease to the intent that KMC would be in the same position as it would be if it were an assignee of the Lease. (paragraph 3)
    (2) The proprietorship register of the Title be amended by the removal of Mr Leon as proprietor and the entry of KMC as proprietor in his place. (paragraph 4)
    (3) Upon subsequent sale by KMC of the property thereby vested, KMC be liable to account as mortgagee to the person next entitled in accordance with s.105 of the 1925 Act. (paragraph 5)

(3) Second appeal

32. Mr Leon appealed unsuccessfully to the Court of Appeal whose judgment, dated 22.11.2019, bears the neutral citation [2019] EWCA Civ 2047.

33. For Mr Leon it was submitted that he had an entitlement to the equity of redemption in the Lease. In rejecting this argument David Richards LJ (who gave the only substantive judgment, with which Lewison and Simon LJJ agreed) said (at paragraph [29]):

> "… [counsel] relied on the right of Mr Leon, as co-debtor with Frinton, to pay the outstanding loan and thereby redeem the Mortgage. [Counsel] submitted that the equity of redemption is the right, on payment of the mortgage debt, to recover the property. This, however, is to confuse the right of the mortgagor of the property, or of a co-debtor or a surety … to redeem a mortgage with the equity of redemption. As it is put in Megarry & Wade, The Law of Real Property, 9th ed., 2019, at 23-108, the mortgagor's equity of redemption is "an interest in the land which includes the right to redeem it, but is much more than a mere right of redemption". If a surety redeems a mortgage, the property does not thereby become the property of the surety. The most that the surety may gain by way of a proprietary interest is subrogation to the rights of the mortgagee. The surety has no interest in the mortgaged unless and until the surety redeems the mortgage. It would in this case be open to Mr Leon to repay the Loan in accordance with its terms and thereby be subrogated to [KMC's] rights, entitling him to sell the Lease, but, like the order under appeal, that would leave open the question of who should receive the surplus."

34. David Richards LJ thus concluded (at paragraph [38]), in agreement with Arnold J, that Mr Leon had no interest in the Lease which entitled him to it.

35. David Richards LJ then went on (paragraph [49]) to agree with Arnold J that a vesting order was not required in order to compensate Mr Leon for any loss arising by virtue of the disclaimer of the Lease.

36. Mr Leon's appeal was therefore dismissed. The outcome was that the Vesting Order made by Arnold J stood.

37. As David Richards LJ observed (at paragraphs [47] & [50]):
    (1) The Vesting Order made in favour of KMC meant that it would obtain no benefit beyond its security interest.

(2) Mr Leon was not deprived of protection as regards the liabilities he owed to KMC as mortgagee since the vesting order in KMC's favour would enable it to realise its security in the event of any default and the value of the Lease meant that KMC would be fully recouped from the proceeds of sale.

Subsequent events

38. Following the decision of the Court of Appeal HMLR implemented the order of Arnold J and with effect from 21.9.2020 KMC was registered as the proprietor of the Lease. Its registered Charge also remains on the Title.

The present position as a result of the previous proceedings

39. As noted above, the vesting of the Lease in KMC was conditional in that, as per s.1017(4) of the 2006 Act (which entitles the court to make a vesting order on such terms as it thinks fit), KMC is only entitled to apply the proceeds of sale in discharge of its costs, charges and expenses and the Mortgage debt and is bound to pay the residue (i.e. the Surplus) to the person entitled to the mortgaged property, pursuant to s.105 of the 1925 Act.

40. Who is the person next entitled, i.e. entitled to the Surplus that would result if the Property were sold by KMC, has not been determined; the point was not live in the previous proceedings and (as above) the Court of Appeal expressly left it open. The current position is that there is thus something of a vacuum. Someone must surely be entitled to the Surplus in that event but who that might be is not at all clear:
    (1) Mr Leon, never having owned the Property, is not an obvious candidate.
    (2) KMC disavows any interest in the Surplus: see e.g. paragraph 17 of its evidence. It is merely interested in recovering the Mortgage debt, i.e. what is due to it under the Loan. It suggests that Mr Leon and Westminster are the two rival claimants for the Surplus.
    (3) Westminster asserts a claim to the Surplus but has not clearly articulated its basis. Further, the basis is not immediately obvious and its claim was judicially doubted in the previous proceedings: see paragraph 30 above.
    (4) Insofar as the Crown acquired the equity of redemption on the dissolution of Frinton (see *Re Wells* [1933] 1 Ch 29, CA), it relinquished the same when it disclaimed the Lease: see also paragraph [28] of Arnold J's judgment.

41. The mystery as to the ultimate destination of the Surplus will remain unresolved whatever my decision because the issue is not live in these proceedings either and I have not been invited to determine it, even if that were possible or appropriate in the circumstances. Consequently, who may receive the Surplus in the future is an issue which remains at large.

42. No doubt, if KMC were to sell the Lease, in practice it would pay the Surplus into court. Indeed, this is KMC's position in its evidence in these proceedings (paragraph 6).

43. For the avoidance of doubt, the foregoing is not to say that the Lease itself was vested in KMC otherwise than fully. Plainly, KMC has complete ownership (both legal and equitable) of the Lease; if the position were otherwise, any purchaser from it could not acquire full ownership in the event of a sale.

Recent developments

44. Nothing in the Vesting Order obliged KMC to sell the Lease, and to date it has not done so. Up to the date of Arnold J's judgment Mr Leon had kept up the payments due under the Mortgage and KMC had no desire to realise its security (see paragraph [34] of Arnold J's judgment). Indeed, Mr Leon had made the Mortgage payments from 2009 onwards, although he was not necessarily out of pocket because I understand that he had received the rental income from the Property (see paragraph [36] of Arnold J's judgment).

45. I understand that, from around June 2021, KMC has refused to accept payments from Mr Leon, for reasons which are not clear to me, and around that time it refunded to Mr Leon all payments made by him after 7.12.2018 (the date of the Vesting Order).

