[HIGH COURT OF AUSTRALIA.]

WILLIAMS AND ANOTHER . . . . APPELLANTS;
PLAINTIFFS,

AND

FRAYNE AND ANOTHER . . . . RESPONDENTS.
DEFENDANTS,

ON APPEAL FROM THE SUPREME COURT OF VICTORIA.

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MELBOURNE, *Mar.* 9, 10.

SYDNEY, *April* 21.

Latham C.J., Rich, Dixon and McTiernan JJ.

Guarantee—Lease—Assignment to creditor as security—Failure of creditor to obtain landlord's consent—Omission to exercise option to renew lease—Breach of covenant—Novation—Agreement to give time to debtor—Property Law Act 1928 (*Vict.*) (*No.* 3754), *sec.* 146.

A tenant under an agreement for a lease of business premises borrowed money from a merchant supplying his stock and assigned his interest under the lease to the lender, the loan being guaranteed. The landlord's consent was not obtained to the assignment as required by the agreement for the lease. The tenant sold the business carried on on the premises, and successive resales took place to different purchasers; each purchaser took possession and paid the rent directly to the landlord and dealt directly with the lender, who by his books treated the purchaser for the time being as his debtor. Finally, the last purchaser at a time prior to the expiration of the agreed term obtained a new lease from the landlord in substitution for the old. The landlord was unaware that the old lease had been assigned to the lender as a security. In an action brought by the borrower and the guarantor for a declaration that they were discharged from repayment of the loan, both plaintiffs relied on novation alleged to arise from the buyers of the business having been accepted as substituted debtors. The guarantor pleaded a discharge by reason of the creditor's having given time to the debtor, and by his having negligently failed to preserve the security by failing to procure the landlord's consent to the assignment of the agreement and by failing to exercise an option to extend the original term.

Held (1) that any inference or implication that the lender agreed to substitute the purchasers or any of them for the borrower as his creditor was excluded by express evidence of a contrary intention; (2) that, if the lender did agree to refrain from calling up the loan while the purchasers continued to deal with him, it was done at the request of the guarantor, who was therefore not released; (3) that, assuming the lease arising from the agreement was lost as a security owing to failure to give the landlord notice of the assignment and obtain his consent, the guarantor was not discharged either wholly or *pro tanto*, because (i.) the omission was not a departure from the contract between the parties on the faith of which the guarantee was given; (ii.) it was not a neglect or default on the part of the lender of which the guarantor could complain; (iii.) as the covenant against assignment had been broken, the agreement for a lease was not specifically enforceable and gave no equitable term, and at best a tenancy from year to year only had subsisted.

Decision of the Supreme Court of Victoria (*Macfarlan* J.) affirmed.

APPEAL from the Supreme Court of Victoria.

Walter Herbert Williams was in possession of certain premises in Main Street, Stawell, under an agreement in writing dated 26th February 1932 for a lease from Robert Hill McCracken. The tenancy was for three years from 29th February 1932 with an option in the tenant to renew for a further two years, the tenant agreeing not to sub-let without the consent in writing of the landlord. Under an agreement dated 27th April 1932 Walter Herbert Williams obtained a loan of £800 from George Frayne and Henrietta Ann Tyree for the purpose of purchasing a bakery business carried on on the premises, Clifford John Williams guaranteeing the loan and being joined as a party to the agreement. The loan was to be repaid by twenty equal quarterly instalments of £40 each, which the guarantor covenanted to repay in case of default by the borrower. For better securing the loan the borrower assigned to the lenders his interest in the agreement for the lease dated 26th February 1932 and the guarantor also provided certain security. The agreement also provided that in case of default by the borrower the lender should be at liberty to sell the borrower's interest in the agreement for lease dated 26th February 1932 and provided that the term "borrower" should include his transferees. The agreement further provided that if the borrower should sell the bakery business carried on by him on the premises the balance of the sum due should thereupon become payable. On 1st June 1932 Walter Herbert Williams sold

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the bakery business to one Holmes, who subsequently sold it to one Dobvitz, who again sold it to one Purse. In December 1933 Purse obtained from McCracken a new lease of the premises. No notice of the original assignment from Walter Herbert Williams to the lenders of the original agreement for a lease from McCracken to Williams was ever given to McCracken, and there was a conflict of evidence as to whether the lenders had or had not substituted each new purchaser for Walter Herbert Williams as debtor in respect of the balance of the £800.

Clifford John Williams and Walter Herbert Williams brought an action in the Supreme Court of Victoria against George Frayne and Henrietta Ann Tyree claiming a declaration that they were discharged from all liability under the loan agreement of 27th April 1932, an injunction restraining the defendants from enforcing the agreement or realizing the securities assigned to them, and an order directing the defendants to re-assign to the plaintiffs the securities assigned to them under the agreement of 1932. The defendants counterclaimed for £594 12s., the outstanding amount of the debt. The action was heard by *Macfarlan* J., who gave judgment for the defendants on the claim and also on the counterclaim.

From that decision the plaintiffs appealed to the High Court.

Gorman K.C. and *O'Driscoll*, for the appellants. There was an implied novation. There was a binding agreement to give time to the debtor or to Holmes, the first purchaser, who became the debtor under the novation. The defendants wasted the security. They were trustees of the lease for the guarantor, and loss of the lease relieves the guarantor. The defendants knew that the various purchasers were paying rent direct to the landlord as tenants. The acceptance of the new lease operated as a surrender of the lease assigned by way of security. At any rate, the defendants would be estopped as against the landlord from challenging the validity of that new lease. It was the basis of the guarantee that the lease should be preserved as a security available to the guarantor on payment by him of the debt. The defendants were guilty of a breach of a term implied in the contract of guarantee in that they failed to notify the landlord of the original assignment of the lease,

such notification being a necessary step to preserve the security. The defendants committed a breach of the contract of guarantee in failing to exercise the option for the extension of the lease. The defendants, as creditors, were guilty of conduct which reacted injuriously to the surety (*Watts* v. *Shuttleworth* (1)). The guarantor had a right to the full and complete benefit of the security (*Newton* v. *Chorlton* (2)). The plaintiffs are entitled to relief on general principles of equity (*Craythorne* v. *Swinburne* (3) ; *Price* v. *Kirkham* (4)).

O'Bryan (with him *Smithers*), for the respondents. No implied novation was pleaded. The evidence accepted by the trial judge is conclusive against an implied novation and also against a release of the principal debtor. There is no evidence of any binding agreement to give time to the debtor other than with the guarantor's concurrence. A binding agreement to give time to a third person is no ground of relief of the guarantor (*Frazer* v. *Jordan* (5)). When the defendants received the security the contract of guarantee was complete. The guarantee and assignment of the lease were contained in the same document. The assignment itself, without consent of the landlord, was a breach of a condition in the lease. Holmes, the first purchaser, was really put into possession by reason of the activities of the guarantor, who understood he would pay rent direct to the landlord. The defendants had no right to prevent the purchasers of the business from taking possession. It was not necessary to give to the landlord notice of the assignment; either there was no obligation to do so arising out of the contract of guarantee (*Polak* v. *Everett* (6)), or, so far as the assignment operated as a transfer of a legal right, it operated of its own force, and a tenancy from year to year vested in the defendants and could not be divested unless the owner of the term surrendered it or did some other act to dispose of it. The defendants, therefore, still have that tenancy from year to year. The legal interest has not been lost by reason

(1) (1861) 7 H. & N. 353 ; 158 E.R. 510.
(2) (1853) 10 Ha. 646, at pp. 651, 652, 654, 656, 659 ; 68 E.R. 1087, at pp. 1089, 1090, 1091, 1092.
(3) (1807) 14 Ves. 160 ; 33 E.R. 482.
(4) (1864) 3 H. & C. 437 ; 159 E.R. 601.
(5) (1857) 8 E. & B. 303, at pp. 310, 311 ; 120 E.R. 113, at pp. 115, 116.
(6) (1876) 1 Q.B.D. 669.

