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The case for tracing forward not backward through an overdraft

David Wilde*

Abstract

This article suggests that there is a respectable argument—contrary to generally held views—that equity can *often* trace through an overdrawn bank account, on general principle. But the direction of that tracing would be *forward* (as normal with tracing); not backward (the unconventional direction usually associated with potential tracing through overdrafts).

Introduction

This article considers the case for a revised understanding of equity's tracing rules in relation to overdrafts.¹ When wrongdoers, on misapplying money in breach of trust or breach of fiduciary duty, pay it into an overdrawn bank account, or a bank account that subsequently becomes overdrawn, it is established that, in general at least, the money is no longer traceable. And there is substantial authority endorsing this familiar proposition. For example, the House of Lords has pronounced that²: 'the moneys in [a] mixed bank account ... ceased to be traceable when the ... account went into overdraft ...'

However, it is widely recognised that this general rule *may* be subject to qualification. The leading English authority on the possibility of tracing through overdrafts is *Bishopsgate Investment Management Ltd v Homan*.³ The Court of Appeal held that occupational pension trust money improperly paid into bank accounts of the employers, which were overdrawn or later became overdrawn, could indeed not be traced—at least on the information before the court. But the divided court left open the possibility that tracing through an overdraft may *sometimes* be possible. Dillon LJ thought so; but Leggatt LJ disagreed; while Henry LJ merely concurred with both judgments.

It is well known that Dillon LJ left open the possibility of so-called 'backward tracing' through an overdraft. What is less noted—but may be worthy of greater note—is that he also mentioned the possibility of conventional *forward* tracing through an overdraft. It is *this* suggestion that will be examined here. Most of the major textbooks are so focused on backward tracing—or perhaps so sceptical about the possibility of forward tracing—that they simply omit to mention that Dillon LJ suggested the possibility of forward tracing through an overdraft.⁴ But a few textbooks are open to the idea of forward tracing, although none gives the

*David Wilde, Associate Professor of Law, University of Reading, School of Law. E-mail: d.c.wilde@reading.ac.uk.

1. Referring to 'equity's tracing rules' is not intended to endorse the view that the common law's rules should be understood as different—it is simply a recognition that they are generally said to be different.

2. *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] AC 669 (HL), 706 (Lord Browne-Wilkinson, delivering the leading judgment).

3. [1995] Ch 211 (CA). (Leave to appeal to the House of Lords was refused: [1995] 1 WLR 31.)

4. For example, only Dillon LJ's comments on backward tracing are mentioned in the discussion of *Bishopsgate v Homan* by one major practitioner text: P Matthews, C Mitchell, J Harris, and S Agnew (eds), *Underhill and Hayton Law Relating to Trusts and Trustees* (20th edn, LexisNexis 2022), para 94.42. Likewise recent specialist monographs: A Nair, *Claims to Traceable Proceeds* (OUP 2018), para 4.37; M Raczynska, *The Law of Tracing in Commercial Transactions* (OUP 2018), para

full rationalisation attempted here—two major practitioner texts,⁵ and one admirable student text.⁶

The backward tracing debate

But first to briefly outline the possibility of backward tracing, for context. The proposed idea of backward tracing—at least as usually understood—is that when money pays off an overdraft, or other debt, it can be traced backward in time or direction *through the debt* into any asset acquired earlier by the borrowing. The classic example would be a wrongdoer taking out a loan to purchase an asset; the wrongdoer then buying the asset with the borrowed money; the wrongdoer then stealing money from a trust and using the misapplied funds to pay off the loan. The immediate use of the trust funds was not to purchase an asset but to discharge a liability—paying off the debt obligation involved in the loan—so there is no asset acquired in direct exchange for the money to trace into. Backward tracing would involve saying: ‘We can trace the trust money, backward through the debt, into the asset that borrowing paid for earlier.’

