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DETERMINATION OF SUPERIOR EQUITIES IN CASES OF MARSHALING AND SUBROGATION

C. SEVERIN BUSCHMANN

The principles of marshaling of securities and of subrogation are useful in placing losses, as far as possible, upon the parties ultimately liable. Developed at an early stage of the law, the rules have been extended to new situations and are of increasing importance in our decisions.

The equitable remedy of subrogation has long been established in our law and has gradually become more extended in its scope. Originally it had a narrow application,—being considered usually in cases where sureties had discharged duties of their principals and were seeking to be subrogated or substituted to rights of the creditors.¹ The doctrine was applied more liberally by later courts and has been expanded until now it applies generally to all those obligations discharged by a person not primarily liable, but who is acting either in performance of a legal duty, to protect a legal right, at the request of the party ultimately liable for the debt, and possibly in other cases where favored by public policy.² In such cases the subrogee can work out his right only through the creditor, and consequently his rights are limited to those of the creditor.³ The usual situation is where he is simply substituted to a single right of the creditor who has been paid off by him. It frequently happens, however, that the subrogee, instead of actually paying out his money to a creditor, has a fund belonging to such subrogee taken by a creditor who had superior rights in the fund. In such a situation, if the paramount creditor has available any other rights by which he might have realized his claim, the possibility arises

¹ 4 Pomeroy Eq. Juris. (4th ed.) 1419.

² 5 Pomeroy Eq. Juris. (2d ed.) 2343.

³ 5 Pomeroy Eq. Juris. (2d ed.) 2349.

of the subrogee ultimately avoiding the loss, by marshaling or subrogation.

The principle underlying the equitable remedy of marshaling of securities is that a person having two funds, from either of which he can satisfy his claim, should not be allowed by his election to take the one from which alone another party can satisfy his claim.⁴ In order to obtain this relief, however, the holder of the two funds must not be inconvenienced in the collection of his debt, or prejudiced,⁵ nor will it be granted where it will prejudice the rights of third persons.⁶

The principle of subrogation as a corollary to the principle of marshaling assets frequently arises where the doctrine of marshaling cannot be carried out. The rule may be stated as follows: Where one party has a right to resort to two funds for the satisfaction of his debt and another has a junior right against only one of them, if the former exercise his superior right to satisfy his claim out of the only one to which the junior claimant can resort, the latter will in equity be subrogated to the right of the senior claimant to proceed against the other fund.⁷ It first arose with reference to mortgages, and was later extended to various other situations.

In discussing subrogation as applied to the two fund situation, Williston says:⁸

"The justice of the principle will be apparent if it is observed that in this way the creditor is denied the power of throwing the ultimate payment of the debt in one way or the other as suits his caprice."

One of the earliest statements of the principle of subrogation in this form was made by Chief Justice Marshall in *Allston v. Mumford*,⁹ as follows:

"If there be two mortgagees, A the prior mortgagee upon two tracts and B the subsequent mortgagee on only one of these tracts, if A should appropriate to his debt the land mortgaged to B, then B would be permitted to take the place of A with reference to the other tract."

The Supreme Court of the United States recognized and applied the rule in the case of *Hawkins v. Blake*.¹⁰ In that case Devereaux as executor paid off certain legacies which were

⁴ 5 Pomeroy Eq. Juris. (2d ed.) 2288, note 1 (citing cases exhaustively).
18 R. C. L., p. 456.

⁵ 5 Pomeroy Eq. Juris. (2d ed.) 2289, 18 R. C. L., p. 462.

⁶ 5 Pomeroy Eq. Juris. (2d ed.) 2290.

⁷ 18 R. C. L., p. 467.

⁸ 2 Williston on Contracts, p. 2302.

⁹ 1 Brock 279, Fed. Cas. 267.

