

“EQUITY LOOKS ON AS DONE THAT WHICH OUGHT TO BE DONE

- OR DOES IT?”

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Introduction

“*Equity looks on as done that which ought to be done*”: how marvellous that sounds, combining poetry and morality in equal measure. The maxim underlies one of the most fundamental principles of property law, the creation of equitable interests by specifically enforceable contracts. This talk explores the relationship between the remedy of specific performance and the creation of equitable interests, and asks what the consequences might be of potential developments in the law of specific performance.

The creation of equitable interests by specifically enforceable contracts

Very early in our legal studies we learn that a person who contracts for value to acquire an interest in land or certain other assets, such as shares in an unlisted company, obtains an immediate equitable interest in the property contracted for. This arises because the contract is specifically enforceable, and equity will treat the purchaser as the true owner of the asset from the moment she enters into the contract. By this means a vendor of land becomes a constructive trustee for the purchaser and equitable leases¹ and equitable mortgages and charges² are created³. In the well-known words of Sir George Jessel MR in *Lysaght v Edwards*⁴

“It appears to me that the effect of a contract for sale has been settled for more than two centuries; certainly it was completely settled before the time of Lord Hardwicke, who speaks of the settled doctrine of the Court as to it. What is that doctrine? It is that the moment you have a valid contract for sale the vendor becomes in equity a trustee for the purchaser of the estate sold, and the beneficial ownership passes to the purchaser, the vendor having a right to the purchase-money, a charge or lien on the estate for the security of that purchase-money, and a right to retain possession of the

¹ *Walsh v Lonsdale* (1882) 9 Ch D 9

² *Swiss Bank v Lloyds Bank* [1982] 1 AC 584 at 595; see Fisher & Lightwood’s *Law of Mortgages* 14th edn paras 1.21, 3.2

³ Other equitable rights, such as assignments of future choses in action, may rest on the maxim, but without depending on a specifically enforceable contract: see Snell’s *Equity*, 33rd edn, para. 5-015; *Tailby v Official Receiver* (1888) 13 App Cas 523 at 541-549; Swadling, “The Vendor-Purchaser Constructive Trust” in Degeling & Edelman, *Equity in Commercial Law*. As this paper is concentrating on specific performance, these are not considered here.

⁴ (1876) 2 Ch D 499 at 506

estate until the purchase-money is paid, in the absence of express contract as to the time of delivering possession.”

The problems of fiction

The concept that, at the moment the contract is made, an order for specific performance has been granted and complied with, so that the purchaser has become the owner of the property is, of course, a fiction. This is by no means the only legal principle to rest upon a fiction, but they can be dangerous things if taken too literally. As Sir Thomas Plumer MR said in *Wall v Bright*⁵,

“The principle that the agreement is to be considered as performed, which is a fiction of equity, must not be pursued to all its practical consequences.”

The first fictional aspect is one of timing. Under an unconditional contract for sale, a purchaser cannot in fact obtain an order for specific performance requiring the vendor to transfer the property to her in advance of the contractual time for completion⁶. That may be some time after the contract is made. There may be things that the vendor and purchaser are required to do before the contractual completion date. The vendor will have to make out a good title, or the purchaser will have to waive any defects in it. Under some contracts, for example off-plan agreements for the sale of flats in a block yet to be constructed, there may be a considerable amount to be done by the vendor before the contractual completion date arrives. Yet the equitable interest arises as soon as the contract is made, and is therefore immediately capable of being the subject of a notice on the register⁷. If in fact the vendor has a good title, or in fact the purchaser later waives any defects, the contract will be treated as creating the equitable interest in the purchaser from the outset; if no good title is ever shown, the purchaser will be treated as never having acquired it⁸.

⁵ (1820) 1 Jac & W 494, 503

⁶ *Hasham v Zenab* [1960] AC 316

⁷ Under Land Registration Act 2002, s.32

⁸ *Garnett v Acton* (1860) 28 Beav 333 at 338; Megarry & Wade, *The Law of Real Property*, 8th edn, p.658, footnote 395. In *Lysaght v Edwards*, above, Sir George Jessel MR defines the phrase “valid contract”, used in the passage cited in the text, as one where the vendor’s title has been made out or accepted by the purchaser (507), yet he also says that the vendor is a constructive trustee from the moment the contract has entered into (510). These comments can only be reconciled by the “relation back” principle. Cf *Jerome v Kelly* [2004] 1 WLR 1409 at [32]

So the first thing we know about the equitable interest created in the purchaser is that the answer to the question: *when does the equitable interest arise?* will not be found by looking at what happens if an order for specific performance is made.