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of the new lease (*Parker* v. *Jones* (1)). Purse, the purchaser to whom the landlord gave the new lease, had no interest in the original term and accordingly could not surrender it. Notice of assignment, so far from preserving the security, might have led to the forfeiture of the lease. As to the exercise of the option.—The time for its exercise never arose. And it could not be considered to be part of the contract of guarantee that the defendants should exercise the option and thus acquire the obligation of a further two years' rent. If the defendants were at fault, the result should be to effect a discharge *pro tanto* only (*Rowlatt* on *Principal and Surety*, 3rd ed. (1936), pp. 289, 290 ; *Northern Banking Co.* v. *Newman & Colton* (2)).

O'Driscoll, in reply, referred to *Purchase* v. *Lichfield Brewing Co.* (3) ; *Smith* v. *Butler* (4) ; *Day* v. *Singleton* (5) ; *McLeod* v. *Cardiff Colliery Co. N.L.* (6) ; *Midland Motor Showrooms Ltd.* v. *Newman* (7).

Cur. adv. vult.

April 21. The following written judgments were delivered :—

LATHAM C.J. This is an appeal from a judgment of *Macfarlan* J. in an action by a debtor and his surety claiming a declaration that they are not liable for the debt guaranteed. There was a counterclaim for the amount of the guaranteed debt. Judgment was given for the defendants on the claim and also on the counterclaim. The surety has appealed to this court. There is no appeal by the principal debtor.

One W. H. Williams, in order to buy a baker's business, obtained a loan of £800 from the defendants under an agreement made on 27th April 1932. The parties to the agreement were the plaintiff W. H. Williams, the defendants, and the plaintiff C. J. Williams as surety. The borrower, W. H. Williams, agreed to repay the sum of £800 by twenty equal quarterly instalments of £40 each. C. J. Williams, as guarantor, covenanted that he would on demand pay

(1) (1910) 2 K.B 32.
(2) (1927) I.R. 520, at pp. 530, 538.
(3) (1915) 1 K.B. 184.
(4) (1900) 1 Q.B. 694.
(5) (1899) 2 Ch. 320.
(6) (1924) V.L.R. 430 ; 46 A.L.T. 45.
(7) (1929) 2 K.B. 256.

the lenders the moneys due if payment had not been made by the borrower. For the better securing repayment, the borrower, W. H. Williams, assigned to the lenders "all his . . . right title and interest as lessee under a lease dated the 26th day of February 1932" made between him and one McCracken. The guarantor also, to support his guarantee, assigned to the lenders his interest under a contract of sale and his interest in a lease. The agreement provided that the expression "borrower" should, wherever the context so admitted or required, be deemed to mean the heirs, executors, administrators or transferees of the borrower. It was further provided that, if the borrower at any time during the term of the agreement sold the baker's business carried on by him at the premises which he had leased from McCracken, the balance of the sum of £800 then owing should thereupon become due and payable. The guarantor, C. J. Williams, contended that he had been released from liability as surety for the following reasons:—

(1) It was alleged that there had been an express agreement by way of novation whereby the defendants had released the principal debtor, W. H. Williams, and had accepted the liability in turn of persons who succeeded him in ownership of the business. This argument was abandoned in this court.

(2) It was contended for the guarantor that if there had not been an express novation there was an implied novation to be inferred from the conduct of the parties.

(3) The guarantor also contended:—(*a*) That the creditors had made a binding agreement with the principal debtor giving him time to pay. (*b*) That the creditors had been guilty of default by deliberately or negligently impairing the security constituted by the assignment of the lease to them by the principal debtor. The default alleged was that, as the agreement for the lease of the premises (referred to in the documents as a lease) provided that it should not be assigned without the consent of the landlord it was the duty of the creditors to obtain such consent; they assigned the lease to the creditors without applying for or obtaining such consent, and therefore the lease could be determined by re-entry and the value of the assignment was accordingly impaired by this default of the creditors in breach of their duty to the surety.

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Associated with this argument was another argument that the creditors in breach of their duty to the surety had permitted various persons in succession to occupy the premises and that when a transferee of the business named Purse went into occupation he obtained a new lease from the landlord which, it was suggested, had the effect of terminating the lease which had been assigned by way of security to the creditors. (c) That the agreement for a lease contained an option to the lessee for renewal for two years exercisable upon the expiry of the term. It was urged that the defendants had not exercised this option and had therefore impaired the security to which the guarantor would have been entitled if he had paid the debt.

Implied Novation.—On this aspect of the case the learned judge found against the plaintiff. He held that none of the parties at any time believed that the liability of the principal debtor had been extinguished or that the liability of any other person had been substituted therefor. The evidence relied upon to support an implied novation is to be found in the fact that certain transferees of the business did make payments to the principal creditors of £40 a quarter from time to time, and that these payments were credited against the liability of the principal debtor. These facts are fully explained by the fact that these transferees undertook with their predecessors in the business to keep up these payments, but there is no evidence in these facts alone that they entered into an undertaking with the creditors. The other evidence which is relied upon for the purpose of supporting the alleged implied novation is to be found in ledger entries in books of the defendants. These entries show that the liability of W. H. Williams on the £800 was shown as transferred to the various transferees of the business. These facts were naturally strongly relied upon by the plaintiffs. But the book-keeper who made the entries was called and gave an explanation of his entries which the learned judge accepted. The explanation was to the effect that he was not a skilled book-keeper and that he did not mean by the manner in which he made the entries to indicate or show there had been any extinguishment of the liability of W. H. Williams. The learned judge accepted this explanation, though it has some weaknesses, and it is difficult for this court as a court of appeal to reject it. The acceptance of the

explanation depended upon the view taken by the trial judge of the honesty of the witness and I do not think that, in the absence of convincing reasons, as distinct from not unreasonable criticism, this court, as a court of appeal, can reject the conclusion of the learned judge who saw and heard the witness. Thus the plaintiff's case, so far as it is based upon implied novation, fails.

Binding agreement to give time to principal debtor.—There is no doubt that the defendant creditors did give time to the principal debtor. The agreement under which the advance was made provided that if the business were transferred by the borrower the whole sum should become due. The business was transferred and the defendants did not claim the payment of the balance at the time of any of the first or subsequent transfers but allowed the amount to run on and accepted quarterly payments on account. It is clear, however, that this procedure was initiated with the knowledge and consent of the guarantor. His own statement shows that on the occasion of the first transfer of the business (to one Holmes) he asked that the balance should not be called up and that the defendants agreed. He cannot now be heard to complain of something that was done at his request. On the occasions of subsequent transfers of the business the balance of the amount owing was not called up. It is very doubtful whether the clause providing that the balance should become payable on the transfer of the business could operate on the occasion of subsequent transfers of the business, but it is not necessary to examine this question because there is no evidence of a binding agreement to give time to the principal debtor. A promise to the creditors by the new owner or owners of the business to pay the amount owing would have been a consideration for an undertaking by the creditors to give time to the principal debtor. But there is no evidence of any such promise, and no other possible consideration is suggested. There was therefore no binding agreement to give time.