¹⁰ 108 U. S. 422, 27 L. Ed. 775.

chargeable on real estate theretofore conveyed to him by his mother, and reimbursed himself from the personal property. The court found that the legacies should have been borne by the real estate primarily and only secondarily by the personal property, and that the reimbursement was therefore wrongful. At that time, however, the real estate had passed into the hands of assignees in bankruptcy and Devereaux was insolvent. The next of kin who had been deprived of personal property were held entitled as against the assignee to be subrogated to the liens of the legatees whose legacies had constituted charges against the real estate. The court said,

“Why are not the next of kin now entitled to stand in the place of those legatees, in respect to the fund out of which they should have been paid? Upon the familiar principle of marshaling assets by means of subrogation, when a party, having a right to resort to two funds to the detriment of another, entitled to be paid out of but one, has been satisfied out of the later, the fund thus exonerated will in equity be subjected to the payment of the postponed claim.”

Jones v. Zollicoffer, an early North Carolina case,¹¹ contains an excellent discussion of the principle, the opinion pointing out the difference between cases where relief will be given by restraining the senior claimant from satisfying his claim out of the doubly charged fund, and cases where relief will be granted by way of substitution after the election has been made. There the court says:

“A court of equity will restrain a person in the capricious exercise of his rights; for benevolence becomes a duty enforced by courts of justice, when its exercise is in no wise prejudicial to the party, and a want of it is injurious to another. Thus, when a person may get satisfaction out of either of two funds, and another can get satisfaction only out of one of them, and they are both equally convenient and accessible to him who may get satisfaction out of either, and nothing but mere caprice governs him in making the selection, there equity will restrain him to the fund not onerated by the claims of the other; but if convenience, and not caprice, is his motive, the most that equity does is to substitute the disappointed claimant to his rights. The first is rarely done; for it is a matter of extreme delicacy to restrain a person in the exercise of a legitimate right, in favor of one who has no claim upon him by contract, and whose only connection with him arises from being interested in the same common fund; yet where there is a fraud, moral or legal, or mere caprice, he will be restrained. The latter to wit, substitution, is very frequently done, and is the foundation of marshaling assets in favor of legatees and simple contract creditors, and applies in cases where there is neither fraud nor caprice; it is sufficient that his fund has been exhausted by one who had a double means of satisfaction.”

¹¹ 9 N. C. 623.

In the recent case of *Sowell v. Federal Reserve Bank of Dallas*,¹² the court refused to grant marshaling in case of a suit by an indorsee bank, holding both a right of action against an insolvent payee and collateral security of the payee, against a maker who has a claim against the payee, apparently mistakenly failing to view the situation as one between creditors.¹³ It is doubtful if the case was a proper one for marshaling, and the decision can be supported on that ground. If the maker had paid the note, he might have obtained the desired result by means of subrogation.

Numerous other authorities illustrate various applications of the principle of subrogation.¹⁴

The operation of the principle is not affected by the nature of the property which constitutes the two funds, but applies whenever a paramount creditor holds collateral security or can resort collaterally to other property of any description for the payment of the debt.¹⁵ It applies although one of the funds consists merely of a chose in action,¹⁶ and although discharged at law, the claim will be treated in equity as still in existence for the benefit of the one entitled to subrogation.¹⁷ In general, the doctrines relative to subrogation apply as completely against a surety whose liability is prior to that of the party seeking subrogation as they do against the principal debtor.¹⁸

A slightly different situation from the ordinary case of substitution, and the two fund doctrine, although based upon the

¹² 45 Sup. Ct. 528.

¹³ 39 Har. L. R. 256.