The merits of this form of backward tracing have been thoroughly debated. In particular, Smith argues that it is always possible to trace payment of a debt

backwards into any asset the debt previously paid for; or, alternatively, into the money originally borrowed, assuming it still exists unspent.⁷ But Conaglen contends backward tracing should not be recognised: arguing the authorities are against it, the law traces through assets not liabilities, and backward tracing would unduly give yet more proprietary protection at the expense of the personal claims of an insolvent wrongdoer’s creditors.⁸

However, it should be noted that the expression ‘backward tracing’ is sometimes used in a wider sense: to mean *any* assertion the law should trace backwards in time or direction—even if no use of credit was involved, so there is no debt to trace ‘through’.⁹ And it should also be noted that it is widely believed two relatively recent cases have significantly developed the law on backward tracing. The decision in *Relfo Ltd v Varsani*¹⁰ arguably involved implicit recognition by the Court of Appeal of backward tracing, through a debt; and in *Federal Republic of Brazil v Durant International Corp*,¹¹ the Privy Council explicitly said it was tracing backward—seemingly using ‘backward tracing’ in the *wider* sense just identified—and said that tracing backward is permissible within stated limits.¹² However, the present writer, at least, has argued elsewhere that *the decision in neither case should be understood as involving backward tracing of any sort*.¹³

3.17. Likewise most leading student textbooks: J Glistler and J Lee (eds), *Hanbury and Martin Modern Equity* (22nd edn, Sweet & Maxwell 2021), para 26.024; G Virgo, *The Principles of Equity and Trusts* (4th edn, OUP 2020), 601–4; PS Davies and G Virgo, *Equity and Trusts: Text, Cases and Materials* (3rd edn, OUP 2019), 888–92; J Garton, R Probert, and G Bean (eds) *Moffat’s Trusts Law: Text and Materials* (7th edn, CUP 2020), 623. JE Penner, *The Law of Trusts* (12th edn, OUP 2022), paras 12.32–12.33, does discuss Dillon LJ’s comments on forward tracing, only to dismiss them: for his objection, see below n 22.

5. Neither book sets out Dillon LJ’s views on forward tracing through an overdraft, but each independently endorses the possibility: J McGhee and S Elliott (eds), *Snell’s Equity* (34th edn, Sweet & Maxwell 2020), para 30.064—quoted in the text below; and L Tucker, N le Poidevin, and J Brightwell (eds), *Lewin on Trusts* (20th edn, Sweet & Maxwell 2020), para 44.113.

6. C Webb and T Akkouch, *Trusts Law* (5th edn, Palgrave 2017), 352, sets out Dillon LJ’s views in full, and separately, 350–51, suggests forward tracing through an overdraft ‘seems not only possible but sensible’.

7. LD Smith, ‘Tracing into the Payment of a Debt’ (1995) 54 CLJ 290. He elaborated on his views in LD Smith, *The Law of Tracing* (OUP 1997), 353–56; and also, 215–17, on how backward tracing works in the more complicated situation where an overdraft has paid for several assets, and only part of that overdraft is paid off using the claimant’s money. For an argument that if we strictly attend to contractual technicalities, practically every sale of an asset involves backward tracing, since the vast majority of sales are technically an exchange of promises rather than an exchange of money for assets, see J Penner, ‘“Sort of” Backwards Tracing’ in Paul S Davies and James Penner (eds), *Equity, Trusts and Commerce* (Hart 2017), 126–27. But contrast an argument that the treatment of a transaction for the purposes of equitable tracing will not—and should not—necessarily correspond to a minute dissection of the same transaction for the purpose of identifying the parties’ contractual rights against one another, given ‘equity looks to substance not form’: see R Nolan, ‘Civil Recovery after Fraud’ (2015) 131 LQR 8 (expanded on in RC Nolan, ‘The Administration and Maladministration of Funds in Equity’, in PG Turner (ed), *Equity and Administration* (CUP 2016)).

8. M Conaglen, ‘Difficulties with Tracing Backwards’ (2011) 127 LQR 432. He suggests that if backward tracing is to be allowed, it should be limited to situations where the wrongdoer *planned* from the outset using misapplied money to acquire the traced asset.