46. This state of affairs has coincided with a desire on the part of KMC to sell the Lease; it has marketed the Property and received two offers (£825,000 and £900,000) although the Property has been withdrawn from sale pending the conclusion of these proceedings.

47. I understand that the current debt under the Loan and secured by the Mortgage is in the region of £500,000 and that the current value of the Property (said to be depressed by virtue of its poor condition) is not less than £825,000 (and according to Mr Leon may be as much

as £1.5 million); so on any view there remains considerable equity in the Lease and, as above, a Surplus will be generated if the Property were now sold by KMC.

48. Faced with the prospect of a sale of the Property to a third party, Mr Leon has considered repaying the Loan. With that in mind he has asked KMC to confirm that, if he did so, it would assign to him both the Lease and the Charge. KMC has refused to give that confirmation. In correspondence it has accepted that, if Mr Leon satisfied the Loan, he would be entitled to be subrogated to the rights of KMC as mortgagee and, as such, to an assignment of the Charge, either by virtue of the equitable doctrine of subrogation or pursuant to s.5 of the Mercantile Law Amendment Law 1856 (the **1856 Act**). However, it has denied that he would be entitled to an assignment of the Lease.

49. KMC's stance prompted Mr Leon to bring the present proceedings.

The present proceedings

50. By the amended Part 8 claim form Mr Leon asserts that upon redemption of the Mortgage KMC is bound to transfer the Lease to him. He relies specifically on s.5 of the 1856 Act. He seeks associated declaratory and injunctive relief.

51. Mr Leon has yet to repay the Loan, and I infer that he is refraining from so doing pending the (positive) outcome of this litigation. However, as outlined above, he seeks the court's determination as to his rights and entitlements in the event that he should pay off the Loan.

52. Although it was suggested during oral argument that in the circumstances the dispute before me is hypothetical (or the qualified relief now sought by Mr Leon – as to which see paragraph 57 below – pointless), I am not persuaded that that is the case. In my judgment, at the very least Mr Leon – whose evidence (paragraph 23) is that he wishes to redeem the Mortgage – genuinely wants (and, I consider, is properly entitled) to know what the position would be vis-à-vis the ownership of the Lease in the event that he were to repay the Loan, in order that he may make a fully informed decision in that regard. I consider that the dispute is real, not hypothetical, even though it concerns specific future events which may not necessarily come to pass.

53. It is evident from Mr Leon's evidence (paragraphs 22 & 25) that he instigated the present proceedings with a view to obtaining the Surplus in the Property (as part and parcel of the overall value of the Lease). This appears from the following paragraphs in his witness statement:
    (1) "… once the mortgage [is] redeemed … it must be right to assign the ownership of the Property to me on the basis that *I alone am entitled to the equity in the property*." (paragraph 22) (emphasis supplied)
    (2) "[KMC has] said they will sell the Lease …. and have indicated that it will not account to me … *for the balance of the sale proceeds*." (paragraph 25) (emphasis supplied)

54. Mr Leon's rationale for this litigation vividly illustrates that the unresolved issue as to the entitlement to the Surplus is the elephant in the room, for, as indicated, it appears that these proceedings were brought by Mr Leon with the hope of engineering for himself (if successful) a position whereby, through prima facie unqualified ownership of the Lease, he would be entitled to the Surplus.

55. I formed the provisional view that, besides the obviously flawed proposition that Mr Leon is currently entitled to any (still less all) of the equity in the Property (flawed because he never had any interest in the Property at the outset and in the light of his failure to obtain a vesting order), Mr Leon was seemingly seeking to obtain (by the back door route of the now claimed subrogation) that which the Court of Appeal denied him (through the front door of his failed claim for a vesting order), namely outright ownership of the Lease (including the Surplus on any sale). To my mind, it looked as if Mr Leon was impermissibly seeking to sidestep the limitation/condition in respect of the Surplus imposed on KMC by the Vesting Order, and effectively to claim the Surplus for himself – despite the entitlement to the Surplus never having been determined.

56. Therefore at the hearing I questioned how Mr Leon, advancing a claim to subrogation the very essence of which was said to put him in the shoes of KMC, could properly end up in a materially different and better position vis-à-vis the Surplus than KMC. That struck me as directly contrary to the position envisaged by the Court of Appeal where David Richards LJ stated at paragraph [29] that if Mr Leon were subrogated to KMC's rights "that would leave open the question of who should receive the Surplus".

57. The result of the exchange was a concession on behalf of Mr Leon that, if successful in his subrogation claim, he would not object to being subjected to a similar limitation as that which currently binds KMC by virtue of the terms of the Vesting Order.

58. For its part though, Westminster advocated that such concession was not satisfactory or sufficient because, if he acquired the Lease, Mr Leon might (for instance) simply hold the same without ever selling it. It was submitted (although the point had never been pleaded) that the court should not countenance that scenario and that, if subrogation to the Lease were permitted, Mr Leon should be subjected to an injunction requiring its sale.

59. Mr Leon strongly resisted any notion that, if his claim were successful and if the Lease were vested in him following payment of the Loan, he should be compelled to realise its value; it was contended that, like KMC, he should not be bound to sell the Property.

60. I recognise the possibility that, if successful in these proceedings and if he took an assignment of the Lease, Mr Leon might potentially retain the Property indefinitely. I remark that such possibility might perhaps be reduced in practice if there were certainty as to the ownership of the Surplus and thus an active claimant for the same (who might keep Mr Leon 'honest' accordingly). However, it strikes me that the arguably unsatisfactory position which might so result is not that dissimilar from the current position in which KMC holds the Lease and in which it has (and asserts) no entitlement to the Surplus and yet is not bound to, or (in the light of its ability to pursue Mr Leon for repayment of the Loan) necessarily even under any particular commercial pressure to, effect any sale of the Property.

61. To my mind, the position is really just an inherent facet of the fact that the entitlement to, and ultimate destination of, the Surplus has yet to be resolved. In the circumstances I do not consider that, even if there is power/a discretion for the court so to refuse subrogation, the foregoing constitutes a reason to deny Mr Leon subrogation to the Lease if he would otherwise be so entitled (whether pursuant to the 1856 Act or in equity).