¹⁴ *Mathews v. Memphis R. R. Co.*, 108 U. S. 368, 2 S. Ct. 780, 27 L. Ed. 756; *Rock Springs First Nat. Bank v. Roder* (C. C. A.), 114 Fed. 451; *Clark v. Manufacturers Mutual Fire Ins. Co.*, 130 Ind. 332; *Wyman v. Fort Dearborn Bank*, 181 Ill. 27, 54 N. E. 946; *Farwell v. Importers' Nat. Bank*, 90 N. Y. 485; *Hannegan v. Hannah* (Ind.), 7 Blackf. 353; *Anthes v. Schroeder* (Neb.), 94 N. W. 611; *Ocoback v. Baker*, 52 Neb. 447, 72 N. W. 582; *Dahlman v. Greenwood* (Wis.), 74 N. W. 215; *Hudkins v. Ward*, 30 W. Va. 204, 3 S. E. 600; *Dickson v. Back*, 32 Ore. 217, 51 Pac. 727; *Webber v. Webber*, 109 Mich. 147, 66 N. W. 960; *Ross v. Duggan*, 5 Colo. 85, 102; *Hunt v. Townsend*, 4 Sand. Ch. 510; *In re Hobson* (Ia.), 46 N. W. 1095; *Cheeseborough v. Millard*, 1 Johns. Ch. (N. Y.) 409; *Harriman v. Skillman*, 33 Barb. 378; *Aldrich v. Cooper*, 8 Ves. Jr. 382; 5 Pomeroy Eq. Jur. (2d ed.) 2293; *Story's Eq. Jurispr.* (14th ed.) 853.

¹⁵ *Clark v. Manufacturers Mutual Fire Ins. Co.*, 130 Ind. 332; *Ross v. Duggan*, 5 Colo. 85; 5 Pomeroy Eq. Jur. (2d ed.) 2288, 2351.

¹⁶ *Clark v. Manufacturers Mutual Fire Ins. Co.*, 130 Ind. 332; *Dahlman v. Greenwood* (Wis.), 74 N. W. 215, 217.

¹⁷ *Hawkins v. Blake*, 108 U. S. 422; *Lidderdale's Executors v. Executors of Robinson*, 12 Wheat. 594; *Sidener v. Pavey et al.*, 77 Ind. 241, 246.

¹⁸ 5 Pomeroy Eq. Jur. (2d ed.) 2351.

same fundamental principles, arises under some circumstances where security given for a loan which is used to pay off an incumbrance turns out to be defective, although the person taking it expected to get good security. Under the circumstances, the payment is held in equity to operate as an assignment of the mortgage, and he will be subrogated to the rights of the holder of the security discharged with his money.¹⁹

The above situations in various forms arise very frequently in suits between banks who have advanced money to pay laborers and materialmen upon public works and the sureties upon the contractors' bonds. A contest involving some of the above principles arose in the case of *State ex rel. Southern Surety Co. v. Schlesinger*.²⁰ There the court was confronted with a mandamus suit by the State on the relation of the surety company against the director of highways and public works. The facts were briefly as follows: Relator was surety upon a contractor's bond for the building of a certain highway. During the performance of the work the contractors borrowed money from the bank upon their notes, giving as collateral security an assignment to the bank for all moneys then due or thereafter to become due from the state upon said contract. The amount of the loan was used to pay labor and material claims. The contractors were unable to complete the road, and the surety company was obliged to complete it. The director of highways and public works held a fund in his hands which had been earned and the surety company, having expended over \$7,000 in completing the road, brought the mandamus action to compel payment to it. The director of highways filed an interpleader praying that the bank and contractors be made parties, and be required to set up their claims for the determination of the court. Thereupon the bank filed an answer and cross-petition setting up its note and pledge, and seeking to have the amount of its loan paid to it. By statute it was provided that the surety

¹⁹ *MacGreal v. Taylor*, 167 U. S. 688, 17 S. Ct. 961, 42 L. Ed. 326; *Sidener v. Pavay*, 77 Ind. 241, 246; *Home Savings Bank v. Bierstadt*, 168 Ill. 618, 48 N. E. 161; *Emmert v. Thompson*, 49 Minn. 386, 52 N. W. 31; *Hughes v. Thomas*, 131 Wis. 315, 111 N. W. 474; *Heuser v. Sharman*, 89 Ia. 355, 56 N. W. 525; *Crippen v. Chappel*, 35 Kas. 495, 11 Pac. 453; *Hall v. Marshall*, 139 Mich. 123, 102 N. W. 658; *Berry v. Stigall*, 253 Mo. 690; *Patterson v. Birdsall*, 64 N. W. 294; *Straman v. Rechline* (Ohio), 51 N. E. 44; *Amick v. Woodworth* (Ohio), 50 N. E. 437; *Brandt on Suretyship* 326; 5 Pomeroy Eq. Jur. (2d ed.) 2347, note 87; 3 Pomeroy Eq. Jur. (4th ed.) 1211 ff.; 27 Cyc. 1438; 25 R. C. L. 1343. See *Miller v. Scott* (Ohio), 154 N. E. 358.