9. For example, see the description of this as ‘a form of backward tracing’, in L Tucker, N le Poidevin, and J Brightwell (eds), *Lewin on Trusts* (20th edn, Sweet & Maxwell 2020), para 44.072. (By way of illustration, suppose a trustee plans to fund a personal investment by stealing from the trust: however, while the investment opportunity only exists now, an occasion to steal from the trust will not arise until next week. So, the trustee uses their own ‘holiday fund’ to make the investment; then steals from the trust to replace the holiday fund; then dissipates that fund by taking the holiday. Some would argue, given this was an overall plan to fund the investment from the trust’s money, the law should trace the stolen trust money back in time or direction *as if* it paid for the investment.)

10. [2014] EWCA Civ 360, [2015] 1 BCLC 14.

11. [2015] UKPC 35, [2016] AC 297.

12. An attempt to survey the resulting law is *Serious Fraud Office v Hotel Portfolio II UK Ltd* [2021] EWHC 1273 (Comm), [21]–[48].

13. D Wilde, ‘A New Direction for Equitable Tracing?’ (2023) 37 TLI forthcoming.

Forward tracing through an overdraft

Turning to tracing *forward* through an overdraft. In *Bishopsgate v Homan*, Dillon LJ began by accepting that¹⁴:

[T]he recognised principles of equitable tracing . . . do not permit tracing through an overdrawn bank account – whether an account which was already overdrawn at the time the relevant moneys were paid into it or an account which was then in credit, but subsequently became overdrawn by subsequent drawings.

But he suggested forward tracing through an overdraft might be possible, giving this example¹⁵:

[M]oneys misappropriated . . . were paid into an overdrawn account [of the wrongdoer] in order to reduce the overdraft and so make finance available within the overdraft limits for [the wrongdoer] to purchase some particular asset.

If this is a scenario where tracing through an overdraft is possible, the judge's words 'in order to' appear redundant. What matters for tracing purposes, it is suggested, must be the objective fact that the payment into the account *did* enhance the spending power of the overdraft, which was then used to purchase an asset. It seems to be immaterial to tracing whether or not the wrongdoer *intended* to do this from the outset: that is, whether the wrongdoer had a plan in mind at the time of the

payment into the overdraft to use the facility to purchase a particular asset. Tracing operates through identifying the substitution of one asset for another, usually by way of exchange: that is what we have to identify here. The degree of premeditation behind a substitution is an irrelevance—at least on conventional notions of tracing.¹⁶

Leggatt LJ, delivering the other substantial judgment in the case, did not directly address this example; but by clear implication did not accept it. He said bluntly¹⁷: 'I do not accept that it is possible to trace through an overdrawn bank account . . .' However, importantly, this was premised on his earlier reasoning that¹⁸: 'it is only possible to trace in equity money which has continued existence, actual or notional.' His objection, therefore, falls away if it is possible to demonstrate the 'continued existence' of misapplied funds despite payment into an overdraft.

Rationalising forward tracing through an overdraft

The supposed impossibility of tracing forward through an overdraft is commonly explained on the basis that an overdraft is 'not an asset but a liability'¹⁹—a debt. However, this is not the whole story. An *authorised* overdraft facility is an asset. As *Snell's Equity* points out, it is a chose in action, arising from the contract between customer and bank²⁰:

[T]he effect of [a] trustee's paying the claimant's money into an overdrawn bank account is generally to render the money untraceable. The claimant may

14. [1995] Ch 211 (CA), 216.

15. [1995] Ch 211 (CA), 216. Dillon LJ was adopting and approving (217) views expressed by Vinelott J at first instance: for which see [1994] Pens LR 179, [77], [79], [130].

16. In *Foskett v McKeown* [2001] 1 AC 102 (HL), 127, Lord Millett, delivering the leading judgment, said, 'Tracing is the process of identifying a new asset as the substitute for the old' *simpliciter*—no mention of premeditation. (But now cf *Brazil v Durant* [2015] UKPC 35, [2016] AC 297 on the role of intention—although see D Wilde, 'A New Direction for Equitable Tracing?' (2023) 37 TLI forthcoming, for why this case is, arguably, and with great respect, not a convincing authority on tracing.)