Subrogation and the 1856 Act

62. The principles of subrogation are not in dispute between the parties. However, their application and effect in the present case is.

63. Subrogation is widely available in equity on the ground of secondary liability: see e.g. *Goff & Jones, The Law of Restitution,* 10th ed., para.39-27. The classic example is a surety who discharges the principal debtor's liability by paying the creditor. In such a case the surety has a personal claim for reimbursement (i.e. right of indemnity or recoupment)) against the principal debtor but also, and as a supplementary measure for obtaining reimbursement, a right to be subrogated to any security interest held by the creditor for the principal debtor's discharged debt: *ibid.* and see *Craythorne v Swinburne (1807) 14 Ves. Jun. 160, 169*; *Hodgson v Shaw (1834) 3 My. & K. 183, 190.* The surety has the right to stand in the shoes of the creditor in enforcing the principal obligation of the debtor and the right to any securities held by the creditor in respect of the principal obligation and any rights and remedies which the creditor enjoyed prior to the performance of the principal obligation.

64. The right to subrogation rests upon the surety's equity not to have the whole burden of debt thrown on them by the creditor's choice not to resort to other remedies available to it: *Rowlatt on Principal and Surety*, 6th ed., para.7-27.

65. The right to subrogation applies whether or not the surety knew of the existence of the security when giving its guarantee and applies to securities taken by the creditor after as well as before the guarantee: *Forbes v Jackson* (1882) 19 Ch D 615.

66. A like position applies where one of co-sureties or co-debtors discharges the entire debt (i.e. more than their share of the same); that person can recover a contribution from the other co-sureties or co-debtors in respect of any excess paid over their share of the liability, and also succeeds to securities held by the creditor: *op. cit.*, para.7-45 and see *Duncan, Fox & Co v North and South Wales Bank* (1880) 6 App Cas 1, 19.

67. Section 5 of the 1856 Act reads:

A surety who discharges the liability to be entitled to assignment of all securities held by the creditor.

> Every person who, being surety for the debt or duty of another, or being liable with another for any debt or duty, shall pay such debt or perform such duty, shall be entitled to have assigned to him, or to a trustee for him, every judgment, specialty, or other security which shall be held by the creditor in respect of such debt or duty, whether such judgment, specialty, or other security shall or shall not be deemed at law to have been satisfied by the payment of the debt or performance of the duty, and such person shall be entitled to stand in the place of the creditor, and to use all the remedies, and, if need be, and upon a proper indemnity, to use the name of the creditor, in any action or other proceeding, at law or in equity, in order to obtain from the principal debtor, or any co-surety, co-contractor, or co-debtor, as the case may be, indemnification for the advances made and loss sustained by the person who shall have so paid such debt or performed such duty, and such payment or performance so made by such surety shall not be pleadable in bar of any such action or other proceeding by him: Provided always, that no co-surety, co-contractor, or co-debtor shall be entitled to recover from any other co-surety, co-contractor, or co-debtor, by the means aforesaid, more than the just proportion to which, as between those parties themselves, such last-mentioned person shall be justly liable.

68. The section effectively gives that person to be treated as a statutory assignee of the creditor, and places them, on payment of the debt, in the same position as the creditor: see e.g. *Chitty on Contracts, 33rd ed*., paras.47-150 & 47-151.

69. The section was introduced to overcome what was considered to be the logical problem that, on payment by the surety, the principal debtor's debt was discharged and the creditor's rights thereby extinguished: *ibid*. This is reflected in the statutory words, "whether such judgment … shall or shall not be deemed at law to have been satisfied by the payment of the debt …".

70. In fact, that problem probably did not actually exist, since for the purpose of protecting the surety, the guaranteed debt is considered, by a legal fiction, notionally to remain in force

and any securities are likewise deemed to continue notwithstanding the discharge of the debt: see e.g. *Goff & Jones*, para.39-05 and following, citing *Banque Financière de la Cité v Parc (Battersea) Ltd* [1991] 1 AC 221, HL (explaining that the extinction of the creditor's rights does not prevent subrogation taking place).

71. Nonetheless, the statute undoubtedly reinforces the basic right of the surety or (as here) co-debtor to the creditor's securities in the event of discharge of the relevant debt in full.

The parties' original positions

Mr Leon

72. Mr Leon's pleaded case and his stance at the hearing, reflected in his counsel's skeleton argument, was that on redemption he is entitled to be subrogated to all of KMC's rights against Frinton, including to the Lease.

73. I interject that this may give rise to an issue as to what, if any, rights KMC retains against Frinton following its dissolution and the disclaimer: see further below. Nonetheless, Mr Leon's position is clear: he claims to be entitled (on redemption) to an assignment of the Lease notwithstanding the dissolution of Frinton on the basis that (so he asserts) the Lease (along with the Charge) is security for the debt payable under the Loan.

74. Mr Leon primarily advances his case based on the 1856 Act. However, if and insofar as is necessary, he also relies on the general law of subrogation.

75. At this point I reiterate that (as per paragraph 57 above) at the hearing it was accepted on behalf of Mr Leon, following the points I had raised, that – on the basis that subrogation entails (in a case such as this) a person standing in the shoes of the creditor whose debt the person has paid – Mr Leon can, after redemption of the Mortgage, be in no better a position than KMC and hence will similarly be bound to account to the person next entitled (whoever that might be) in the event of a sale of the Property, i.e. that Mr Leon will not (by dint of any subrogation alone) be entitled to the Surplus for himself.

KMC

76. KMC's stated concern is solely to recover the money owed to it; as per paragraph 40 above, it is not concerned with the destination of the Surplus following sale. However, since there are two rival claimants to the Lease (or its proceeds of sale), namely Mr Leon and Westminster, KMC feels that it cannot agree to any arrangement that might leave it open to challenge in advance of a decision by the court. In that context KMC's initial position was to admit a limited right of subrogation. It accepted that on redemption Mr Leon will be entitled to be subrogated to its rights, including its power to sell the Lease as conferred by the Charge. However, it denied that Mr Leon would be entitled to acquire the Lease, for it maintains that the Lease is not security for the Loan debt.