²⁰ (Ohio) 151 N. E. 177, 45 A. L. R. 371.

bond shall contain "an additional obligation for the payment by the contractor, and by all subcontractors, for all labor performed or materials furnished in the construction, erection, alteration or repair of such building, works or improvements." The contention of the surety was that it stood in the position of the state and that having paid out money to complete the road, it was subrogated to all rights the state would have if the state had declared the contract forfeited and had proceeded to complete the work, and that the contractors could not make an assignment of the funds as collateral security to the bank, even though the money was used to pay labor and material claims, if the effect was to deprive the surety of its right to stand in the position of the state. In other words, they contended that the surety having completed the road, was subrogated or substituted to the right of the state to retain the amount in its hands to reimburse itself for any loss. The bank, on the other hand, contended that the laborers and materialmen had an election to proceed either against the surety on its bond or against the retained fund, and since the bank's money was used to pay them, the bank was subrogated to their rights. It will be observed that although the laborers and materialmen had two or more funds from which they could collect (the retained percentage, a right of action against the surety and also a claim against the contractor) this is not an example of the two fund doctrine, not being a case where the bank is deprived of its fund, but is an example of the first type, namely, substitution. The bank was merely seeking to be substituted to the right of the laborers and materialmen against the fund by reason of the fact that it paid out its money. Not having seen fit to take an assignment of their claims from the laborers and materialmen, it is evident that the bank loaned its money on the credit of the contractor, and relied upon the assignment of the contract for security. Since the contract was of no value, they reserved nothing from it, and their right against the contractor alone remains.²¹ But, assuming that the bank had actually paid laborers and materialmen and is seeking to be substituted to their rights, and the surety is seeking to be substituted to the rights of the state, then since the rights of the state are superior to the rights of the laborers and materialmen, the equities of the surety are superior to those of the bank. Of course the surety standing in the shoes of the state would even prevail over the laborers and materialmen except for the reason that it has relinquished that

²¹ *Illinois Surety Co. v. City of Galion*, 211 Fed. 161; *Henningsen v. U. S. F. & G.*, 208 U. S. 404.

superior quality by contract when it became surety for labor and material claims. It has not relinquished it in favor of any one else, however. This is what the dissenting opinion had in mind at page 180 of the *Schlesinger* case where the court says:

“Had the loaner, instead of advancing the sum of \$800, for the payment of materials, actually furnished the materials, there could be no doubt that it would have a lienable claim for that amount.”

The answer to that argument is that the surety surrendered its equity only to laborers and materialmen and to no one else. In case, however, the equity of the bank should be superior to that of the surety for any reason (as by consent, agreement or otherwise) then the situation is reversed, and the bank should prevail. Few, if any, of the cases involve this stage of subrogation.

The majority of the court held that the right of subrogation of the surety operated as an equitable assignment, which right attached at the time the contract of suretyship was entered into, and that it took priority over the assignment, legal or equitable, which may be given by the contractor to any third party who enters into the transaction after its inception. The court therefore found that the right of the surety in the fund prevailed over that of the bank. (Three justices dissenting.)