17. [1995] Ch 211 (CA), 222.

18. [1995] Ch 211 (CA), 221.

19. *Shalson v Russo* [2003] EWHC 1637 (Ch), [2005] Ch 281, [138] (Rimer J)—elaborated on at [140]: '[I]t is not possible to trace into and through an overdrawn account, because such an account is not an asset at all: it is a liability. The consequence is that the claimant cannot show that his money has become represented by an asset into which it is possible to trace: all his money has done is to reduce a liability, and so has ceased to exist.'

20. J McGhee and S Elliott (eds), *Snell's Equity* (34th edn, Sweet & Maxwell 2020), para 30.064 (note omitted). However, it must be conceded that whether an item such as an authorised overdraft facility should be treated as an 'asset' or 'property' depends on the *context* in which the question is being asked: *JSC BTA Bank v Ablyazov* (No 10) [2015] UKSC 64, [2015] 1 WLR 4754, esp [37].

however assert a lien over the account to the extent that his money reduces an authorised overdraft since the authorised overdraft is a chose in action equivalent to a credit balance in the account.

The equivalence to a credit balance is not total—as will be seen in due course. But the recognition that an authorised overdraft facility is a chose in action—an asset—is an important starting point.

An authorised overdraft facility is a somewhat unusual asset, because it entails a liability. But so do many other assets through which tracing regularly takes place. This includes assets where the liability substantially counterbalances the benefit derived from the asset. For example, a lease is an asset, which can doubtless be traced into when purchased. It confers a right to the use of land; but it entails a countervailing liability, to pay the rent. An authorised overdraft facility is similar: it is a prized asset of many businesses and individuals, enabling them to use credit to their advantage; but it comes with a liability, to repay the borrowed amounts and meet any applicable charges.

Suppose I have an authorised overdraft facility for £10,000 at my bank. But I am already £10,000 overdrawn. I misappropriate £5,000 from a trust and pay it into the account. Most explanations of equity's tracing rules would say the money is now no longer traceable. These descriptions would say the trust's money has been used solely to pay off a debt: I acquired no asset with it. And the bank that provided me with credit is untouchable as a bona fide purchaser of the money it received. Accordingly, these accounts of the law would say, if I then use my overdraft to buy a painting for £5,000, the trust's money cannot be traced to the painting.

But is this correct? It is possible to say that the £5,000 of trust money used to pay down the overdraft *did* go

into an asset: the overdraft facility viewed as a chose in action. Before the payment in, this facility had zero spending power; after the payment in, it had £5,000 of spending power—just as, supposing the account balance had instead been £1,000 *in credit*, after the payment in it would be £6,000 in credit, and nobody would see any difficulty in tracing the £5,000 difference into the credit balance of the account. Of course, superficially there is a distinction between the overdrawn account and the account in credit. In the case of the account with a credit balance, there is 'money in the account'; whereas it is tempting to think that, in the case of the overdrawn account, 'the money paid in has disappeared into the debt.' But suppose I had used the £5,000 to instead purchase a lease. Again, the money has 'disappeared' (into the purchase): *I no longer have any money*. But I have substituted for it a different asset, a lease giving me the valuable right to use land; and entailing a liability, to pay the rent. Nobody would see any difficulty tracing the trust's money into the purchased lease. Likewise, when I paid the £5,000 into my overdrawn account, I no longer had 'the money'—but by way of substitution I had another asset: the chose in action constituted by my overdraft facility, now with the valuable right of £5,000 in spending power; albeit entailing a liability to repay the borrowed money and meet associated charges.²¹

It seems possible to trace a claim through, but not into, an overdraft

If this analysis is correct, it should be possible, in the example given, to trace the £5,000 of misapplied trust money through the overdraft facility, to make a claim against the painting purchased with it.²² But while it seems possible on this basis to trace a claim *through* an authorised overdraft, to property purchased using its