Default of creditors in not preserving or protecting security constituted by the assignment of the lease.—It is not disputed that, if a principal creditor has made a contract whereby he has undertaken to perfect or preserve a security and he breaks that term of the contract, the result may be that a surety for the debt is discharged. There was

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in this case, however, no contract, express or implied, that the creditors should do anything with respect to the lease or agreement for a lease which had been assigned.

Further, however, reliance is placed upon the equitable principle that a surety is entitled, on payment by him of the guaranteed debt, to a transfer of all the securities held by the creditor in respect of the debt in the same condition as that in which they were originally received, so that if the creditor interferes with or impairs this right, the surety is relieved from liability, at least to the extent of any loss inflicted, and, possibly (if the act of the creditor in relation to the securities really substantially alters the relations between the parties without the consent of the surety) the latter may be discharged altogether from his liability.

It is sought to apply this principle to the lease which was assigned by W. H. Williams as security for the payment of the debt by him to the creditors.

In order to examine this contention it is necessary to consider the provisions of the agreement for a lease between McCracken and W. H. Williams relating, first, to the assignment of the leased premises, and, secondly, to the option of renewal of the lease.

In the first place it should be observed that the document which records the transaction between McCracken the landlord and W. H. Williams is not a lease but is an agreement for a lease and is not under seal. It was executed on 26th February 1932 and provided that the landlord agreed to let and the tenant to take the premises in question at a weekly rent of £2 7s., the tenancy to commence on 29th February 1932 (i.e., a future date) and not to cease except as thereinafter provided (upon breach of covenant) until notice in writing had been given by one party to the other, such tenancy to continue for a term of three years at the least. The landlord also agreed "to give the tenant a further option of two years on expiry of this lease." It has been assumed in argument that this agreement for a lease (the term being for a minimum of three years from a future date with a possible extension) does not fall within the provision of the *Property Law Act* 1928, sec. 54 (derived from the Statute of Frauds) which permits certain leases taking effect in possession for a term not exceeding three years to

be made otherwise than by deed. Upon this basis W. H. Williams did not obtain any legal estate by virtue merely of the existence of the document, because the document purporting to create the interest was not made under seal. He, however, entered into possession under the agreement and paid rent. He was therefore entitled in equity to hold under the terms of the agreement and could have brought an action for specific performance. He therefore must, in all courts having full equitable jurisdiction (*Foster* v. *Reeves* (1)), be regarded as holding on the same terms as if a lease had been granted (*Walsh* v. *Lonsdale* (2)).

The agreement contained the following provision : " The tenant hereby agrees not to sub-let, lease or assign over, nor in any way dispose of or part with the possession of the said shop and premises or any part thereof to any person whatsoever . . . without the consent in writing of such landlord." W. H. Williams did assign all his right, title and interest as lessee under this document to the creditors by way of security for the debt which he owed. The assignment was made without the consent in writing, or any consent or knowledge, of the landlord. Thereafter the tenant, having broken the contract, was not in a position to claim specific performance (See *Hill* v. *Barclay* (3)) so as to gain the advantage of applying the principle of *Walsh* v. *Lonsdale* (4). Thus he was a tenant who had entered into possession of premises under a lease void at law of which he was unable to obtain specific performance. If so, it was said, he then became a tenant from year to year. I do not agree with the argument if it is put in this way. The argument, so expressed, depends upon the well known case of *Walsh* v. *Lonsdale* (4), but it is, I think, not consistent with what was actually said in that case. *Jessel* M.R. says very definitely :—" There is an agreement for a lease under which possession has been given. Now since the *Judicature Act* the possession is held under the agreement. There are not two estates as there were formerly, one estate at common law by reason of the payment of the rent from year to year, and an estate in equity under the agreement. There is only one court, and the equity rules prevail in it. The tenant holds

(1) (1892) 2 Q.B. 255.
(2) (1882) 21 Ch. D. 9, at p. 15.
(3) (1811) 18 Ves. 56, at p. 63 ; 34 E.R. 238, at p. 241.
(4) (1882) 21 Ch. D. 9.

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under an agreement for a lease. He holds, therefore, under the same terms in equity as if a lease had been granted, it being a case in which both parties admit that relief is capable of being given by specific performance" (1). If this statement accurately describes the position, the tenant in the present case had one estate only—namely, a tenancy for three years (with a possible extension). That estate could not be turned into another estate—a tenancy from year to year—by the fact that one party, by committing a breach of the agreement, lost his right to specific performance. The result of the stated principle of the decision in *Walsh* v. *Lonsdale* (2) is that the tenant, by his entry into possession under the agreement, placed himself in the position of actually holding, in any court where the rules of equity prevail and can be enforced, upon the terms of the agreement.

But, as *Maitland* says (*Lectures on Equity*, 2nd ed. (1936), at p. 156) *Walsh* v. *Lonsdale* (2) is "a somewhat difficult and dangerous case." Despite the clear language of *Jessel* M.R. denying the existence of two estates, it must be taken that in such a case as *Walsh* v. *Lonsdale* (2) there are still two estates—a legal estate and an equitable estate. As *Maitland* says:—"An equitable right is not equivalent to a legal right; between the contracting parties an agreement for a lease may be as good as a lease; just as between the contracting parties an agreement for the sale of land may serve as well as a completed sale and conveyance. But introduce the third party and then you will see the difference. I take a lease; my lessor then sells the land to X; notice or no notice my lease is good against X. I take a mere agreement for a lease, and the person who has agreed to grant the lease then sells and conveys to Y, who has no notice of my merely equitable right. Y is not bound to grant me a lease" (*Maitland*, 2nd ed. (1936), at p. 158). *Swain* v. *Ayres* (3) shows that if a tenant who has entered under an agreement for a lease loses the right to specific performance which he originally had, he cannot be considered as holding upon the same terms as if a lease had been granted. Accordingly, in the present case if the tenant did not acquire a legal estate for at least three

(1) (1882) 21 Ch. D., at p. 14. (2) (1882) 21 Ch. D. 9.
(3) (1888) 21 Q.B.D. 289.

years the position is that, upon entering and paying rent under the agreement for a lease, he became at law entitled to hold as a tenant from year to year upon the terms of the agreement so far as they were consistent with a tenancy from year to year. He originally also had an additional right as against the landlord to obtain specific performance and could have obtained a decree for the granting of a lease in accordance with the agreement. If he had obtained such a lease, he would have had a legal tenancy for at least three years. But as matters were, the only additional right which he had was a right, as against the landlord, to be treated in the same way as if such a lease had been granted. He lost this right when he lost the right to specific performance by reason of his breaking the term of the agreement forbidding assignment without the previous consent of the landlord. He therefore remained merely a tenant from year to year without any superadded equitable right.

But, however the argument may be put, the lessee was bound by the provision that he should not assign without the consent in writing of the landlord. The assignment of his interest to the creditors without the previous consent of the landlord was a breach of this provision which entitled the landlord to re-enter after giving notice under sec. 146 of the *Property Law Act* 1928. This fact constitutes the basis of the contention on behalf of the surety that the defendant creditors were guilty of a breach of duty which impaired the value of the lease which they held as security for the debt.