It is submitted that the majority opinion is clearly right and that the dissenting opinion shows a failure to comprehend the principles of subrogation hereinbefore discussed. As pointed out in the majority opinion a surety upon a contractor's bond required by statute for the performance of a contract for public work has an equitable lien upon the fund to be used in payment therefore which arises when the bond is executed.²² The

²² *Prairie State Nat. Bank v. United States*, 17 S. Ct. 142, 164 U. S. 227, 41 L. Ed. 412; *Henningsen v. United States Fidelity & Guaranty Co.*, 28 S. Ct. 389, 208 U. S. 404, 52 L. Ed. 547; *In re Freeman & Brooks* (7th C. C. A.), 1 Fed. (2d) 430; *Henningsen v. U. S. F. & G. Co.* (9th C. C. A.), 143 Fed. 810; *Hardaway v. National Surety Co.*, 211 U. S. 552, 29 S. Ct. 202, 53 L. Ed. 321; *First National Bank of Seattle v. City Trust, Safe Deposit & Surety Co. of Philadelphia.* (9th C. C. A.), 114 Fed. 529; *Hardaway & Prowell v. National Surety Co.* (6th C. C. A.), 150 Fed. 465; *Title Guaranty & Surety Co. v. Dutcher*, 203 Fed. 167; *Pratt Lumber Co. v. Gill Co.*, 278 Fed. 783; *Cox v. New England Equitable Ins. Co.*, 247 Fed. 955; *Columbia Digger Co. v. Sparks*, 227 Fed. 780; *Peoples National Bank v. Corse*, 133 Tenn. 720, 182 S. W. 917; *American Bonding Co. v. Central Trust Co.*, 240 Fed. 400; *Wasco County v. New England Equitable Ins. Co.*, 88 Ore. 465, 172 Pac. 126, L. R. A. 1918 D. 732, Ann. Cas. 1918 E. 656; *Derby v. U. S. F. & G. Co.*, 87 Ore. 34, 169 Pac. 500; *First National Bank v. Pasha*, 99 Neb. 785, 157 N. W. 924; *Neodesha Nat. Bank v. Russell*, 109 Kans. 562, 200

Supreme Court of the United States in the case of *Prairie State Bank v. United States* furnishes a good example. There the question arose as to whether the surety (Hitchcock) on the contractor's bond or the bank who was assignee of the reserved fund had a prior lien upon the fund retained by the government where the contractor defaulted and the surety completed the work. In holding that the lien if any acquired by the bank was subordinate to the equity of the surety therein arising at the date of the contract, the court said,

"The sole question, therefore, is whether the equitable lien which the bank claims it has, without reference to the question of its subrogation is paramount to the right of subrogation which unquestionably exists in favor of Hitchcock. In other words, the rights of the parties depend upon whether Hitchcock's subrogation must be considered as arising from, and relating back to the date of, the original contract, or as taking its origin solely from the date of the advance by him." * * *

"Hitchcock's right of subrogation, when it became capable of enforcement, was a right to resort to the securities and remedies which the creditor (the United States) was capable of asserting against its debtor, Sundberg & Co., had the security not satisfied the obligation of the contractors; and one of such remedies was the right, based upon the original contract, to appropriate the 10 percent retained in its hands. If the United States had been compelled to complete the work, its right to forfeit the 10 percent, and apply the accumulations in reduction of the damage sustained, remained. The right of Hitchcock to subrogation, therefore, would clearly entitled him, when, as surety, he fulfilled the obligation of Sundberg & Co., to the government, to be substituted to the rights which the United States might have asserted against the fund. It would hardly be claimed that, if the sureties had failed to avail themselves of the privilege of completing the work, they would not be entitled to a credit of the 10 per cent reserved in reduction of the excess of cost to the government in completing the work beyond the sum actually paid to the contractor, irrespective of the source from which the contractor had obtained the material and labor which went into the building."

This reasoning has been generally followed. Some of the cases either purport to place the decision upon the ground that a bank in loaning money to a contractor is under no obligation to do so, and is therefore to be treated as a volunteer and so acquires no rights or contain dicta to that effect.²³ The sound-

Pac. 281; *Massachusetts Bonding & Ins. Co. v. Ripley County Bank*, 208 Mo. App. 560, 237 S. W. 182.