21. Of course, the obligation to repay merely restores the overdraft's liabilities to where they stood before the misapplied funds were ever paid in. In our example, the account was £10,000 overdrawn; £5,000 was wrongfully paid in; and when that £5,000 spending power was used to buy a painting, the overdraft returned to where it stood originally, at £10,000—but with the wrongdoer now holding as an additional asset the £5,000 painting. In fact, the liabilities on the overdraft overall may have been reduced by the misapplication—through lower interest charges on the debt during the period the overdraft was halved.

22. JE Penner, *The Law of Trusts* (12th edn, OUP 2022), para 12.33 objects that (emphasis in the original), 'The reduction of the overdraft [through a wrongdoer paying misapplied funds into their account] allows [the wrongdoer] to use the *bank's money* to make ... purchases, not to use the [misapplied funds] to do so.' Presumably this is simply a reiteration of the point that the wrongdoer has no credit balance in the account—to which the answer here is the wrongdoer nevertheless has an asset in the form of spending power within the chose in action constituted by the overdraft facility. However, if this passage were read as suggesting a bank has *title* to money at the point when a customer spends it from an overdraft facility, that is not so. As Harman J held in *Re Hone, ex p The Trustee v Kensington Borough Council*

spending power, it is not possible to trace a claim *into* the authorised overdraft itself—that is, as the final destination, where it is sought to identify property to make a claim against. An authorised overdraft facility is not amenable to such a claim. The standard claim following on from tracing is to an equitable charge or lien. And we can meaningfully say that the authorised overdraft was subject to an equitable charge or lien, to denote that it could be traced *through*. But the basic remedies arising from an equitable charge or lien against an asset are (1) a court order for payment from a fund, for the amount of money the claimant is due, or (2) a court order for an order for sale of the asset, to get the claimant's money out (or direct transfer of the asset itself). In respect of (1), an authorised overdraft facility is not a fund containing any money. It has spending power of course, but with a liability to repay it: and while the court will order a wrongdoer to pay over money they have, it will not order them to, effectively, borrow money to pay over to a claimant. And in respect of (2), an authorised overdraft facility—invariably non-assignable by its terms—has no sale (or transfer) value. The option to elect to claim (proportionate) ownership, rather than an equitable charge or lien, of course would fare no better. To extend the comparison with a lease, it is as if the money has been paid into a lease with no realisable value: there is an asset there, but one not amenable to any viable claim *into* the asset. However, if fortuitously the lease were subject to compulsory acquisition, with compensation payable, it would be possible to trace *through* the lease to a viable claim against that money.

Impact on the 'lowest intermediate balance' rule

Although forward tracing through an authorised overdraft cannot lead to an effective claim against the overdraft, it could nevertheless *facilitate* a claim against the

bank account *insofar as it is later in credit*—through the impact that recognising forward tracing through an authorised overdraft facility should logically have on the 'lowest intermediate balance rule'.

*James Roscoe (Bolton) Ltd v Winder*²³ held that if a wrongdoer pays misapplied funds into their own bank account, the lowest credit balance to which the account falls, before new money is paid in, is all that can traceably remain of the misapplied money. This is the so-called 'lowest intermediate balance' rule. A trustee paid £455 of trust funds into his private bank account. Personal expenditure then reduced its credit balance to £25. Later he deposited his own money and by his death there was a credit balance of £358. But it was held that only £25 could traceably remain of the trust money—this was the 'lowest intermediate balance' before other money was paid in. However, suppose this account had an authorised overdraft facility of £100. An extra £100 could now be seen to traceably survive in the account—within the chose in action constituted by the authorised overdraft facility—even when the credit balance alone was reduced to £25. In other words, when identifying the lowest intermediate balance, we have to factor in any authorised overdraft limit. The claimant should eventually recover £125 from the final £385 credit balance.