It has been argued for the surety that it was the duty of the assignees, the defendant creditors, to protect the interest which was assigned to them by obtaining the consent of the landlord to the assignment, and that this was a duty which was owing to the surety. But in fact the relation of suretyship was created by the document which purported to make the assignment, and the duty of the creditors cannot possibly have been greater than to protect, preserve or perfect the security which was actually transferred to them at that time. So far as the absence of consent operated prejudicially to the assignees' interest, the damage, if any, had already been done. The agreement for a lease did not provide that an assignment should not be made unless the consent of the landlord

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were obtained within some period after the assignment. It provided that no assignment should be made without the consent of the landlord. Therefore the complaint that the creditors did not obtain the consent of the landlord, when applied to the facts of the case, really becomes a complaint that the creditors, before accepting the assignment of the lease as a security, did not take pains to see that the assignment had been made safe by reason of the prior consent of the landlord having been obtained. This is a complaint that the creditors accepted an imperfect or incomplete security. But the duty of the creditors to protect, preserve or perfect securities in the interests of the surety cannot possibly be alleged to have come into existence until the relationship of surety has been constituted. Thus, in my opinion, upon any view, there was no duty resting upon the creditors to obtain the consent of the landlord.

It has further been urged that the creditors should have given notice of the assignment to the landlord. There is no substance in this argument. Giving notice of the assignment after it had been made would not have improved the position so far as the rights of the parties were concerned and might possibly have affected them prejudicially, because the landlord might, upon learning of the assignment, have exercised his right of re-entry, thus determining the tenant's interest. In my opinion, therefore, there is no ground for the allegation that the creditors were subject to an obligation as between themselves and the surety either to obtain the consent of the landlord prior to the assignment or to give him notice thereof after the assignment. Thus it is unnecessary to consider whether the failure of the creditors to perform the alleged obligation has prejudicially affected the surety.

In December 1933, before the three years from the beginning of the tenancy had expired, the landlord granted a new lease to one Purse, a transferee of the business. There was no surrender of the lease which had been assigned to the creditors. *Macfarlan* J. held that the old tenancy was not affected by the fact that the landlord purported to grant a lease of the premises to another person. My brother *Dixon*, on the other hand, gives weighty reasons for a contrary view. In my opinion it is unnecessary for me to examine this question, because I can discover no evidence that the creditors

had any share in bringing about the granting of the new lease. If such grant did prejudicially affect the surety (which, in my opinion, is not shown to be the case) this result is not due to any default on the part of the creditors.

It was also argued that, as the agreement for a lease contained an option for renewal, the creditors should have exercised the option in order to protect the rights of the surety. No authority has been cited to support the proposition that the principle requiring a creditor to protect securities in the interest of a surety requires him to undertake a new obligation by taking an extension of a lease and paying rent thereunder. If the term of the lease still exists, the option is still exercisable. If the term has expired, the option is not exercisable, but, as I have already said, it is not shown that the creditors were responsible for this result. If further evidence showed, as may well be the case, that W. H. Williams, the original tenant, has abandoned his rights under the lease so that his tenancy, together with the option, has been determined by an acceptance by the landlord of such abandonment, this result would be due to the conduct of the landlord and W. H. Williams, and not to any act or default of the creditors.

Thus, in my opinion, the learned judge was right in refusing to declare that C. J. Williams was no longer bound by his guarantee and in giving judgment against him for the amount of the debt guaranteed.

The appeal should be dismissed.

Since the institution of this appeal the respondent George Frayne has died. It is ordered by consent that the Ballarat Trustees Executors and Agency Co. Ltd. and Bessie Frayne the executors of the will of George Frayne deceased be joined as respondents to the appeal, any liability arising from such joinder being limited to the assets in the estate of the said George Frayne.

RICH J. The facts in this case are already in statement and I need not repeat them. Although the appellant presented an argument of prima facie plausibility in support of the various grounds upon which he contends he has been discharged wholly or *pro tanto* from the liability under the guarantee, the examination

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to which they have been subjected has, in my opinion, disposed of all of them. If we were to confine ourselves to the documents there would be much to be said in favour of the novation upon which the appellant relied. The ledger account considered in relation to the circumstances of the case and to the tenor of the original agreement suggests the likelihood of the tripartite agreement tacitly made substituting the first purchaser of the business for the appellant's brother as the immediate debtor of the respondents. It shows that the respondents looked upon each successive purchaser as their debtor. But it is not enough that they should regard a purchaser as if he owed them the money which, as between them and his vendor, he had undertaken to pay. There must be a common intention to effect the substitution. The evidence which *Macfarlan* J. must be taken to have accepted definitely negatives such an intention. According to that evidence there was an express statement on the part of the creditors that there would be no substitution releasing the debtor. It follows that the appeal cannot succeed on the ground of novation.

As the argument progressed it became apparent that there had been no agreement between the respondents and the principal debtor binding the respondents to give time to the latter. But there was evidence of an agreement between the respondents and the purchaser of the business not to call up the money owing by the principal debtor, the payment of which the purchaser had undertaken. Unfortunately for the appellant the transaction was negotiated by him and it was through him that the request was made to allow repayment by instalments to go on. He must be taken to have consented and, therefore, cannot complain.

The ground that the respondents had lost or sacrificed the security which they took from the principal debtor was presented in various aspects, but, in my opinion, in no aspect can it succeed. It was said that the option contained in the lease was lost for various reasons which it is unnecessary to particularize. The short answer is that from the assignment of the lease as security the option ceased to be enforceable against the lessor. The assignment was a breach of condition and specific performance of the option if exercised could not be obtained. There was, therefore, never any effective security

over an option. The " lease " did not take effect in possession and was for a term of three years. In fact the " lease " was an agreement for a lease. Owing to the breach of condition it was not specifically enforceable and no equitable term within *Walsh* v. *Lonsdale* (1) continued to subsist after the assignment. Of course a common law tenancy arose from entry and payment of rent (See *Moore* v. *Dimond* (2), where the reasons for implying a tenancy from year to year as opposed to a lesser recurring period are explained). But a tenancy from year to year liable to be determined by breach of condition affords no very valuable security for the debt owing to the assignee of the term. Such as it was it appears to have been lost when the new lease was granted to the purchaser Purse, if not before when rent was accepted by the landlord from the first purchaser as tenant. If Purse were assignee of the old lease as the landlord believed, the grant of a new lease to him would involve a surrender by operation of law of the existing tenancy from year to year. I cannot think that the respondents who suppressed from the landlord all knowledge of the assignment to them and allowed Purse with their knowledge to assume the position of assignee of the previous tenants would remain at liberty to set up their tenancy from year to year against the new term. It is just as if they had consented to the grant of a new lease. They are precluded from denying its efficacy. But the main fact which leads to their estoppel is the failure of all parties at the time of the assignment of the original term to obtain the landlord's consent. The subsequent failure to disclose the assignment was the natural if not necessary consequence of the fact that it was not a permitted assignment. No failure can be imputed to the respondents in continuing the non-disclosure. The original failure to obtain the landlord's consent is a matter preceding the creation of security and cannot be accounted negligence on the part of the creditors in dealing with the security. It probably arose from a misunderstanding, but whatever its cause the solicitors for all parties prepared the assignment and carried it through on the basis that the landlord should know nothing about it, and, in my opinion, it follows that none of the consequences of this non-disclosure can be relied upon by the appellant as surety as a discharge from

(1) (1882) 21 Ch. D. 9.

(2) (1929) 43 C.L.R. 105.

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his obligations. The security, in other words, was not lost through the neglect or default of the creditors in maintaining or protecting the only security they received, but through the defect or infirmity in the nature of the only security they obtained and from the course of conduct which it was necessary for them to pursue in consequence of that defect.

In my opinion the appeal should be dismissed.