77. As pleaded in its answer to the claim, KMC's position was:
    (1) The Lease vested in it is not itself security for the performance of any obligations of Mr Leon or Frinton. (paragraph 4)
    (2) The security held by KMC is the Mortgage, not the Lease. (paragraph 7)
    (3) Mr Leon is not entitled to redeem the Mortgage, a position said to be supported by paragraph [29] of the Court of Appeal's judgment (as to which see paragraph 33 above). (paragraphs 5 & 7)
    (4) Mr Leon is not entitled to the relief claimed. (paragraph 11)

78. At the hearing KMC confirmed that its position is in fact that Mr Leon *is* entitled to redeem the Mortgage, i.e. to repay the Loan, but it maintained that any consequential subrogation would see him entitled only to a transfer of the Charge and not the Lease on the basis that KMC's security is said to be the Charge alone.

79. So far as KMC's acceptance that Mr Leon can redeem the Mortgage is concerned, I believe that the concession is plainly correct. The pleaded denial, and KMC's original reliance in that regard on paragraph 29 of the Court of Appeal's judgment, is unsustainable and, to my mind, is the confused product of the failure to distinguish, as the Court of Appeal there did, between the right of a surety or co-debtor to redeem a mortgage (i.e. to repay the debt) – a right which *is* available to Mr Leon – with the equity of redemption, namely the interest of the owner of a property which is subject to a mortgage – which entitlement is <u>not</u> held by

Mr Leon because he was, despite the label of "co-mortgagor", never the owner/mortgagor of the Property.

Westminster

80. Westminster's pleaded case is broadly similar to that of KMC. It too maintains that Mr Leon has no entitlement to demand the transfer of the Lease upon payment of the Mortgage debt. (paragraph 13).

The issues raised by the court

81. At the hearing, I questioned whether subrogation (whether in equity or under the 1856 Act) is in fact available *at all* in a case where the principal debtor or, as the case may be (as in this case), one or two co-debtors has been dissolved, and hence whether it is available to Mr Leon following the dissolution of Frinton and the disclaimer of the Lease.

82. My query stemmed from doubt as to whether, in the light of the dissolution of the Frinton and the disclaimer, it can properly be said (either for subrogation purposes or at all) that:
    (1) Mr Leon remains a *co*-debtor *with Frinton* (which has ceased to exist and shoulders no liability for the Loan), and hence whether e.g. s.5 of the 1856 Act is or can be engaged. In other words, whether a person can properly be regarded as the surety for the debt of another, or jointly liable with that other, where that other has been dissolved and its liability for the debt extinguished.
    (2) Mr Leon can, on repaying the Loan, be entitled to a contribution or indemnity against (the non-existent) Frinton. In other words, whether a surety (or co-debtor) can have a right of recourse (either for an indemnity or contribution for a just proportion, as applicable) against a non-existent legal person.
    (3) KMC in fact retains any rights against Frinton to which Mr Leon can, on satisfying the debt, be subrogated (whether under s.5 of the 1856 Act or at all). In other words, whether a creditor can be regarded as having:
        a. Any ongoing rights and remedies against the principal debtor or a co-debtor; and/or
        b. Any security in respect of the principal (or co-) debtor's debt (to which security the surety or other co-debtor might in turn be subrogated),

    where such person has ceased to exist and its personal liability has been extinguished.

83. Counsel had not anticipated these issues and their oral submissions were thus limited. Therefore after the hearing I invited further written submissions. All parties provided such submissions.

The parties' revised positions

Mr Leon

84. Mr Leon's core position remained broadly unchanged. He now accepts that he has, and can have, no *in personam* claim for an indemnity or contribution against the dissolved Frinton. However, he contends that, that apart, the dissolution is immaterial so far as his entitlement to subrogation to KMC's security is concerned. I examine below his submissions in this regard.

The defendants

85. By contrast, the defendants' position regarding Mr Leon's entitlement to subrogation has materially shifted in the light of the issues I flagged, as I next outline.

KMC

86. KMC has changed course. It now contends that the continued existence (or otherwise) of the principal/co-debtor *is* material. Moreover, as I understand its argument, it submits that because of the dissolution of Frinton *any* (and all) rights of subrogation that Mr Leon might otherwise have had have been lost. Specifically, it maintains that: (a) Frinton cannot now bear any liability to Mr Leon (and so Mr Leon can have no recourse against Frinton); (b) the essence of a security is to secure payment of an enforceable debt; (c) following redemption, if the security held by KMC (i.e. the Charge) were assigned to Mr Leon, it would have no value in the hands of Mr Leon because there is (and would be) no debt owed by Frinton to Mr Leon, and thus the Charge would liable to immediate discharge (for it would secure nothing). It seeks to reinforce its argument by reference to the second limb of s.5 of the 1856 Act which indicates the purpose of subrogation is to enable the subrogated party to obtain indemnification from the principal or other co-debtor (as the case may be). Its essential point is that, as acknowledged by Mr Leon, he can no longer have any direct claim against Frinton. That being so, it contends that subrogation is precluded.

Westminster

87. Westminster also now adopts a similar stance. It maintains that because KMC has no ongoing rights against Frinton (save that it retains its security for the Loan) in turn there is nothing to which Mr Leon could be subrogated. It says that the fact of Frinton's dissolution renders the possibility of subrogation academic. Mr Leon cannot stand in KMC's shoes vis-à-vis Frinton because KMC itself has no rights against the erstwhile entity.

Analysis

(1) Can there be *any* right to subrogation following the dissolution of Frinton?