The rights and obligations created between vendor and purchaser under a specifically performable contract for sale have been the subject of considerable case law⁹ and much academic commentary. In the interests of time I will not attempt a comprehensive review. There are three distinct proprietary interests: the equitable interest acquired by the purchaser, the vendor's lien on the property for the unpaid price¹⁰ and the purchaser's lien for any part of the price which is paid¹¹. The interaction between these three interests over the life of the contract means that ownership can be seen as passing in stages to the purchaser¹².

Whether the vendor ought properly be described as a "trustee" for the purchaser is a sterile debate: what matters is that fiduciary obligations are imposed on him by virtue of his entry into the contract. It is these fiduciary obligations which give the purchaser her proprietary interest in the property and to which a transferee from the vendor becomes liable, if the contract has been properly protected: the transferee is bound by the equitable interest of the purchaser, not by the contractual obligations which the vendor has entered into.

From the perspective of the vendor, the beneficial ownership of the property has passed sufficiently to the purchaser to convert the vendor's interest from the land itself into money¹³, to pass his interest under a gift in his will of trust property¹⁴ and to require him to preserve the property in the state it was at the date of contract¹⁵. On the other hand, unlike other trustees he can remain in possession of the property and retain the rental income until

⁹ See *Englewood Properties Ltd v Patel* [2005] EWHC 188, [2005] 1 WLR 1961 at [42]-[57] for a review

¹⁰ *Barclays Bank v Estates & Commercial Ltd* [1997] 1 WLR 415 at 419-424

¹¹ *Sookraj v Samaroo* [2004] UKPC 50 at [15]

¹² *Jerome v Kelly*, above, at [32]; PG Turner, "Understanding the Constructive Trust between Vendor and Purchaser" (2012) 128 LQR at 585-588

¹³ *Lysaght v Edwards*, above, at 507

¹⁴ *Lysaght v Edwards*, above

¹⁵ *Englewood Properties Ltd v Patel*, above, at [48]-[57]

the contractual completion date¹⁶ and has no right of indemnity from the purchaser in respect of his outgoings on the property¹⁷.

From the perspective of the purchaser, the beneficial ownership of the property has been transferred sufficiently to pass her the risk of damage or destruction of the property¹⁸ and to entitle her to the sale proceeds if the vendor sells to a third party¹⁹. On the other hand her interest, although assignable and capable of being devised by will²⁰, is insufficient to allow her to create derivative proprietary interests²¹. It is an odd kind of beneficial ownership: not obviously ownership and not always beneficial, either. Nevertheless, in the remainder of this paper I shall use the phrase “beneficial ownership” to describe this package of rights when I need to differentiate this equitable interest from other kinds.

The problem is that none of above can be explained by reference to an order for specific performance. A purchaser under an order for specific performance does not become the owner until she has paid the purchase price: by virtue of the equitable interest she obtains beneficial ownership without paying the price, with the vendor’s interest in the purchase monies protected by his lien instead. That the purchaser might be insolvent and unable to pay the purchase price is irrelevant to the creation of the equitable interest²². Equally, a purchaser under an order for specific performance would not take the risk of damage to the property until she had full rights of ownership in it, including an ability to create derivative interests out of it. The peculiar passing of risk without all that much reward is a feature of the equitable interest which bears no relationship to what would happen under an order for specific performance. It is a direct consequence of the need to reconcile the fiction of the purchaser’s accelerated ownership with the reality of the vendor-purchaser relationship.

¹⁶ *Jerome v Kelly* above at [32]

¹⁷ *Re Watford Corporation and Ware’s Contract* [1943] Ch 82

¹⁸ *Paine v Meller* (1801) 6 Ves 349. In modern contracts, this position is usually reversed by standard conditions of sale.