DIXON J. The question at issue is whether a guarantor has been discharged from his liability either wholly or in part. The obligation of suretyship is included in an instrument of security under seal made between all three parties, the guarantor, the principal debtor and the creditors. The guarantor claims on three grounds that he was relieved of liability. He says that the principal debt was discharged by novation, that by the default of the creditors an interest over which the principal debt was secured was lost and that the creditors made an agreement by which for a period of time they were prevented from resorting to the principal debtor, or alternatively, to their security for immediate satisfaction of the debt.

The guarantor is the appellant, the principal debtor is his brother, by trade a baker, and the creditors are the respondents, who were flour-millers. The debt consists in the unpaid residue of an advance made by the flour-millers to enable the baker to purchase a bakery business. The premises at which the business was carried on were occupied under a tenancy, and upon purchasing the business the principal debtor obtained from the landlord an agreement for a lease for a minimum term of three years with a further option of two years, but to continue until terminated by notice. The instrument of security contained a covenant by the principal debtor, who was described as the borrower, to pay principal and interest, the former by twenty quarterly instalments, a covenant by the guarantor, incompletely expressed, but meaning that on demand he would pay principal and interest on the borrower's default, and an assignment of the borrower's interest as lessee under the lease of the bakery. By the same instrument, to further secure the advance, the guarantor also assigned a contract under which he had agreed to dispose of another bakery business, a business that had belonged to him.

The instrument defined "borrower," "lender" and "guarantor" as including the heirs, executors, administrators or transferees of the parties, and it provided that if the borrower at any time during the term of the instrument should sell the bakery business the balance of the advance then owing should become due and payable.

In this transaction the same solicitors acted for all parties. The lease of the bakery contained a provision against assignment without the landlord's consent and a condition of re-entry for breach. The instructions received by the solicitors from the creditors were to the effect that it was desired to avoid publicity and to leave the guarantor in receipt of some of the moneys arising from the security he had furnished. The creditors gave the instructions as a result of a discussion in which the guarantor had expressed himself as against a proposal to give a bill of sale, on the ground that he wanted the transaction kept as private as possible. Having been so instructed the solicitors, who were acting for all parties, did not inform the landlord. Neither they nor anyone else obtained the landlord's consent to the assignment and the landlord was never notified that it had taken place.

After some time the principal debtor sold the business. The guarantor was active in the sale, which he superintended, if he did not promote it. In the contract of sale the purchaser agreed to undertake the liability to the creditors for the unpaid balance of the advance. What passed between the creditors and the parties to this sale is a matter of dispute, but upon its taking place the ledger account in which the amounts falling due and the sums paid in respect of the advance were entered was altered so as to make it appear that the purchaser had replaced the vendor as their debtor. The purchaser entered into possession and appears to have paid rent to the landlord. But a few months later the purchaser again sold the business, and his purchaser resold it a month afterwards. In the ledger account the names of these successive purchasers were in turn substituted as if they were the debtors. In the contract of sale by which the earlier of them bought provision was made for the assignment of the lease of the premises. The transaction was made subject to the creditors' transferring the advance to the purchaser,

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who undertook with the vendor that he would enter into an agreement with the creditors, as flour-millers, to obtain all his flour from them. The later of these two purchasers bought under an open contract containing no conditions and describing the subject of the sale as the bakery business. But, after he had taken possession, he obtained from the landlord a new lease of the bakery for another term of three years, although the existing term had not expired. The landlord was unaware of the assignment of the former lease. About four months later, the business was again resold and, of course, the new lease was included in the sale. The quarterly repayments of the advance to the creditors had not been kept up, and shortly after the last sale they made recourse to the principal debtor and the guarantor, to whom they sent letters of demand. The latter instituted an action seeking to have it declared that they were no longer liable. The creditors counterclaimed for the unpaid balance of the original advance, £520, and interest which up to that date amounted to £74 12s. Judgment upon the claim and counterclaim was entered for them by *Macfarlan* J., who heard the action, and from that judgment the present appeal is brought.

The first ground taken in support of the appeal is that, when the principal debtor sold his business, the creditors agreed to substitute the purchaser for him as their debtor in respect of the balance of the advance and that as the principal debtor and the purchaser were parties to the agreement, a novation was thus effected discharging the principal debtor. It is said too, if it be material, that, as each succeeding purchaser took over the business, he was substituted as the debtor by novation. The novation relied upon is not express but tacit, an inference from circumstances. The entries in the ledger and the circumstances lend much support for the inference, but it is an inference of fact and not an implication of law, and it cannot be made in the face of an express communication of a contrary intention by one party to another. One of the witnesses deposed that the guarantor, who acted for himself and his brother, the principal debtor, was expressly informed, when he sought the creditors' approval for the first sale, that they had no objection to it provided that the principal debtor and the guarantor remained liable, and further that on the occasion of the second and third sales the parties

to those transactions were told that, as the principal debtor and the guarantor were responsible, they should be consulted. In his reasons for judgment *Macfarlan* J. did not deal specifically with this evidence, but he found against a novation and said that throughout he had been much impressed with the testimony of the witness, which broadly he accepted.

It would be impossible for a court of appeal to reject the statement that the continued reliance of the creditors upon the liability of the original parties was expressly mentioned if the learned judge believed it, and it seems almost certain that he did. We must, I think, treat the statement as having been made, and this, in my opinion, puts out of question the contention made on the part of the guarantor that the principal debt was discharged by novation. Even if there were a novation, it does not follow in the present case that the guarantor is discharged; for in defining "borrower" to include his transferees the instrument appears to provide against the very case.

But the same evidence contains the material relied upon for the further contention that the creditors precluded themselves for a space of time from enforcing their debt against the principal debtor or the surety. One object of applying to the creditors for their approval of the sale was to induce them not to put into effect the provision in the instrument making the residue of the advance immediately due and payable if the business was sold. According to the evidence, the guarantor requested the creditors to forgo their right to call up the balance outstanding, and to this they agreed, provided that the original parties remained liable. It is said that, whether there was or was not a novation and whether the promise resulted in a contract with the principal debtor or the ingoing purchaser, it at least bound the creditors to refrain from calling up the money and resorting to their securities to satisfy the whole debt. The argument is, in my opinion, entirely answered by the guarantor's own participation in the arrangement. He himself requested the creditors to allow repayment by instalments to continue, or so we must assume, and received the answer that so long as he and his brother remained liable the creditors would agree. A binding agreement to give time made with the surety's consent does not discharge the latter.

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The third ground upon which the guarantor relies is that through the default of the creditors the benefit has been lost of the lease of the bakery, by the assignment of which the principal debt was secured. This means that, owing to the omission to obtain the landlord's consent or to notify him of the assignment, and, perhaps, owing to further conduct of the creditors amounting to active encouragement, dealings have taken place between the landlord and the successive purchasers of the business who entered in possession of the premises, particularly the third to whom the new lease was given, as a result of which the creditors have lost the rights in respect of the security to which on payment of the principal debt the surety would otherwise be subrogated. The contention necessarily calls for some examination of the successive changes of interest in the tenancy of the premises and of the ultimate fate of the security given over the lease or agreement for a lease. The document itself was undoubtedly an agreement for a lease, not a lease. But the lessee, the principal debtor, before the date of the assignment had entered under it and paid rent and, no doubt, a legal tenancy from year to year had arisen (*Moore* v. *Dimond* (1)). In addition, he was before the assignment entitled in equity specifically to enforce the agreement and thus had as against the landlord an equitable term according to the tenor of the agreement. But, as the agreement for a lease contained a covenant against assignment without the landlord's consent, and as this was broken by the assignment to the creditors, the landlord became entitled to resist specific performance and consequently there ceased to be an equitable term as distinguished from a legal tenancy from year to year. It is true that the statutory provisions disabling a landlord from forfeiting for breach of condition until he has given notice and the tenant has failed in compliance therewith to remedy the breach if it is capable of remedy and to make compensation in money apply now to conditions against assignment (sec. 146 of the *Property Law Act* 1928). But an agreement for a lease does not come within the provisions unless "the lessee has become entitled to have his lease granted." His breach of covenant appears to prevent fulfilment of this requirement (*Coatsworth* v. *Johnson* (2)). The legal tenancy from year to

(1) (1929) 43 C.L.R. 105, at pp. 112-117.