88. I consider that whether subrogation is available in a case such as this where a co-debtor has been dissolved (and, to compound matters, there has been a disclaimer of its interest in the particular asset said by the subrogation claimant to be available to it if it repays the debt) is a difficult issue. The very dissolution of the co-debtor (Frinton) renders the position messy and gives rise to conceptual issues along the lines outlined in paragraph 82 above.

89. Counsel told me that, so far as they are aware, there is no authority on the point. Therefore, it falls me to me to determine whether, and if so to what extent, subrogation is available in this case based on consideration of the competing arguments and the relevant factors.

90. Mr Leon submits that he "was (*and still is) jointly* liable for the same debt *owed by Frinton* and himself" (emphasis supplied). I have difficulty with, and indeed am unable to accept, that submission, so far as it uses the present tense and relates to the current time, given the dissolution of Frinton. Indeed, the same submission goes on to state that, since Frinton's dissolution "Mr Leon remains *the sole person* under the … obligations" owed to KMC pursuant to the Mortgage. This appears, in my view, to be inconsistent with the preceding passage and, in my judgment, is the more accurate statement of the two. Moreover, Mr Leon's acknowledgment that he can have no *in personam* right of indemnity or contribution against Frinton seems to me rightly to reflect the undoubted reality of the situation, which is that, by virtue of its dissolution, Frinton can shoulder no financial liability to Mr Leon (or, for that, matter to KMC or anyone else).

91. It follows that, strictly speaking, I do not believe that it can be said that Mr Leon now *remains* (present tense) a co-debtor with Frinton in respect of the Loan. The debt pursuant

to the Loan is now Mr Leon's alone. Frinton, having been dissolved, neither has a legal existence nor any longer owes the debt.

92. Mr Leon submits that subrogation is designed to prevent or reverse unjust enrichment. I do not question that as a general principle. However, it is unfortunate that Mr Leon's submissions do not clearly identify who would allegedly be unjustly enriched if the claimed (or any) subrogation were denied in the present case.

93. In the vanilla case of a principal and surety, or co-debtors, where both such persons remain in existence and liable to the creditor (whether on a primary or secondary basis), it is not at all difficult to see that, upon discharge of the debt by the surety or one of the co-debtors, which entails the payer either bearing the debt owed by the principal (in the case of a surety) or more than its aliquot share (in the case of a co-debtor), the person unjustly enriched in the absence of subrogation will be the non-paying principal or co-debtor. However, that cannot be the case here, for (as above) Frinton, having been dissolved, does not exist and is not liable for the Loan and thus cannot be enriched by Mr Leon's repayment of it.

94. Neither can it readily be said that KMC would be unjustly enriched by reason of Mr Leon's repayment of the Loan alone. Mr Leon is, after all, liable to KMC in that regard. KMC would receive from Mr Leon only that payment to which it is entitled.

95. Less clear, though, is whether KMC could be said to be unjustly enriched at the expense of Mr Leon if it were to retain its security in respect of the Property (whatever that be, although all parties concur that it extends to the Charge at least) following repayment of the Loan by Mr Leon.

96. On the one hand, that might indeed be said to be so, despite the fact that (if it elected to sell the Property) KMC would effectively be bound to pay the Surplus (which in that event would constitute the entire proceeds of sale) into court, bearing in mind that (as it submits) KMC is not prima facie compellable to sell.

97. On the other hand, in view of the fact that (as above) KMC has, and Mr Leon can have, no direct recourse against Frinton, and given that (to my mind) an underlying function of

subrogation in a case where a surety or co-debtor has paid off the relevant debt is to enable the subrogated party to recover an indemnity, or as the case may be, a contribution from the principal or co-debtor (as reflected in the second limb of s.5 of the 1856 Act), it may be said that the inability to achieve this purpose connotes that subrogation is not available in a setting where the principal or co-debtor has ceased to exist.

98. Mr Leon further contends that the result of subrogation is that the subrogated party steps into the shoes of the creditor who has been repaid. The argument proceeds that, although there is no longer any available *in personam* claim against the dissolved party (Frinton), nonetheless (as is common ground between the parties) KMC holds security (the Charge at the very least) in respect of the Loan and that, accordingly, on redemption Mr Leon should be entitled to an assignment of that security. This is said to be supported by the first limb of s.5 of the 1856 Act which, where applicable, mandates the assignment of any security held by the creditor in respect of the satisfied debt. A wrinkle in this argument though is the fact that, as noted above, s.5 prima facie bites in a case where there is an extant principal or co-debtor whose debt the subrogated party (the surety or other co-debtor) discharges; where that is no longer the case (even though it once was) it is at least open to doubt whether s.5 (and, for that matter, the equitable principles of subrogation more generally) is (are) actually engaged.

99. In addition, Mr Leon submits that, just as the insolvency of a principal debtor has no effect on a surety/co-debtor's rights of subrogation (*Andrews and Millett, Law of Guarantees*, 7th ed., para.11-027), the position is likewise in the case of dissolution of the principal debtor. It is said that a surety's or co-debtor's right to subrogation is unaffected by the dissolution of the principal debtor or the other co-debtor because if the position were otherwise it would yield an unfair result which would work to the prejudice of the paying surety or co-debtor and would differ materially from the position which would obtain if the debt happened to be discharged while the principal debtor was in an insolvency process (before dissolution). It is submitted that such a difference of outcome, potentially depending on the chance of relative timings (payment versus dissolution) cannot be justified. No authority was cited for this proposition of equivalence, however.

100. I observe that: (a) there is a real legal distinction between a company in liquidation and a company which has been dissolved and no longer has any legal existence; (b) subrogation is no doubt a remedy designed to achieve a just outcome but, whilst a relevant consideration, perceived fairness of outcome cannot alone be the touchstone; there must be a principled and explicable basis for the availability of the remedy in any given case.

101. As I have said, the position is not straightforward. However, having reflected on the competing arguments (and notwithstanding my rejection of, and doubts in relation to, certain limbs of Mr Leon's arguments), I have ultimately concluded that the better view is that, in a case such as the present, subrogation (both in equity and also under the 1856 Act) *is* available in favour of the person who pays off the relevant debt which is the subject of the security held by the creditor, notwithstanding the dissolution of the original principal debtor/co-debtor and the associated consequence that neither the creditor nor the subrogated paying party any longer has any *in personam* rights enforceable against the dissolved entity.