This approach potentially makes sense of the otherwise problematic decision in *Re Tilley's Will Trusts*.²⁴ There the wrongdoer was a lay executor trustee, who thoroughly confused trust money with her own money in her bank account, while dealing in property on her own account, all the time enjoying extensive overdraft facilities. A trust beneficiary claimed a share of ownership in two houses the wrongdoer bought using the mixed account. Each house purchase took place after trust money had been paid into the account. The first purchase was funded to a small extent by going overdrawn on the account, and the second purchase was made when the account was already substantially overdrawn, the entire purchase being funded using the overdraft facility further. The account was restored to

[1951] Ch 85 (Ch), 89: '[A] payment by a bank, under an arrangement by which the customer has an overdraft, is a lending by the bank to the customer of the money. It is the customer who pays the money and not the bank . . . They have only paid it as agent for the customer just as if she had money there.'

23. [1915] 1 Ch 62 (Ch).

24. [1967] Ch 1179 (Ch).

substantial credit by the time of the beneficiary's claim—easily enough to repay the misapplied trust money. The beneficiary was held entitled to enforce an equitable charge or lien against the bank account for the amount of the misapplied trust money; but not entitled to trace into the houses purchased. The decision looks wrong if we apply the lowest intermediate balance rule *without factoring in the authorised overdraft facility*. All of the trust money paid in would have become untraceable *within the account itself* once its credit balance hit zero at the time of the first house purchase. And trust money within the credit balance at the date of the first house purchase *should* have been traceable into the house, given that the purchase left nothing in the account, so *must* have used the trust's money. However, the decision may make sense if we factor in the authorised overdraft facility when applying the lowest intermediate balance rule.²⁵ The trust money could then be seen to have survived in the account at all times, either within its credit balance or within spending power as an unused part of the authorised overdraft facility: and given the credit balance of the account was sufficient to repay the trust money in the end, the claimant had to be satisfied with an equitable charge or lien against the account.²⁶ This is consistent, at least, with what Ungood-Thomas J said in *Re Tilley*,²⁷ that the presence of the trust money in the account 'merely avoided, to the extent of their [small] amount, the use of Mrs. Tilley's ample overdraft facilities'. He concluded²⁸:

Mrs. Tilley's breach halted at the mixing of the funds in her bank account. Although properties bought out of those funds would, like the bank account itself, at any rate if the moneys in the bank account were

inadequate, be charged with repayment of the trust moneys which then would stand in the same position as the bank account, yet the trust moneys were not invested in properties at all but merely went in reduction of Mrs. Tilley's overdraft which was in reality the source of the purchase-moneys.

Issues for consideration before recognising forward tracing through overdrafts

If a court were asked to recognise forward tracing through an overdraft, there would be a range of factors to be considered in the judicial balance—beyond the obvious weight of precedent apparently against the possibility: from judgments saying repeatedly, *without qualification*, that it is not possible to trace through an overdraft. To highlight a few policy or practical matters.

Impact on an insolvent wrongdoer's creditors

If a wrongdoer who has misapplied funds in breach of trust or breach of fiduciary duty is insolvent, any extension of the victim's right to trace to a proprietary claim over proceeds of the misapplied funds, of course, adversely affects the wrongdoer's creditors with only personal claims. In such situations, deciding the law governing the distribution of the wrongdoer's assets is effectively a contest between innocent parties. Would recognition of forward tracing through an authorised overdraft come at the undue expense of insolvency creditors? Oakley was prepared to endorse the example of forward tracing through an overdraft given by Dillon LJ in *Bishopsgate v Homan* that we started

25. 'May' because there was no clear finding as to the extent of the authorised overdraft limit at the date of the second house purchase, although inferences can be drawn from the reported facts that would support the analysis in the text.