(2) (1886) 54 L.T. 520; 55 L.J. Q.B. 220.

year was, of course, within the protection of the section. Subject to non-compliance with a notice, therefore, the landlord might have terminated that tenancy by forfeiture for breach of condition in assigning without consent, but, unless and until he did so, the tenancy from year to year subsisted. The document expressly stated that the tenancy should continue until notice, so that the tenancy from year to year would not *ipso facto* determine at the end of three years under the doctrine explained in *Doe d. Davenish* v. *Moffatt* (1). On the other hand, in the absence in fact of any waiver by the landlord, no exercise of the option could be specifically enforced and, subject to sec. 146 of the *Property Law Act* 1928, the tenancy was liable to termination at any time. But, as the assignment was under seal, it was capable of passing any term of years, including a tenancy from year to year, and, although the interest assigned is described as that existing under the document, there can, I think, be no doubt that it would suffice to carry the term arising from entry in pursuance of the document and payment of rent. An assignment, although in breach of condition, operates to transfer the estate or interest (See, per *Blackburn* J., *Williams* v. *Earle* (2)), although it is true that *Shee* J. seems to have been under the contrary impression (*Elliott* v. *Johnson* (3)). A tenancy from year to year is assignable by deed, and an assignment transfers the interest without the assignee's entry and payment of rent (*White* v. *Hunt* (4)). But it is not settled at what stage the liability to the landlord is incurred by the assignee of a tenancy from year to year or whether that of the lessee continues after his assignee has entered and has been accepted, although up to that time it undoubtedly does (Cp. *Allcock* v. *Moorhouse* (5); *Elliott* v. *Johnson* (6); *Buckworth* v. *Simpson* (7)). Of course the lessee who assigns remains liable upon his agreement for a lease as a contracting party, whatever may be the position of the obligations implied from his entry and payment of the rent.

When, in the present case, the creditors took the assignment they obtained the legal title to the tenancy from year to year.

(1) (1850) 15 Q.B. 257, at p. 265; 117 E.R. 455, at p. 458.
(2) (1868) L.R. 3 Q.B. 739, at p. 750.
(3) (1866) L.R. 2 Q.B. 120, at p. 126.
(4) (1870) L.R. 6 Ex. 32.
(5) (1882) 9 Q.B.D. 366.
(6) (1866) L.R. 2 Q.B. 120.
(7) (1835) 1 C.M. & R. 834, at p. 844; 149 E.R. 1317, at p. 1322.

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Neither notice to the landlord nor his consent was a condition precedent to the passing of the property in that tenancy. The principal debtor who remained in possession as their mortgagor became in law a tenant at will to them. When he agreed to assign his lease to the immediate purchaser to whom he sold the business, he had no interest in the premises which he could transfer except the equity of redemption in the tenancy from year to year. When that purchaser was put into possession, apart from any question of estoppel, he in turn would become at law the tenant at will of the creditors. The landlord, who was ignorant of the assignment by way of security, accepted rent from the purchaser. But it would seem on the facts that the landlord supposed him to be assignee of the residue of the term of three years which the agreement for a lease was intended to create, and in these circumstances an intention to create a new tenancy would not be imputed. In the absence of such an intention, the purchaser would acquire only a derivative title ; he would obtain no interest superior to that which his vendor, the principal debtor, purported to confer. In fact the latter executed no actual assignment, and the parties to the sale were content to act upon the contract between them without completing it by formal documents. This is unimportant if the purchaser understood that a security existed over the lease so that he was buying only an equity of redemption. But it is or may be suggested that he was entitled to suppose that he was acquiring the unencumbered residue of the term of three years and that by their silence at a time when they knew the transaction was on foot the creditors have estopped themselves from setting up their assignment against him or his successors in title. No facts sufficient to support such an estoppel have been proved. It does not appear what the purchaser believed about the lease. He may have been fully aware that the creditors claimed a security over whatever interest the principal debtor had as tenant of the bakery. It does not appear who had custody of the tenant's part of the agreement for a lease, much less that it was produced to the purchaser by the principal debtor as vendor. The transactions by which the two succeeding purchasers acquired possession of the bakery stand, as regards proof, in the same position. No affirmative inference can be drawn that either

of them was led to believe that he was acquiring an unencumbered term or that either of them, up to the actual grant of the renewal of the lease to the second of them, intended to occupy the premises otherwise than as successor in title to the original lessee, the principal debtor. It follows that up to the date of the renewal of the lease, the interest of the creditors must be taken to be that which they took under the assignment and, such as it was, it must be taken to have remained unimpaired ; that is, the creditors remained entitled to a tenancy from year to year liable to forfeiture after notice and failure to comply therewith and pay compensation and also liable to termination by notice to quit ; they remained so entitled subject to an equity of redemption apparently vested in the then last purchaser, who was in possession with no better title at law than as tenant at will under them and in equity as assignee of their mortgagor.

But a different situation arose on the landlord's granting a new lease to the purchaser then in possession, the third in succession from the principal debtor. At that date a year and ten months had passed since the commencement of the original term of three years intended to be created by the agreement for a lease made between the landlord and the principal debtor. By the new lease the landlord meant to supersede that term. If it were not for sec. 146 of the *Property Law Act* 1928, the position might be very simple. For, in granting a new title to the tenant under which he would hold immediately from the landlord, the latter might be taken constructively to have re-entered (*Baylis* v. *Le Gros* (1)), and, if, as the case was, a breach of condition entitled him but for the statute to do so, the old lease would have been determined, notwithstanding, I think, the landlord's ignorance of the breach justifying the re-entry. For, as a general rule, it is enough that upon the true facts a party is entitled to act as he has done and his justification is independent of his own knowledge of the facts (Cp. the cases mentioned in *Shepherd* v. *Felt and Textiles of Australia Ltd.* (2) ; see, however, per *Darling* J., *Parker* v. *Jones* (3)). But the statute does not allow an immediate re-entry,

(1) (1858) 4 C.B.N.S. 537 ; 140 E.R. 1201.

(2) (1931) 45 C.L.R. 359, at pp. 377, 378.

(3) (1910) 2 K.B. 32, at p. 37.

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and the question whether the old tenancy survived depends upon more difficult considerations. If the tenant with whom the landlord was dealing was, as he supposed, entitled to whatever term the earlier tenancy agreement had created, the grant of the new lease would have operated to extinguish it. For the old tenancy would have been determined by the surrender implied in the acceptance of the new. Further, if the creditors as assignees of the old tenancy, that is, the term from year to year, had given their consent to the grant of the new term, a surrender would in that case have ensued. It is well settled that a term of years is surrendered by operation of law when the lessee consents to the lessor's granting a new lease to a stranger who enters into possession (*Nickells* v. *Atherstone* (1); *Davison* v. *Gent* (2); *Wallis* v. *Hands* (3)).