102. In this regard I consider that the overall position of Mr Leon is to be preferred to that of KMC and Westminster, and I consider that the original stances of KMC and Westminster, which recognised an enduring (albeit, they asserted, limited) subrogation right, were sound and are to be preferred to their more recently modified positions.

103. Hence, in my judgment, if Mr Leon satisfies the Loan in full he will be entitled to an assignment of whatever security is held by KMC in that regard. My reasons for this conclusion are as follows.

104. Firstly, although KMC has (by reason of Frinton's dissolution) lost its *in personam* rights against Frinton and is unable now to sue the now non-existent Frinton, KMC has nonetheless retained security for the Loan despite the dissolution and the ensuing disclaimer of the Lease by the Crown. This is common ground even though the extent of KMC's security (considered below) is disputed.

105. For what it is worth, I consider that this consensus is correct. It is borne out by the following:

(1) In *Hindcastle Ltd v Barbara Attenborough Associates Ltd* [1997] AC 70, HL it was held that, in a case involving third party rights, the disclaimer of a lease (under the Insolvency Act 1986, the relevant provisions of which are essentially the same as those in the 2006 Act) – although freeing the tenant from liability under the lease – does not affect the interests of third parties, such as a sub-tenant or, in my judgment, a mortgagee. The third party's interest continues notwithstanding the disclaimer, as it would if the disclaimed lease continued – subject always to the right of the superior landlord to forfeit the disclaimed lease and to any application for a vesting order.

(2) Moreover, in the case of a disclaimer of freehold land following the dissolution of a company (resulting in escheat), although the escheat determines the freehold estate, it does not terminate derivative interests such as mortgages: *Scmlla Properties Ltd v Gesso Properties (BVI) Ltd* [1995] BCC 73; *Pennistone Holdings Ltd v Rock Ferry Waterfront Trust* [2021] EWCA Civ 1029 at [22]. I see no reason why, even leaving aside *Hindcastle*, a different result should obtain in the case of the disclaimer of a lease formerly held by a dissolved company (albeit that there is no escheat in the case of a leasehold estate).

106. Secondly, the initial security (the Charge), which charge remains extant and on the Title, was over the property of Frinton, then a co-debtor along with Mr Leon.

107. Thirdly, I do not conceive that KMC's security would have lapsed on the dissolution of Frinton or by reason of the disclaimer *even if* the Loan had been solely owed by Frinton (as opposed to a joint debt for which Mr Leon was/is also liable). As above, escheat and disclaimer do not end the proprietary rights of third parties who hold derivative interests. This being so, I consider that KMC's security can (despite the dissolution of Frinton) properly be regarded as ongoing security for the debt originally generated by Frinton (in this case together with Mr Leon), even though no personal claim now lies against Frinton.

108. Fourthly, I consider that the key purpose of subrogation is to enable the subrogated party to obtain recompense for its outlay (or, as the case may be, excess of outlay) including (where applicable) through enforcement of any security held by the creditor. Just as the creditor can use such security to recover what is owed to it notwithstanding the dissolution of the debtor (including, as above, where there never was a surety or co-debtor), just so the

subrogated party can use the same security to recover what is owed to it, again despite such dissolution.

109. Fifthly, it is in my judgment extreme and untenable for KMC and Westminster now to contend that Mr Leon could not obtain even the Charge by subrogation. The initial stance of both parties was that Mr Leon would be able to acquire the Charge and, with it, the ability to sell the Lease (via the mortgagee's statutory power of sale). Now, in a marked reversal of position, it is said by them that the security would have no value and so be nugatory, thus impliedly precluding, or at least negating the meaningful benefit of, *any* subrogation.

110. As it is, the essence of subrogation in both principal/surety and co-debtor cases is that subrogated paying party acquires the very security formerly held by the creditor in respect of the debt in question, irrespective of whether the same is deemed to have been satisfied, i.e. *as if* the debt remained: see paragraph 70 above. That must, at the very least, surely include the Charge in this case.

111. I also do not accept that any security which might now be obtained by Mr Leon would be valueless (in the sense that it could not secure anything). Just as, in my judgment, a creditor's security is not denuded of worth if a sole debtor is dissolved, so too as regards the subrogated security in a case where a surety or co-debtor is involved.

112. In addition, I do not believe that it is material whether the amount which the surety or a co-debtor might be able to claim against the principal debtor (but for its dissolution) is the same as the sum which was secured for the creditor by the relevant security, or whether it is a different sum. That there may be a distinction is evident from the terms of s.5 of the 1856 Act which provides that an object of subrogation is to enable the recovery of advances to and losses sustained by the surety or a co-debtor and which is subject to the express proviso that the co-surety may only recover a just proportion; any such proportion will invariably be less than the whole debt which was secured for the creditor.

113. Additionally, in my view it makes no material difference whether the dissolution occurs before or after satisfaction of the debt by the surety or co-debtor and the consequential subrogation of that party to the security held by the creditor.

114. My thinking may be explained by the following scenarios:

(1) Suppose that A (alone) owes £100 to C. C has the benefit of a charge over A's property by way of security. A is dissolved. C's charge survives and it continues to serve as security for the £100, even though following A's dissolution C cannot sue A for the sum. This is the point made in paragraph 107 above.

(2) Next suppose that B is a co-debtor along with A in respect of the £100. Each owes C the full sum, i.e. joint and several liability. As between A and B, however, the liability to contribute is fixed at 50/50. C again has the benefit of a charge over A's property by way of security. The charge secures the total £100 debt. Posit that B pays off the entire debt. B is thereupon subrogated to C's charge, even though in B's hands the charge secures only the £50 just proportion which A is liable to reimburse him. This is the point made in paragraph 112 above.