²³ *State v. Schlesinger* (Supra); *Henningsen v. U. S. F. & Co.*, 28 S. Ct. 389, 208 U. S. 404, 52 L. Ed. 547; *Lion Bonding & Surety Co. v. First State Bank of Paris* (Tex. Civ. App.), 194 S. W. 1012; *Carr Hardware Co. v. Chicago Bonding & Surety Co.*, 190 Ia. 1320, 181 N. W. 680; *Hess & Skinner Engineering Co. v. Turney*, 110 Tex. 148, 216 S. W. 621; *American Bonding Co. v. Central Trust Co.*, 240 Fed. 400; *Aetna Life Ins.*

ness of this ground has been questioned since even in case of a voluntary payment by the bank an implied assumpsit might be based upon a subsequent ratification by the debtor.²⁴ However where the bank pays the money at the request of the contractor (as is the usual case) it is not a volunteer at all.²⁵ The author of Brandt on Suretyship in enumerating the three classes comprising those entitled to subrogation states the third class to be those who act at the request of the debtor directly or indirectly or upon invitation of the public. Of this third class the author says,

“Cases coming third in the classification suggested above are those in which payment is made by a stranger to the obligation acting neither under compulsion nor for self protection, but at the request of some party liable for the debt. In these cases perhaps upon the ground of an implied promise the party making the payment is usually held subrogated to the rights of him who is paid.”

The cases cannot therefore be disposed of on the evasive ground that equity will not aid a volunteer. To do so would be misapplication of an equitable maxim. In the last analysis the matter for the determination of the court is simply which of the parties has the superior equity. In the *State v. Schlesinger* case the right of subrogation of the surety was paramount to the right of the bank since the surety's prior right to the fund arising at the time of the contract of suretyship could not be impaired by any act of the contractor and the bank.²⁶

The dissenting opinion seems to attach some importance to the fact that the state claimed no right in the retained fund. That is the very reason for the invocation of subrogation, which is to prevent a paramount creditor from having the power to throw the loss where it chooses, or convenience or caprice dic-

Co. v. Middleport, 124 U. S. 534, 31 L. Ed. 537, 8 S. Ct. 625; *Prairie State National Bank v. United States*, 164 U. S. 227, 17 S. Ct. 142.

²⁴ While the debtor has the right to repudiate such payment and refuse to indemnify the stranger, he has no right to benefit by it. If repudiated, since the debtor has been paid by the stranger, he should hold the claim in trust for him. Accordingly in such cases the stranger or volunteer should then be entitled to reimbursement in case of subsequent ratification and otherwise to subrogation. *Neely v. Jones*, 16 W. Va. 625; *Crumbish v. Central Implement Co.*, 38 W. Va. 390; *Kenan v. Holloway*, 16 Ala. 53, 5 Pom. Eq. Jurispr. (2d ed.) 912, 921 d. See *Gifford v. Corrigan*, 117 N. Y. 257, 22 N. E. 756.

²⁵ *Warford v. Hankins*, 150 Ind. 489, 493; *Clark v. Marlow*, 149 Ind. 41; Brandt on Suretyship 325; 5 Pom. Eq. Jurispr. 2347.

²⁶ *Prairie State National Bank v. United States* (supra).

tates.²⁷ In the last paragraph of the dissenting opinion the writer expresses his inability "to see why a surety who has guaranteed against its principal's default should avail itself of that default and recover as against a creditor who has in good faith loaned its money to pay for labor and materials furnished that surety's principal." It seems rather inaccurate to say that the surety is availing itself of the default of the principal. As for the proposition that the bank has loaned its money in good faith to pay off laborers and materialmen who were creditors of the surety's principal, the answer would be that it loaned the money on the credit of that principal and not at the request of the surety, knowing that the surety had an equitable lien upon the reserved fund ahead of the bank, and which could not be impaired by the assignment to the bank.