26. By extension of the rule in *Turner v Jacob* [2006] EWHC 1317 (Ch), [2008] WTLR 307. That case decided that where a wrongdoer mixes misapplied funds with their own money in a bank account, so long as the account maintains a balance at least equalling the misapplied funds—or what now traceably remains of them—so that the account balance is sufficient to repay those funds, they are taken to remain in the account: that is, a claimant cannot say those funds should instead be traced into property purchased by the wrongdoer from the account, which has increased in value. We would have to extend this decision by saying that, if sufficient money to meet the claim traceably survives within the account throughout, in either its credit balance or unused authorised overdraft limit, and is present in the final credit balance, tracing into property purchased from the account is not possible. (For the view that the rule in *Turner v Jacob* only applies where the wrongdoing involves no breach of fiduciary duty—as in both *Turner v Jacob* and *Re Tilley*—that is, an argument that the rules of tracing take account of the type of wrongdoing, see D Whayman, 'Obligation and Property in Tracing Claims' [2018] Conv 157. But contrast the view that *Turner v Jacob* is just wrong, because it is inconsistent with underlying principles of tracing law, which subordinate the interests of a wrongdoer mixer of property to those of an innocent party: LD Smith, *The Law of Tracing* (OUP 1997), 199–203; and PS Davies and G Virgo, *Equity and Trusts: Text, Cases and Materials* (3rd edn, OUP 2019), 880.)

27. [1967] Ch 1179 (Ch), 1192.

28. [1967] Ch 1179 (Ch), 1193.

from, above, on the simple ground that the trust money was paid into the wrongdoer's account, then traced out again, so not affecting the assets otherwise available to the creditors²⁹:

Provided that the link between the reduction of the overdraft and the subsequent purchase can be genuinely established, this limited modification of the rule in *James Roscoe (Bolton) v. Winder* [the lowest intermediate balance rule] will not deprive the general creditors of assets which would otherwise have been available for them; consequently, there seems no reason why the view of Dillon L.J. should not be adopted in appropriate circumstances.

However, after *Foskett v McKeown*,³⁰ the legal scope for victims of misapplications to trace into assets that have significantly increased in value and to elect to claim (proportionate) ownership of them is clearer than it was at the time Oakley wrote this. A court would have to weigh these policy considerations.

Unauthorised overdrafts unaffected

One limitation on the impact of forward tracing through an overdraft on an insolvent wrongdoer's creditors is that it could only apply in the case of *authorised* overdraft facilities. Only then is there a chose in action—an asset—to trace into. But this creates what could be seen as a somewhat arbitrary dichotomy for claimants: forward tracing through an overdraft is sometimes possible, sometimes not.

Forward tracing through an overdraft ruling out backward tracing

Further, recognition of forward tracing through an authorised overdraft could exclude the possibility of

backward tracing through an authorised overdraft. After all, it is hard to see how both forward tracing and backward tracing could be accepted—the law surely cannot trace in both directions.³¹ And arguably this would militate against the recognition of backward tracing through any other debt, or backward tracing in its wider sense, not involving any debt. This, in turn, would spare an insolvent wrongdoer's creditors the impact of the backward tracing doctrine, which is generally thought to be establishing itself, to a degree at least, in recent case law (above); but correspondingly it would restrict claimants.

Complexity

Recognition of forward tracing through an overdraft would add to the complexity of tracing. In particular, additional facts to be investigated, examining overdraft histories; greater difficulty applying the lowest intermediate balance rule, as outlined above; and a need for the courts to analyse the interplay, when tracing, between any credit balance in an account and any unused part of an overdraft facility, and to identify within an unused overdraft which part represents misapplied funds—although this should not pose serious problems, well-established tracing principles being available for development by analogy.

Brazil v Durant's pronouncements on tracing through overdrafts

Finally, the argument made here should be put into the context of the Privy Council's important decision in *Brazil v Durant*. That judgment is, respectfully, problematic to the present writer: ostensibly based on tracing, in truth it seems instead to create a quite separate novel non-tracing doctrine of 'premeditated reconstruction' of a fund.³² But insofar as it is generally

29. AJ Oakley, 'Proprietary Claims and their Priority in Insolvency' (1995) 54 CLJ 377, 413. (To like effect, see AJ Oakley (ed), *Parker and Mellows: The Modern Law of Trusts* (9th edn, Sweet & Maxwell 2008), para 22.173.)