The change of possession is essential to complete the surrender and make it effective. But I think that, where the old tenant is already out of possession and the new already in, the same result is produced by the change in the character of his possession effected by his attorning to the landlord on the grant of the new lease. In the converse case of the old tenant's remaining in possession but on the grant of a new lease to a stranger becoming sub-lessee or sub-tenant of that stranger and in that character attorning to him, the possession does not become referable to a relation of tenure established by the new lease, but it has been held by a Divisional Court that the change in the character of the possession is sufficient to complete a surrender of the old tenancy by operation of law (*Metcalfe* v. *Boyce* (4)).

In all such cases the foundation of the surrender is estoppel *in pais*. The creditors in the present case did not consent to the landlord's granting a new lease, and the consent of the person in whom the old term was vested is an element giving rise to the estoppel. But modern estoppels do not depend on intention alone. They may arise from neglect if it be the cause of an innocent party's acting upon a false assumption, departure from which would operate to his detriment. The landlord, here, acted upon the assumption that

(1) (1847) 10 Q.B. 944; 116 E.R. 358.
(2) (1857) 1 H. & N. 744; 156 E.R. 1400.
(3) (1893) 2 Ch. 75.
(4) (1927) 1 K.B. 758.

he was dealing with a tenant who had succeeded to the term which under the prior agreement for a lease he had meant to create. He thus assumed that he could grant to him a new lease in extinguishment of that subsisting. Was this assumption the consequence of the creditors' failure to speak, in circumstances which made it incumbent upon them to do so? An affirmative answer to this question means, I think, that they were precluded from setting up, as against the landlord, their title to the tenancy from year to year, and, of course, neither the principal debtor as owner of the equity of redemption nor the guarantor in virtue of his right of subrogation would be in any better position. The question itself falls into two parts. Did the occupier of the bakery to whom he granted the new lease present the appearance of having succeeded to the subsisting term, that is, was he ostensible owner of the outstanding lease? If so, were the creditors called upon to disclose the truth to the landlord? I say two parts, because little doubt can exist that if the claim of the creditors to the old lease had been disclosed, the landlord would not have granted the new lease until it had been disposed of. In ordinary circumstances ostensible ownership of an interest in land does not arise from possession and is little aided by it. But, in the present case, the circumstances make the fact that the grantee of the new lease had been put in possession important from the landlord's standpoint. For the successive purchasers of the business were put into possession of the bakery by their predecessors in title who obtained the landlord's consent. The tenancy agreement made that consent necessary for an assignment and the landlord would naturally conclude affirmatively, on the one hand, that each of them had acquired the beneficial right to the tenancy and negatively, on the other hand, that no other disposition of the term had been made. The condition contained in the agreement for a lease was against sub-letting, assigning over, or in any way disposing of, or parting with the possession of, the shop and premises. It may be that a mere equitable charge would not contravene this condition, but it covers every form of alienation which would deprive the landlord of the right to deal with the occupier of the demised premises as the tenant. A landlord would assume that no such alienation had been made without his consent and that he might

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treat a permitted assign in possession as the tenant and accept a surrender from him, at any rate if he were able to produce the tenant's part of the agreement of tenancy. The evidence does not trace the history of that document. But it does not appear to have been kept in the custody of the creditors as mortgagees. Notwithstanding the deficiency of the evidence upon this point, I think on the whole that the landlord was justified in dealing with the purchaser then in possession as beneficially entitled to the tenancy under the agreement for a lease and to all rights arising therefrom. The creditors were, or must be taken to have been, aware of the circumstances to which I have referred. They knew that successive purchasers were put forward to the landlord and entered with his consent. They knew that he was ignorant of their assignment. They knew or must be taken to have known that the tenancy agreement contained a condition against disposing of the tenancy. This knowledge made it incumbent upon them to disclose their interest if they wished to preserve it. Before there is an estoppel from failure to speak, there must be a duty to do so, a duty the sanction of which is preclusion, not liability. I do not wish to repeat what is already stated in *Thompson* v. *Palmer* (1). But in the circumstances in which the creditors stood they did incur such a duty. It follows that, in my opinion, after the date of the new lease the tenancy from year to year could not be set up against the landlord. The position of the tenant under the new lease in relation to the creditors need not, I think, be considered. If he was unaware of the existence of their security, he would hold the new lease absolutely and free from any encumbrance in their favour. If not, it might be bound by an equitable charge in their favour. Such a charge would not be the same but a different security and in relation to the guarantor could be relied upon by the creditors only for the purpose of diminishing the amount of the injury suffered by him, if the question between them became one of equitable discharge *pro tanto*. On that question the burden of proof would be upon the creditors and as they have given no evidence that, when the third successive purchaser took the new lease, he was aware of their security, they have not made good the first step in establishing that they became entitled to a security over it.

(1) (1933) 49 C.L.R. 507, at pp. 545-547.

It thus appears that from that time the principal debt was no longer secured over the tenancy of the bakery and, for what it was worth, that security was no longer available to the guarantor, had he been minded to pay off the debt. From this conclusion it follows that the decisive question is whether the loss of the security in the manner described operates either in discharge or reduction of the surety's liability. Upon this question it is an important consideration that, when the assignment was given, the landlord's consent was not antecedently sought or obtained. Upon the sale of a lease it has always been considered the vendor's and not the purchaser's obligation to obtain the landlord's consent, or to endeavour to do so, when the lease makes that a condition of assigning (*Lloyd* v. *Crispe* (1); *Lehmann* v. *McArthur* (2); *Day* v. *Singleton* (3)). No prior arrangement was proved which would support an inference that the guarantor incurred his obligation of suretyship upon the faith of his brother's giving an assignment of which the landlord had approved, or upon terms that a perfect and indefeasible security over the lease should be obtained. When the solicitors for all parties drew up the instrument of security, they formulated the contract between them. The creditors obtained no better security than an assignment without the landlord's consent and they promised neither impliedly nor expressly to improve it by seeking an *ex post facto* approval by the landlord amounting to a waiver of the forfeiture.

The course taken by the solicitors in preparing an assignment without seeking the landlord's consent may have been due to a misunderstanding of the degree of secrecy desired by the principal debtor and the guarantor. But, however that may be, it was decisive of the nature of the security upon which the creditors made the advances guaranteed and, therefore, of the basis of the guarantee. The omission to obtain the landlord's consent involved no departure from the contract on the part of the creditors. But it is that omission that caused the loss of the equitable term otherwise arising under the agreement for a lease. The breach of condition made the contract unenforceable and so brought about the loss of the term of

(1) (1813) 5 Taunt. 249; 128 E.R. 685.
(2) (1868) 3 Ch. App. 496.
(3) (1899) 2 Ch. 320.

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three years and the further option, leaving only the common law tenancy from year to year. None of the consequences flowing from the fact that the security was not a permitted assignment can afford the guarantor a ground of relief. For they involve no alteration in the contract or its performance and no default in the creditors (See, per Lord *Atkin*, *Pratapsing* v. *Keshavlal* (1)). The creditors are not in this respect in a position analogous to the creditor who in *Wulff* v. *Jay* (2) failed to register his bill of sale, or who in *Capel* v. *Butler* (3) did not register his security over the craft assigned to him, or who in *Strange* v. *Fooks* (4) abstained from giving notice of an equitable assignment. If the guarantee is given upon a condition, whether express or implied from the circumstances, that a specific security shall be obtained, completed, protected, maintained or preserved, any failure in the performance of the condition operates to discharge the surety and the discharge is complete. But otherwise the surety can complain only if the creditor sacrifices or impairs a security, or by his neglect or default allows it to be lost or diminished, and in that case the surety is entitled in equity to be credited with the deficiency in reduction of his liability. The cases are collected in the ninth chapter of Sir *Sidney Rowlatt's* book, and there is an examination of some of them in the judgment of *Hanna* J. in *Northern Banking Co.* v. *Newman & Colton* (5).