There are authorities which state the rule broadly, and perhaps without regard to its full legal significance, that subrogation will not be granted where one of the funds consists of the liability of a surety. For example where one creditor can proceed either against the property of the principal debtor or against a surety, and another creditor can proceed only against the property of the principal debtor, the former creditor ordinarily cannot be compelled to proceed against the surety and permit the other creditor to collect his debt from the principal, and the reason assigned is the one above stated.²⁸ It is submitted that this broad statement ought to be qualified by adding "unless the equity of the one seeking subrogation is superior to the equity of the surety." The usual application of the rule is shown in the following class of cases. Separate lands of a husband and wife are mortgaged to secure the debt of the husband. A junior mortgage is executed by the husband upon his own land. It has been generally held that the junior mortgagee cannot compel the senior mortgagee to first exhaust the property of the wife because her equity is equal or superior to that of the junior mortgagees.²⁹ Other cases involving substantially similar situations deny marshaling or subrogation against a

²⁷ *Pace v. Pace's Admr.*, 95 Va. 792; II Williston on Contracts 1265; 18 R. C. L., p. 456.

²⁸ 5 Pom. Eq. Jurispr. (2d ed.) 2291; *Ex parte Kendal*, 17 Ves. 520; *Swift & Co. v. Kortrech*, 112 Fed. 709; *Trentman v. Eldridge*, 98 Ind. 525; *In re Hobson*, 81 Ia. 392, 46 N. W. 1095; *Woolen v. Hillen*, 9 Gill. 185, 52 Am. Dec. 690; *Dorr v. Shaw*, 4 Johns. Ch. 17; *Hall v. Myer*, 48 W. Va. 353, 37 S. E. 594.

²⁹ *Swift & Co. v. Kortecht* (supra); *Gaines v. Hill*, 147 Ky. 445, 144 S. W. 92; *Stewart v. Stewart*, 209 Pa. 59, 56 Atl. 323; *Zeller v. Henry*, 157 Pa. 1, 27 Atl. 559; *Shinn v. Smith*, 79 N. C. 310.

surety but in all of them the facts show that the junior creditor has no superior equity against the surety.³⁰ In many of the cases the courts qualified the holding with such words as "unless he has the superior equity" as in *Trentman v. Eldridge*,³¹ or "in the absence of some special equity" as in *In re Hobson*.³² In the latter case the court states the true principle of marshaling assets as follows:

"In the absence of some special equity, it is not applicable to a case where one of the funds is the property of a surety. If a surety be compelled to pay the debt of his principal, he becomes his creditor by virtue of the payment with the right of subrogation."

Where the surety has no such right of subrogation, or reimbursement either because he has postponed his right to that of the creditor or because for some other reason the creditor has a superior equity, such a "special equity" arises and no reason exists for refusing marshaling or subrogation against the surety. In two cases the courts have found circumstances to exist that rendered the equity of the creditor superior to that of the surety and entitled the creditor to subrogation even against a surety.³³ It would seem therefore that the true statement of the rule would be that marshaling or subrogation will be granted although one of the funds is the liability of a surety, provided that the equity of the one seeking relief is superior to that of the surety.

It has been further stated that the rule is only applicable between creditors of one debtor and that both funds must belong to one debtor.³⁴ For example where one creditor has a claim against two debtors and another creditor has a claim against but one of them, the latter cannot as a rule require the joint creditor to proceed to collect his debt from the one against whom the other creditor cannot resort. The principle here is the same as in the case of the surety. In the case of the surety his right to reimbursement usually fixes his equity as superior to that of the one seeking relief by marshaling or subrogation. In the case of joint debtors the one paying has a right not of reimbursement (as in the case of the ordinary surety) but of

³⁰ *Union Bank v. Laird*, 2 Wheat. 390, 4 U. S. (L. Ed.) 269; *Thompson v. Spittle*, 102 Mass. 207; *Mason v. Hull* (Ohio), 45 N. E. 632; *Jenkins v. Smith*, 48 N. Y. Supp. 126.

³¹ 98 Ind. 525.

³² (Ia.) 46 N. W. 1095.

³³ *Massachusetts Bonding & Ins. Co. v. Chouteau Trust Co.*, 264 Fed. 793; *Chouteau Trust Co. v. Massachusetts Bonding & Ins. Co.*, 1 Fed. 136.