¹⁹ *Lake v Bayliss* [1974] 1 WLR 1073

²⁰ *IRC v Angus* (1889) 23 QBD 579 at 595

²¹ *Re North East Property Buyers Litigation* [2015] AC 385. This would appear to mean that the purchaser cannot confer a proprietary interest on a sub-purchaser with whom she makes a sub-contract. *Industrial Properties (Barton Hill) Ltd v Associated Electrical Industries Ltd* [1977] QB 580, in which it was held (580, 598) that an agreement for lease entered into by purchasers under a contract for sale created an equitable lease under the doctrine of *Walsh v Lonsdale*, was not cited to the Supreme Court.

²² *Lysaght v Edwards*, above, at 517; *Whittaker v Whittaker* (1792) 4 Bro CC 31

So the second thing we know about the equitable interest created in a purchaser is that the answer to the question: *what rights and obligations arise by virtue of this interest?* will not be found by looking at what happens if an order for specific performance is made.

The maxim that “equity looks on as done that which ought to be done” now looks less and less apt. “*Equity looks on as done that which might be done, at some time in the future and then in a different way*” does not sound nearly so poetic, nor so morally right.

Vendor’s and purchaser’s liens give rise to their own difficulties²³. The vendor’s lien is said to arise from the vendor’s right to claim specific performance of the contract²⁴, but this is not obviously right²⁵. The purchaser’s lien is said not to depend on the contract being specifically enforceable, but on the purchaser having had at some time a present, future or contingent right to the legal estate²⁶. The reasoning by which this position is arrived at is considered below. In any event, whilst the liens provide useful protection for vendor and purchaser against the other’s insolvency, the connection between them and the remedy of specific performance is less than obvious.

Conditional contracts, options and rights of pre-emption

It is in the area of conditional contracts, options and rights of pre-emption that we seem to struggle most with the difficulties thrown up by the equitable principles. I venture to suggest that that is because the courts have failed to heed Sir Thomas Plumer’s warning not to pursue the fiction of specific performance to all its practical consequences. Specific performance of conditional contracts will not be granted²⁷ until all conditions precedent have been satisfied or waived²⁸, it will not be granted of an option agreement until after the option has been exercised and it will not be granted of a pre-emption right until the right to call for a transfer has arisen. All these things are true, but are they relevant? We have already seen that beneficial ownership passes under an ordinary unconditional contract of

²³ Barnsley, “Conveyancing Liens” [1997] Conv 336

²⁴ *Capital Finance v Stokes* [1969] 1 Ch 261 at 278; *London & Cheshire Insurance Co Ltd v Laplagrene* [1971] Ch 499 at 514

²⁵ Megarry & Wade, above, at 15-055, argues that the better view is that the contract does not need to be specifically enforceable at all for the vendor’s lien to arise.

²⁶ *Chattey v Farnedale Holdings Inc* (1996) 75 P & CR 298. Cf *Hewett v Court* (1983) 46 ALR 87 at 104-109

²⁷ Strictly speaking, in appropriate circumstances an order for specific performance may be made, but the order will not require the vendor to transfer the legal estate until these events have taken place: *Hasham v Zenab*, above

²⁸ *Heron Garage Properties Ltd v Moss* [1974] 1 WLR 148; *Hawksley v Outram* [1892] 3 Ch 359

sale before the time at which that contract would be specifically performed. Why should the timing of an order of specific performance be the critical factor for other contracts?

In *Lawes v Bennett* (1785) 1 Cox 167, a tenant was given an option to purchase the freehold for £3,000. The tenant assigned the lease and the option to a successor. Before the option was exercised, the landlord died, leaving his real estate to A and his personal estate to A and B. The option was exercised and the question was whether the £3,000 price was to be treated as part of the landlord's real estate, passing to A, or part of his personal estate, passing to A and B. The court held the latter. Sir Lloyd Kenyon MR said that the principles on which the case depended "are perfectly clear, and are so well established in this court, that if I am wrong it must be by misapplication of those principles". He continued:

"It is very clear that if a man seized of a real estate contract to sell it, and die before the contract is carried into execution, it is personal property of him. Then the only possible difficulty is, that it is left to the election of [the option-holder] whether it shall be real or personal. It seems to me to make no distinction at all...when the party who has the power of making the election has elected, the whole is to be referred back to the original agreement, and the only difference is, that the real estate is converted into personal at a future period."

That looks like a decision that an option operates (at least if subsequently exercised, at which point the exercise is treated as relating back to the grant) to pass the beneficial ownership to the option-holder from the date of grant, and that is how *Lawes v Bennett* was treated in *Lysaght v Edwards*²⁹.