(3) As in (2) above, but after the payment by B, A is then dissolved. Just like C's position in (1), B's ability to enforce the subrogated charge in order to recover the £50 is unimpeached (despite B, like C in (1), having lost the right to sue A). This is the point made in paragraph 111 above.

(4) Now suppose that the situation is as above except that A is dissolved *before* B pays off the debt. Once again, C's security does not cease and it remains extant in respect of the full £100, despite C having lost the right to sue A for the money; the retention of the security is in no way dependent on the happenstance that B is a co-debtor. The dissolution of A (and B, if also dissolved) will similarly not affect the C's charge. This is the point made in paragraph 104 above.

115. Can it be, however, that, because of the *intervening* dissolution of A, B is disqualified, on its *subsequent* payment of the £100 debt, from being subrogated to C's preserved security in order to recoup the £50 owed by A to it (but for A's dissolution)? In my judgment, that is not the result of the dissolution of A.

116. I consider the defendants' argument that B's subrogated charge would secure nothing in that scenario to be fallacious. Just as C's charge remains, in my judgment, fully effective security and does not cease to have any meaningful content or value in the light of A's dissolution, the same goes for B's subrogated charge in like circumstances. In both instances the charge is to be taken to secure such sum as *would have been* payable by A had it not been dissolved and its *personal* liability for the debt thereby extinguished. The sum secured by the charge (whether held by C or B) is unaffected by the dissolution; it is to be assessed (pursuant to the loan agreement, the contribution agreement or the applicable legal principles, as the case may be) *as if* A had remained in existence.

117. Sixthly, even though, in a case like the present, Mr Leon cannot have *in personam* rights against Frinton, nonetheless that is not a sufficient reason to deny subrogation, and in particular that element of subrogation which focuses on the assignment of the proprietary rights held by the creditor as security; to my mind, there is no conceptual reason why Mr Leon cannot step into the shoes of KMC, and inherit a like status so far as holding the security over the Property is concerned.

118. Seventhly, it would be most quirky if different outcomes might occur depending on what course of action KMC chose to take:

(1) On the one hand, KMC might elect, rather than looking to Mr Leon for payment of the Loan, to sell the Property and to recoup what it was owed from the proceeds. In that event Mr Leon would not in practice fund any share of the debt.

(2) Alternatively, KMC might decide to pursue Mr Leon for payment and Mr Leon might then satisfy the debt. Yet, if subrogation to KMC's security were not available to Mr Leon (in the light of the dissolution of Frinton), Mr Leon would be left high and dry, i.e. out of pocket and with no means of recourse to recover his expenditure (or, as the case might be, a due share thereof) from the Property.

119. In my view, the law should not readily countenance such a difference of outcome (which would be subject to the whims of the creditor and/or the timing of when the surety/co-debtor happened to satisfy the debt relative to any sale of the property) unless compelled to do so, and I am not persuaded that the law drives me to such an unattractive result. The

outcome noted in paragraph 118(2) above would run contrary to the rationale for subrogation noted in paragraph 64 above.

120. Eighthly, I am fortified in reaching my decision by the dicta of the Court of Appeal in paragraph [29] of its judgment. It is true that the issue of subrogation and s.5 of the 1856 Act were not directly before the court in the previous proceedings and that the court was not expressly addressed on the consequences of the dissolution of Frinton on any entitlement of Mr Leon to subrogation. Nonetheless, the considered view of the Court of the Appeal that Mr Leon would be entitled to repay the Loan and thereby be subrogated to KMC's rights is plainly of considerable weight.

121. The fundamental purpose of subrogation (both in equity and under the 1856 Act) is to enable a surety/co-debtor to stand in the shoes of the creditor in respect of the security held by the creditor prior to payment of the debt by that person. That being so, for the above reasons I believe that, in a case where the principal debtor/other co-debtor has been dissolved, the equitable doctrine is engaged and a purposive reading of s.5 is warranted, so that where (as here) the creditor retains a security for the debt notwithstanding the dissolution, the surety/co-debtor is entitled (on discharge of the debt) to be subrogated thereto.

122. I believe that this is achieved by regarding a case involving a dissolution as one in which, for the purposes of protecting the surety/co-debtor, the debt is considered notionally to remain extant and owed by the dissolved company notwithstanding the dissolution, in much the same way that the 1856 Act expressly directs that it is immaterial that the relevant debt may have been satisfied by the payment made by the surety/co-debtor. In other words, for the purposes of subrogation, one is to regard the position *as if* the dissolved company subsisted and remained a co-debtor; there is a hypothetical deeming: see paragraph 70 above. Irrespective of the dissolution the security is kept alive for the benefit of the paying party and, upon payment, transferred to it.

123. In my view, subrogation (in the event that Mr Leon repays the Loan in full) is justified in the present case because otherwise KMC will indeed be unjustly enriched at the expense of Mr Leon: see paragraphs 96 and 118/119 above. Such enrichment would occur even

though KMC's hands would be tied by the condition imposed by the Vesting Order in the event of any sale of the Property by it because (absent subrogation) Mr Leon would be denied the ability to recover his overpaid share of the Loan from the Property.

124. Consequently, in my judgment the equitable principles of subrogation apply in the present case and so too does the 1856 Act, which I regard as operative in a case like this (where a person was jointly liable with another for a debt immediately before that other's dissolution) as if the dissolution had not happened.

125. Therefore, I hold that, if he repays the Loan in full, Mr Leon will be entitled to be subrogated to the security held by KMC, and that the realisation of such security will in turn enable Mr Leon to recover from the Property such proportion of the Loan as he would have been entitled to claim from Frinton if Frinton had not been dissolved.

126. It is not for me in these proceedings to determine what that sum is (an exercise which may well have to take into account the fact that Mr Leon has been renting the Property and thereby deriving value from it) and I acknowledge that the process of quantification (i.e. the requisite accounting process) may be complicated and even somewhat artificial in the absence of Frinton, but in my judgment such practical impediments do not undermine the basic entitlement of Mr Leon to subrogation.

(2) What is the security held by KMC to which Mr Leon would be subrogated?