³⁴ 5 Pom. Eq. Jurispr. (2d ed.) 2291.

contribution which gives him a paramount equity to that of the one seeking relief. To compel the joint creditor to collect his debt from the one not liable to the other creditor, or to allow subrogation in the latter's favor would defeat an equal or superior equity and for that reason the statement has been made that there must be a common debtor. The same qualification should be made, it is submitted, to the so-called common debtor requirement, that was suggested in case of the surety. Where there is some supervening equity which makes the equity of the surety or of the other joint debtor inferior to that of the one seeking marshaling or subrogation, the superior equity should be recognized and relief granted by way of marshaling or subrogation, even though a surety or joint debtor is involved. This so-called common debtor requirement was first stated by Lord Eldon in *Ex parte Kendall*³⁵ as follows:

"We have gone this length. If A has a right to go upon two funds, and B upon one, having both the same debtor, and the funds are the property of the same person, A shall take payment from that fund to which he can resort exclusively, so that both may be paid. But it was never said, that if I have a demand against A and B, that a creditor of B shall compel me to go against A without more. If I have a demand against both, the creditors of B have no right to compel me to seek payment from A if not founded in some equity, giving B for his own sake, as if he was surety, etc., a right to compel me to seek payment of A. It must be established that it is just and equitable that A ought to pay in the first instance, or there is no equity to compel a man to go against A, who has resort to both funds."

The case recognizes that where there is some supervening equity whereby the entire debt should be paid by the debtor against whom the junior creditor has no right, marshaling or subrogation will be granted even though there is no common debtor.³⁶ In *Boone v. Clark*³⁷ the court states that the principle of marshaling assets does not apply where a creditor has a lien upon two funds of two separate debtors, and a creditor of one of

³⁵ 17 Ves. 514, 520.

³⁶ The following authorities recognize that supervening equities may render the common debtor requirement inapplicable. *Ayres v. Husted*, 15 Conn. 503, 515; *Dorr v. Shaw*, 4 John. Ch. 17; *Lloyd v. Galbraith*, 32 Pa. St. 103; *Rixey v. Pearre* (Va.), 15 S. E. 498; *Sanders v. Cook*, 22 Ind. 436, 439, and the courts have not only recognized but allowed subrogation in the following cases: *Wise v. Shepard*, 13 Ill. 42, 47; *Huston's Appeal*, 69 Pa. St. 485; *Hodges v. Hickey* (Miss.), 7 So. 404; *Merchants Nat. Bank v. Stanton* (Minn.), 56 N. W. 821; *Clark v. Manufacturers Mut. Fire Ins. Co.*, 130 Ind. 332. See also *Sterling v. Brightbill* (Penn.), 5 Watts 229; *Adams v. Young*, 200 Mass. 588, 86 N. E. 942.

³⁷ 129 Ill. 466, 21 N. E. 850.

the debtors has a lien upon one of the funds. However the opinion cites as authority *Wise v. Shepard* where the equitable exception to the rule is both recognized and applied.

In legal effect joint debtors are as between themselves each principals as to half and sureties as to half. They are only different from sureties in that the surety is generally entitled to full reimbursement if compelled to pay whereas they are only entitled to half. Equity will protect either the surety or joint debtor therefore unless there is some special equity by reason of which marshaling or subrogation should be granted in spite of the fact that the one against whom it is sought is a surety or is not a common debtor. The authorities cited in the case of a surety are therefore equally applicable to the common debtor requirement.

The real determination of the right to marshaling and reimbursement in this class of cases should therefore depend upon who has the superior equity. It is a misapplication of the maxim to decide the cases on the ground that equity will not aid a volunteer. Moreover the requirement of a common debtor is not sound nor is the statement that relief will not be granted where one of the funds is the liability of a surety. The reason for the common debtor requirement and the surety exception is that ordinarily they have the superior equity, but that result need not necessarily follow and the repetition of that principle may result in a failure to look into the equities and thus reach a wrong result.