The well-known case of *London & South Western Railway v Gomm*³⁰ concerned an option which had been granted in 1865. In 1879 the land had been sold to the defendant with notice of the option, and in 1880 the option was exercised. The relevant question (for the purpose of the rule against perpetuities) was whether the unexercised option created an interest in land which was in existence at the time of the sale to the defendant in 1879. Sir George Jessel MR said

"The right to call for a conveyance of the land is an equitable interest or equitable estate. In the ordinary case of a contract for purchase there is no doubt about this, and an option for repurchase is not different in its nature. A person exercising the option has to do two things, he has to give notice of his intention to purchase, and to pay the

²⁹ At 520

³⁰ (1882) 20 Ch D 562 at 580-1

purchase-money; but as far as the man who is liable to convey is concerned, his estate or interest is taken away from him without his consent, and the right to take it away being vested in another, the covenant giving the option must give that other an interest in the land.”

In this passage, Sir George seems to be simply assimilating the unexercised option to an ordinary contract of sale. The “right to call for a conveyance of land” in the case of an unconditional contract derives from the specifically enforceable contract, even though the time for completion has not yet arrived. An option is “not different in its nature” from such a contract, despite the need to exercise the option by the option-holder giving “notice of his intention to purchase”.

Twentieth century property cases equally treated an option as giving rise to an immediate interest in land, with no sign at all that this interest might be different in any way from the beneficial ownership that arises under an unconditional contract for sale, or might fundamentally change its nature after exercise of the option³¹.

However, other lines of authority developed, drawing distinctions between options and conditional contracts on the one hand, and unconditional contracts on the other. First, a conditional agreement for lease was held not to create an equitable lease under the doctrine of *Walsh v Lonsdale*³². Second, *Lawes v Bennett* was interpreted as meaning that conversion of the vendor’s interest from land into money only took place upon exercise of an option, or satisfaction/waiver of conditions precedent³³. Third, a series of cases concerned with the meaning of “beneficial ownership” in taxation statutes held that neither an option nor a conditional contract, for example of shares in an unlisted company, passed the beneficial interest to the purchaser until the option was exercised or the conditions fulfilled or waived³⁴.

³¹ See e.g. *Re Mulholland’s Will Trusts* [1949] 1 All ER 460; *McCarthy & Stone v Hodge & Co* [1971] 1 WLR 1547 at 1554F-H; *Armstrong & Holmes Ltd v Holmes* [1993] 1 WLR 1482

³² *IRC v Derby* [1914] 3 KB 1186; *Cornish v Brook Green Laundry Ltd* [1959] 1 QB 394

³³ *Re Marlay, Duke of Rutland v Bury* [1915] 2 Ch 264; *Re Carrington* [1932] 1 Ch 1; *Re Sweeting (decd)* [1988] 1 All ER 1016. This has given rise to the very odd rule that a gift in a will may be adeemed by reason of the exercise of an option, or fulfilment of conditions precedent, after a testator’s death.

³⁴ See e.g. *Wood Preservation v Prior* [1969] 2 All ER 849 (decided on different grounds on appeal [1969] 1 WLR 1077); *J Sainsbury Plc v O’Connor* [1991] 1 WLR 963

In 1998, some of the tax cases came to be cited in a property case, *Chattey v Farndale Holdings Inc*³⁵. The plaintiffs were off-plan purchasers who had paid deposits for flats in a block to be constructed; their contracts were conditional on the grant of planning permission. Planning permission was never obtained, the block was never constructed and the vendor's mortgagee sold off the land, which was now held by the defendant. The plaintiffs claimed liens for their deposits. The defendant argued that a purchaser's lien was dependent on the prior existence of a specifically enforceable contract, which, since these contracts were conditional on planning permission, never granted, the purchasers could not show. It relied on the tax cases for the proposition that a purchaser under a conditional contract does not obtain any equitable interest until the conditions are performed. The Court of Appeal tacitly agreed with the tax cases that a conditional contract does not pass beneficial ownership until the conditions are fulfilled or satisfied. However, it held it nevertheless passes a "lesser interest or right"³⁶. Based on (in my view) a misunderstanding of the passage from *Gomm* set out above, this "lesser" equitable interest was said to arise whenever a purchaser had a right to call for the legal estate, albeit future and unconditional, which the vendor has no right to refuse. A purchaser's lien could be based on this lesser equitable interest and did not depend on a specifically enforceable contract ever having come into existence.