127. The remaining question is that which has divided the parties from the outset, namely the extent of KMC's security and hence the extent of any subrogation which Mr Leon might obtain.

128. As indicated above, the dispute is whether the relevant security held by KMC for the Loan is just the Charge or is also the Lease.

129. On this I consider that Mr Leon again has the better of the argument.

130. It is true that originally the sole security held by KMC was the Charge. However, I consider that matters altered when the Vesting Order was made in KMC's favour. In that regard I believe that the following points are material.

131. One. KMC was only entitled to the Vesting Order in respect of the Lease by reason of it having an interest in the disclaimed property, i.e. by reason of its security in the form of the Charge: s.1017 of the 2006 Act.

132. Two. The Vesting Order was evidently granted because of a concern that, absent any vesting order, KMC's security under the Charge would be lost: see the judgment of Arnold J at [34].

133. Three. In the circumstances the Vesting Order was clearly made in KMC's favour *as mortgagee:* see the judgment of the Court of Appeal at [47].

134. Four. The clear intention underlying the grant of the Vesting Order to KMC was that the Lease would represent (substituted) security for KMC in respect of the Loan. This appears from paragraph [50] of the judgment of the Court of Appeal: "The vesting order in [KMC's] favour will enable it to realise *its security* in the event of any default and the value of the Lease is such that it will be fully recouped out of the proceeds of sale." (emphasis supplied).

135. Five. The fact that the Vesting Order in respect of the Lease was granted by way of security (and no more) to KMC as mortgagee is underscored by the fact that, as noted, the Vesting Order was expressly made on terms that KMC was to account *as mortgagee* to the person next entitled under section 105 of the 1925 Act (which is, in terms, directly applicable to a sale by a mortgagee). The Court of Appeal observed at paragraph [47] that "[KMC] would accordingly obtain no benefit [from the Vesting Order] beyond its security interest."

136. Six. If (contrary to the above) the Lease were not regarded as part of KMC's security (albeit a security conferred by the court following the dissolution of KMC and the disclaimer), a strange and unsatisfactory position would result if Mr Leon repaid the Loan. In that scenario the Charge would be redeemed but, without more (and absent subrogation),

KMC would nonetheless remain the owner of the Lease despite it having been fully repaid. It would hold the Lease indefinitely but as essentially an empty shell in the sense that if it ever sold the same it would have to account to whoever might be next in line for the entire proceeds of sale. KMC's counsel stated that he doubted that in that event KMC would wish to retain the Lease and he accepted that KMC would be in an "uncomfortable position". I do not believe that such an outcome is what the courts in the previous proceedings can possibly have had in mind.

137. For KMC it was submitted, with reference to *Smith v Retail Money Market Limited* [2019] EWHC 2771 (Ch), itself citing *Bristol Airport v Powdrill* [1990] Ch 744, that a real security comprises only: (a) a mortgage; (b) a pledge and possessory lease; (c) a charge and non-possessory lien, and that the Lease (unlike the Charge) therefore cannot be security.

138. I disagree. I see no reason why, in an appropriate case, a lease may not properly be regarded as security.

139. In argument I gave the following example. Suppose a person has a mortgage over a lease. The lease is forfeited by the landlord. The mortgagee obtains relief from forfeiture under s.146(4) of the 1925 Act. This takes effect by way of vesting order, vesting a new lease in the mortgagee. The old lease is gone, as is the mortgage over it. In such a case it is established that the new lease is held by the mortgagee as substituted security and the mortgagor has the right to redeem that security notwithstanding the forfeiture of the original lease: *Chelsea Estates Investment Trust Co v Marche* [1955] Ch 328. Counsel did not present a convincing answer to the fact that this clearly demonstrates that, as a matter of principle, a lease may itself be security in some circumstances.

140. In the present case the lease vested in KMC pursuant to the Vesting Order is the original (disclaimed) Lease rather than a new lease. However, I do not consider that the fact that the Lease was effectively resurrected rather than replaced by an equivalent interest alters the above analysis.

141. What is more, in *Bristol Airport* Sir Nicholas Browne-Wilkinson V-C approved the following description of a security: "Security is created where a person (the 'creditor') to

whom an obligation is owed by another ('the debtor') … obtains rights exercisable against some property … in order to enforce the discharge of the debtor's obligation to the creditor." In my judgment, the Vesting Order in respect of the Lease in this case broadly fits that description. As explained above, it was made in favour of KMC to make good its security and in order to enable it to enforce against the Property the discharge of the debt owed to it.

142. As Mr Leon puts it in his witness statement (paragraph 23), "[KMC] does not have proprietorship for the Lease for its own sake or benefit. Its only interest in the Property is to hold the Lease as security for repayment of the Loan that is secured against the Property." I agree.

Result

143. Consequently, I shall declare that if Mr Leon should repay the Loan, he will be entitled to be subrogated to KMC's interest in the Lease, and to the assignment thereof, on terms that he is to account to the person next entitled in accordance with s.105 of the 1925 Act, as if he were a mortgagee (and so in a position akin to that of KMC).

144. In this way the Lease will, in the hands of Mr Leon, represent security for such sum, if any, as (following his repayment of the Loan) he would be entitled to receive by way of contribution from Frinton but for Frinton's dissolution. As the Court of Appeal previously noted in paragraph [29] of its judgment, that will (continue to) leave open the question of who should receive the Surplus in the event of any sale of the Property.

145. In the circumstances I do not believe that any injunctive relief is necessary or appropriate. It is clear that KMC and Westminster will abide by the court's decision. There is no basis for an injunction.

146. I invite counsel to agree and CE-file a draft order reflecting my judgment (which order I anticipate will contain a provision mirroring paragraph 5 of the Vesting Order, *mutatis mutandis*) and also dealing with the question of costs, and to do so by 4pm on 13 February 2023. If the parties are unable to reach agreement in any respect they should provide brief

submissions dealing with the outstanding matters by the same time, after which I will make any necessary further decisions.