The question remains whether the failure of the creditors in the present case after the unpermitted assignment to inform the landlord of its existence amounted to a non-observance of any condition implied in the suretyship, or to a neglect or default. The loss of the tenancy from year to year, such as it was, has already been attributed to the creditors' standing by while the landlord obtained a surrender by operation of law from the third purchaser of the business. But it is one thing to say that because of the consequences to the landlord of their maintaining silence the creditors fell under a duty to disclose to him their interest in the tenancy, and another thing to say that their failure to do so amounted to a neglect of their obligations towards the guarantor. To the latter they were under a duty to

(1) (1934) L.R. 62 Ind. App. 23, at pp. 33-35.
(2) (1872) L.R. 7 Q.B. 756.
(3) (1825) 2 Sim. & St. 457; 57 E.R. 421.
(4) (1863) 4 Giff. 408; 66 E.R. 765.
(5) (1927) I.R. 520, at pp. 536-539.

take reasonable care that the benefit of the security over the tenancy should not be lost. What steps reasonable care demanded depended upon the circumstances, including the nature of the security taken and the conditions attending it. Doubtless the state of the law and perhaps the provisions of the lease were not actually within the cognizance of the creditors and probably they formed no part of the considerations from which their inaction arose. But they constitute some of the conditions which determine the reasonableness of their actual conduct. In point of law the security was exposed to forfeiture at the landlord's instance, unless by complying with the requirements of a notice to remedy the breach of condition, if capable of remedy, and to pay compensation, the forfeiture could be avoided. To inform the landlord of the assignment would have been to raise the question what course he would take and what demands he would make. Whether the breach of a condition against assignment can be remedied by re-assignment is, perhaps, uncertain, but, if the landlord could insist on a restoration of the lease to the principal debtor, the creditors presumably could refuse to comply without immediate repayment of the debt. The solicitors for all parties have adopted the form of security out of which these difficulties arose, and the creditors might assume that on behalf of the guarantor they were content that he as well as they themselves should encounter the risks it involved. Of those risks that material to the present question was the danger of one of the successive purchasers acquiring from the landlord rights superior to the security. The creditors knew that the guarantor himself was responsible for the negotiation and completion of the first sale and participated in the second transaction. If the successive purchasers understood that they were acquiring an encumbered lease, none of them could without bad faith attempt to take a new lease in derogation of the old, and, if he did, the new lease, because of the tenant's notice of the existing security, would become subject to an equitable charge as a substituted security. In all these conditions I do not think that it was an unreasonable course on the part of the creditors to continue the policy of not apprising the landlord of the existence of their security. It must be remembered that notification to the landlord is not a recognized legal precaution for the protection of

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an assignment of a leasehold interest. The only proper course was to obtain his prior consent.

In my opinion the creditors in the circumstances were not guilty of neglect or default in failing after the unpermitted assignment to inform the landlord of its existence.

I therefore think the appeal should be dismissed.

McTIERNAN J. In my opinion the appeal should be dismissed.

The first point relied on by the appellants was that the principal debtor's liability to the creditors ceased upon the assignment of that liability with the creditors' consent to a stranger to the contract of suretyship. The novation of the principal debtor's liability could only have taken place by an agreement, express or implied, to substitute a new debtor for him. The names of the first and the subsequent assignees, who were alleged to have been substituted successively for the principal debtor, are recorded in the creditors' ledger, showing the credits and debits of the account, in a way which might be consistent with the substitution of each of them in turn as the debtor and the discharge of the party liable immediately before each alleged assignment of the liability. There is no evidence that, upon any of the alleged assignments, a novation of the principal debtor's liability had taken place by express agreement. The inference that there was a tacit novation might have been drawn from the evidence of the ledger, if that were the only evidence to be considered. But no such inference is open upon the whole of the evidence. The existence of any agreement to discharge the principal debtor by substituting any new debtor for him is negatived by the oral evidence, and the entries in the ledger are not irreconcilable with this evidence.

The principal debtor had covenanted to pay the debt by instalments, but it was a condition of the agreement, the performance of which had been guaranteed by the surety, that, if the principal debtor should sell the business, for the purchase of which the creditors had advanced the moneys which were the subject of the suretyship, the balance then owing would immediately become due and payable. The second point relied on by the appellants is that the surety was discharged because the creditors relinquished their rights under this condition. The contract of suretyship did not authorize the creditors

to waive these rights. But, even if the creditors had in fact bound themselves not to enforce this condition, the appellants' point cannot be sustained in view of the evidence that the surety assented to the principal debtor receiving the indulgence.

In the agreement by which the moneys were advanced—the debtor, surety and creditors all being parties to the agreement—the debtor assigned to the creditors, as security for the repayment of the moneys, all his right, title and interest under an agreement for a lease of the premises on which he carried on the business. The assignment was made without the landlord's consent and was in breach of a condition of the agreement for a lease which provided that the lessee would not assign without such consent. The instrument under which the surety guaranteed payment of the debt showed that it was secured by the assignment of the debtor's interest as lessee under the agreement for a lease. The third point on which the appellants rely is that the surety is entitled to be discharged from his liability to pay the whole of the moneys which the principal debtor is bound to pay, because the creditors did not preserve this security for the surety's benefit, or, alternatively, that the surety is entitled to an allowance equivalent to the value of the protection of which he was deprived by the loss of the security, the loss being attributable to the wilful default and neglect of the creditors. The principle upon which the appellants base the surety's right to be discharged is contained in the following statement of *Cotton* L.J. in *Carter* v. *White* (1): "The principle is this, that if there is a contract express or implied that the creditor shall acquire or preserve any right against the debtor, and the creditor deprives himself of the right which he has stipulated to acquire, or does anything to release any right which he has, that discharges the surety; but when there is no such contract, and he only has a right to perfect what he has in his hand, which he does not do, that does not release the surety unless he can show that he has received some injury in consequence of the creditor's conduct."

The creditors cannot now enforce the security because a third party is in possession of the premises under a new lease granted by the landlord. In tracing the stages by which this obstacle became interposed between the creditors and the enforcement of the security,

(1) (1883) 25 Ch. D. 666, at p. 670.

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my brother *Dixon* has shown that it is not removable by the creditors. The responsibility of the creditors for the loss of the security is based on their alleged failure to perfect the security by obtaining the landlord's consent to the assignment to them. But neither by the contract of suretyship nor by the general law were the creditors under any obligation express or implied to obtain that consent. Any attempt on their part to remedy the position created by the absence of the landlord's consent might well have been fruitless or even fatal to the interests of all parties. The inactivity of the creditors in not approaching the landlord in order to obtain his approval of the assignment cannot be imputed to them as wilful default and neglect in the observance of their duty to the surety in relation to this security. Indeed, there is evidence that all the parties, including the surety, purposely withheld the assignment from the knowledge of the landlord.

Order that the Ballarat Trustees Executors and Agency Co. Ltd. and Bessie Frayne the executors of the will of George Frayne deceased be joined as respondents to the appeal, any liability arising from such joinder being limited to the assets in the estate of the said George Frayne. Appeal dismissed with costs.

Solicitors for the appellants, *H. E. Elliott, Downing & Oldham.*
Solicitor for the respondents, *J. Allan Anderson.*

H. D. W.