Since *Chattey v Farndale* there seems to be general acceptance that an unexercised option or conditional contract does not pass the beneficial ownership of property at the time it is made, but that the purchaser nevertheless acquires some equitable interest in the contracted-for property³⁷. Quite what the nature of that interest is and to what rights and obligations it gives rise is unexplored, but it clearly can have nothing to do with specific performance, for it comes into existence in precisely those circumstances where beneficial ownership is said not to have passed because specific performance is not available.

Meanwhile, whilst this was all going on in relation to options and conditional contracts, in *Pritchard v Briggs*³⁸ the Court of Appeal decided that, unlike an option, the grant of a right of

³⁵ (1996) 75 P & CR 298

³⁶ At 306

³⁷ See *Michaels v Harley House (Marylebone) Ltd* [2000] Ch 104 at 113, 116; *UBS Global Asset Management v Crown Estate Commissioners* [2011] EWHC 3368; *First Laser v Fujian Enterprises* [2011] HKCA 1; Lewin on Trusts, 19th edn para. 10-005

³⁸ [1980] Ch 338

pre-emption did not create an equitable interest in the grantee. Widely criticised, this decision has been addressed in relation to registered land by s.115 of the Land Registration Act 2002, which declares that

“A right of pre-emption in relation to registered land has effect from the time of creation as an interest capable of binding successors in title (subject to the rules about the effect of dispositions on priority)”.

This is helpful in terms of allowing grantees of pre-emption rights to register notices protecting their rights, but there are fundamental questions which it does not answer. By what kind of interest is the successor in title bound? What are the obligations which he owes the grantee? Does the grantee have the same beneficial ownership which a purchaser under an unconditional contract for sale would have, or the lesser equitable right which is conferred by the grant of an option or conditional contract, or something else entirely? Only one thing is clear: that whatever rights are conferred by s.115, they are created by statute and can have nothing to do with specific performance.

Specific performance as a discretionary remedy

Specific performance is a discretionary remedy, in the sense in which that term is used in equity, i.e. that it will be granted or refused on the basis of well-settled principles. Some of the grounds on which specific performance may be refused will depend on events which have occurred by the time the contract is made, such as mistake or misrepresentation falling short of that which would invalidate the contract or permit its rescission; others, such as delay or great hardship, will occur only later. Various *dicta* suggest that the existence of facts giving rise to a discretionary defence to a claim of specific performance will prevent the beneficial ownership passing to the purchaser, or cause it to be subsequently re-vested in the vendor³⁹. In *Cornwall v Heston*⁴⁰, Cozens-Hardy J said:

“It is often stated that the effect of a contract for sale of land is to make the purchaser from that moment in equity owner of the land. I think, however, that this statement is too wide. The doctrine is subject to one obvious qualification—namely, that the contract is one of which the Court under the circumstances will decree specific performance. For, instance, if the vendor is not in a position to obtain a decree for

³⁹ *Howard v Miller* [1915] AC 318 at 326; *Central Trust and Deposit Co v Snider* [1916] 1 AC 266 at 272; *McLaughlin v Duffell* [2010] Ch 1 at 75-76

⁴⁰ [1899] 2 Ch 710 at 714 (reversed on other grounds [1900] 2 Ch 298)

specific performance, whether by reason of some defect in title or by reason of some collateral misrepresentation, the purchaser never was, in the view of the Court, owner in equity of the property. So, too, if by reason of delay or other circumstances the Court declines to grant to the purchaser specific performance, the purchaser is not treated as being in equity owner of the property.”

There are obvious problems with tying the existence of property interests too closely to discretionary remedies. One is the problem of certainty: the idea that even equitable interests can move in and out of existence depending on particular factual scenarios is not an attractive one. The other is that most defences to a claim of specific performance are inherently one-sided: if the vendor has misled the purchaser, for example, it is for the purchaser to decide whether she wishes to use that as a reason for avoiding the purchase and paying damages instead: the vendor cannot use his own conduct as a ground for refusal to complete. How is the existence of a one-sided defence to play out when the relevant question is not about a remedy as between vendor and purchaser, but what the tax consequences of a contract might be, or its effect on third parties?