30. [2001] 1 AC 102 (HL).

31. L Smith 'Tracing, "Swollen Assets" and the Lowest Intermediate Balance: *Bishopsgate Investment Management Ltd v Homan*' (1994) 8 TLI 102, 104, makes the same point from the opposite perspective, supporting backward tracing.

32. D Wilde, 'A New Direction for Equitable Tracing?' (2023) 37 TLI forthcoming.

understood to be a tracing case, it is high authority, apparently—albeit obiter and only persuasive—that the law *already* recognises forward tracing through overdrafts, at least to a limited extent; although, incongruously, forward tracing is said to operate *alongside* backward tracing. Lord Toulson JSC, delivering the judgment, said this³³:

The development of increasingly sophisticated and elaborate methods of money laundering, often involving a web of credits and debits between intermediaries, makes it particularly important that a court should not allow a camouflage of interconnected transactions to obscure its vision of their true overall purpose and effect. If the court is satisfied that the various steps are part of a co-ordinated scheme, it should not matter that, either as a deliberate part of the choreography or possibly because of the incidents of the banking system, a debit appears in the bank account of an intermediary before a reciprocal credit entry. The Board agrees with Sir Richard Scott V-C's observation in *Foskett v McKeown* [1998] Ch 265, 283 that the availability of equitable remedies ought to depend on the substance of the transaction in question and not on the strict order in which associated events occur.

Similarly, in a [backward tracing] case such as *Agricultural Credit Corp'n of Saskatchewan v Pettyjohn* 79 DLR (4th) 22, the Board does not consider that it should matter whether the account used for the purpose of providing bridging finance was in credit or in overdraft at the time. An account may be used as a conduit for the transfer of funds, whether the account holder is operating the account in credit or within an overdraft facility.

The Board therefore rejects the argument that there can never be backward tracing, *or that the court can never trace the value of an asset whose proceeds are paid into an overdrawn account*. But the claimant has to establish a

co-ordination between the depletion of the trust fund and the acquisition of the asset which is the subject of the tracing claim, looking at the whole transaction, such as to warrant the court attributing the value of the interest acquired to the misuse of the trust fund...

The argument made in the present article is capable of rationalising, at least in part, that is, with respect to authorised overdrafts, the apparent statement in this quotation (as highlighted) that forward tracing through overdrafts *is* possible; although it does not support the limitation apparently placed on such tracing within the passage, to coordinated schemes. But this discrepancy is part of a wider picture. It is suggested that there is *much* said in the case regarding tracing that cannot be justified—at least according to traditional, conventional understandings of tracing.³⁴

Conclusions

If the analysis here is correct, there is an arguable case for recognising forward tracing through an authorised overdraft, on the basis that regular assertions that an overdraft is simply a liability and not an asset are wrong: an authorised overdraft *is* an asset (albeit entailing a liability)—a chose in action. If a wrongdoer misapplies money in breach of trust or breach of fiduciary duty into a bank account with an authorised overdraft, and that account is overdrawn or later becomes overdrawn, then to the extent that the misapplied money frees up spending power within the overdraft limit, it traceably survives. And if the spending power is used, its use can be traced into any asset later acquired by that spending power. However, so long as all that exists is spending power within the overdraft, that is not itself an item that can be successfully claimed against—such spending power is not amenable to any remedy. Moreover, it

33. [2015] UKPC 35, [2016] AC 297, [38]–[40], emphasis added.

34. Above n 32.

logically follows that, when applying the lowest intermediate balance rule, any authorised overdraft should be factored in. Finally, it is questionable whether, or

how far, notions of backward tracing can coexist with any recognition of forward tracing through an authorised overdraft.

***David Wilde** studied law at Oxford University (BA, BCL), is a non-practising Barrister (Inner Temple) and obtained his PhD at the University of Reading, where he is now an Associate Professor of Law. E-mail address: d.c.wilde@reading.ac.uk.*