There are those who argue that such discretionary defences are irrelevant to the generation of the equitable proprietary interest: that all is required is that there is a valid and binding contract for valuable consideration of a unique subject matter, for which damages are recognised not to be an adequate remedy⁴¹. This has much to commend it as a theory, but it does not reflect the reasoning of the courts: it cannot live with the maxim “equity looks on as done that which ought to be done”, for example. Moreover, if the availability of specific performance really is the key to the equitable interest, it is difficult to see why facts which are relevant to the grant of an order for specific performance should be ignored.

We can see from the cases on options and conditional contracts the willingness of the courts to take the fiction of specific performance literally and it does not seem too much further a step for them to hold, consistently with the *dicta* referred to above, that, because a contract would not, on the facts of the specific case, be enforced by an order for specific performance, the equitable interest should not be recognised.

⁴¹ PG Turner, “Understanding the Constructive Trust between Vendor and Purchaser”, above, at 590-1

Developments in the remedy of specific performance

In this jurisdiction, specific performance is the default remedy for breach of contracts for the sale of an interest in land. Land is treated as unique, and therefore damages for breach of such a contract are assumed to be an inadequate remedy. There are certain well-recognised equitable defences to a claim for specific performance but, in general, specific performance is granted to both vendors and purchasers as a matter of course.

This is not the same in other jurisdictions and there are those who have questioned whether specific performance should remain the presumptive remedy for all contracts for the sale of an interest in land. The vendor, for example, is only interested in the purchase price: why should damages not be an adequate remedy for him? In Canada, not all land is treated as unique, so a purchaser seeking specific performance has to demonstrate by evidence that the land she contracted for really was special enough to justify specific performance rather than damages⁴². If this was applied in England and Wales, there might be doubt about the ability of a commercial investor to obtain specific performance of a contract to purchase land, since it could well be said that if the land is only of interest for its investment value, it is not unique. In both Northern Ireland and the Republic of Ireland, the purchaser's inability to raise the purchase price has been recognised as a defence to a claim for specific performance⁴³.

It follows from what I have said above that I do not think that the relationship between the remedy of specific performance and the creation of equitable property rights is a coherent one. Some equitable rights arise under contracts because of the fiction of specific performance, but at a time and in a way which is different from the way in which an order for specific performance works. Other rights arise under contracts without any apparent link to the remedy of specific performance at all. Some argue that the equitable interests of a purchaser under a specifically enforceable contract should be abandoned as having no

⁴² *Semelhago v Paramadevan* [1996] 2 SCR 415; *Corse v Ravenwood Homes Ltd* (1998) 226 AR 214; *Southcott Estates Inc v Toronto Catholic District School Board* [2012] SCC 51

⁴³ *Titanic Quarter Ltd v Rowe* [2010] NICH 14; *Aranbel Ltd v Darcy* [2010] IEHC 272

rational basis⁴⁴. I do not agree – these rights are fundamental and much of our law, including statutory law, is based on their continued existence.

This lack of coherence does seem to me to make it particularly dangerous for the courts to meddle with the remedy of specific performance without a complete understanding of the ramifications for our property law. The risk of unintended consequences from a response to a particular fact situation is very high. Take the vendor's lien, for example. As matters currently stand, this is said to depend on the vendor's right to specific performance: sweep away the vendor's right to specific performance and you risk sweeping away the vendor's right to remain in possession pending completion. Or take the idea that the purchaser's impecuniosity is a good defence to a vendor's claim for specific performance. Would that mean that the court would need to track the state of the purchaser's finances to work out whether and when she lost the benefit of the fiduciary duties owed by the vendor? And I certainly do not look forward to breaking the news to my investor clients that they do not obtain a registrable interest in land they contract to buy because they are only interested in it for its investment value.

Conclusion

Perhaps it is time to allow the maxim that "equity looks on as done that which ought to be done" to retire gracefully and doze in a corner. It has done its work for many centuries but it is now well past its best. Works of fiction have their place on the bookshelf, but can be unpredictable things in the courtroom.

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⁴⁴ Swadling, "The Vendor-Purchaser Constructive Trust", above. cf. PG Turner, "Understanding the Constructive Trust between Vendor and Purchaser", above.