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## PERFORMANCE OF DEBT ON BEHALF OF DEBTOR

**Key words:** performance of debtor's debt, performance of debt, payment of the debt on behalf of the debtor, enforcement of debt on behalf of another, enforcement of obligation on behalf of another, enforcement of third-party debt, subrogation, legal cession, forced cession, *cesio legis*

### Summary

This paper analyses the general Latvian private law framework and the legal consequences in cases where a third party performs the debt on behalf of the debtor. Historically, the Latvian Civil Law has taken a conservative position on this issue, not recognizing legal subrogation in the event of a debt termination. Although legal subrogation is considered foreign in the Latvian Civil Law (with certain exceptions in the case of recourse by a guarantor), it is recognized in certain Latvian laws. An assessment of Latvian case law reveals a number of judgments, which have addressed this issue, and historically the courts have not recognized legal subrogation. However, recent case law also contains judgments, which may lead to the conclusion that in certain cases there is legal subrogation where a person performs an obligation on behalf of the debtor. Given that there is some uncertainty on this issue, including the legal consequences of a third party performing a debt on the debtor's behalf without the debtor's knowledge and against his will, the paper sets out proposals and solutions to be taken to harmonize the approach in similar cases not only in case law but also in legal doctrine.

### Introduction

Article 1815 of the Civil Law<sup>1</sup> (hereinafter – CL) states:

*If the subject-matter of an obligation pertains only to the personal affairs of the obligor, then the obligor must perform the obligation personally. In all other cases, the obligation may be performed by a third person in place of the debtor, even without his or her knowledge and contrary to his or her intent.*

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<sup>1</sup> Civil Law. Available: <https://likumi.lv/ta/en/en/id/225418-civil-law> [viewed 08.01.2024.].

The purpose of this paper is to analyse the second sentence of Article 1815 CL, which applies to obligations that may also be performed by a third party who is not in a legal relationship with the creditor. Although the second sentence of the said Article allows the performance of an obligation in the place of another and even against the will of the creditor or the debtor<sup>2</sup>, the Article does not regulate whether and what legal relationship exists between the former debtor and the third party in whose place the obligation was performed, after the obligation has been performed. It is clear that the lengthy content of the Article does not imply that the law would provide for legal subrogation in this case. A solution is provided by Article 1797 of the CL, which states:

*A person who in lieu of a debtor satisfies a creditor shall provide by contract that the creditor cedes the claim to him or her, either before the satisfaction or during the time of satisfaction, and if this has been done, then the claim per se shall be considered to have been ceded to him or her at the moment of satisfaction.*

This Article makes it clear that, in order to acquire a claim against a former debtor, a third party must first contract a cession with the debtor's creditor. However, recent case law raises the question whether an assignment is indeed always necessary or whether there are certain cases where, even in the absence of such an agreement, a third party who performed the debt in the debtor's place has a claim against the former debtor for reimbursement of the performance made.

## 1. Concept of subrogation

Subrogation under the "Draft Common Frame of Reference"<sup>3</sup> (DCFR) is a process of transfer of rights in which a person who has made a payment or performance to another person acquires that person's rights against a third party on the basis of law. Subrogation is therefore the transfer of a claim from a creditor to a third party by operation of law in situations where a third party performs an obligation in place of another person. In other words, subrogation is the performance of an obligation in place of another person (the debtor), acquiring a claim against the debtor to the extent of that performance. It may arise by operation of law or by contract, e.g. an insurer, by paying an insurance claim, acquires a claim against the wrongdoer who caused the insured event.<sup>4</sup>

<sup>2</sup> Cakste K. Civiltiesības. Lekcijas. Raksti [Civil law. Lectures. Articles]. Riga: Zvaigzne ABC, 2011, pp. 146, 147.

<sup>3</sup> Principles, Definitions and Model Rules of European Private Law Draft Common Frame of Reference (DCFR), p. 1601. Available: [https://www.cbbe.eu/fileadmin/speciality\\_distribution/public/documents/EUROPEAN\\_PRIVATE\\_LAW/EN\\_EPL\\_20100107\\_Principles\\_definitions\\_and\\_model\\_rules\\_of\\_European\\_private\\_law\\_-\\_Draft\\_Common\\_Frame\\_of\\_Reference\\_\\_DCFR\\_.pdf](https://www.cbbe.eu/fileadmin/speciality_distribution/public/documents/EUROPEAN_PRIVATE_LAW/EN_EPL_20100107_Principles_definitions_and_model_rules_of_European_private_law_-_Draft_Common_Frame_of_Reference__DCFR_.pdf) [viewed 07.01.2024.].

<sup>4</sup> Rozenbergs J. Subrogacija. Juridisko terminu vārdnīca [Subrogation. Dictionary of legal terms]. Riga: Nordik, 1998, pp. 247, 248.

Subrogation is the act of a third party who has paid a debt to a creditor entering in the creditor's place and receiving a claim from the creditor<sup>5</sup>, thus, it is a special type of change of the subject of the active part of the obligation. The following view in the earlier Latvian legal doctrine is misleading and inaccurate –

*If only the right of claim is transferred under the cession agreement (Art. 1800 CL), then in case of subrogation not only the right of claim is transferred, but also the contractual relationship from which this right arises. [...] Complete legalization of subrogation would be highly detrimental to the personal nature of the obligation and would be contrary to the provisions of the CL. Like the transfer and delegation of a debt, subrogation is possible by means of contract of novation to which the debtor is a contracting party<sup>6</sup>.*

In the case of subrogation, there is no contractual relationship, nor does the finding of subrogation require a novation, it is based on a unilateral legal fact, i.e. the giving of performance. This also follows from the only legal definition of the term “subrogation” found in the Latvian legal system, which is contained in Point 23 of Article 1(1) of the Insurance Contract Law – the right of subrogation – the right of the insurer who has disbursed the insurance benefit to take over the right to claim of the insured person against the person responsible for losses in the amount of the disbursed sum. As can be seen from the definition, subrogation does not require a separate novation agreement and is based on the law. Subrogation is most often relevant in monetary obligations, where the identity of the debtor is indifferent to the creditor<sup>7</sup>, but it is also possible in other types of obligations. Although the term “subrogation” is more commonly used, in Latvian legal literature this concept is sometimes also referred to as legal cession, forced cession or cesio legis.

## 2. The institute of subrogation in Civil Law from a historical perspective

The question of whether the Civil Law recognizes legal subrogation when another person performs the debt on behalf of the debtor has also been analysed in the interwar period. As the legal scholar N. Vinzarajs has pointed out,

<sup>5</sup> Sinaiskis V. Civiltiesības [Civil law]. 1938, p. 207. Available: <http://gramatas.lndb.lv/periodika2-viewer/?lang=fr#panel:pp|issue:693919|article:DIVL2045|page:407> [viewed 07.01.2024.]. See also: Civiltiesību pamati. Sakara ar vietejo civillikumumu III. dalu. Pec prof. V. Sinaiska lekcijam [Fundamentals of civil law. Due to Part III of local civil law. After “Prof. V. Sinaiski's lectures”. 1934, pp. 252, 253. Available: <http://gramatas.lndb.lv/periodika2-viewer/?lang=fr#panel:pp|issue:663992|article:DIVL12|page:73> [viewed 18.08.2023.].

<sup>6</sup> Torgans K., Grutups A., Balodis K., Visnakova G., Petrovics S., Kalnins E., Bitans A. Civillikuma komentari. Prof. K. Torgana zinātniskā redakcija [Commentaries on the Civil Law. Under the scientific editorship of Prof. Torgans K.]. Mans Ipasums. Rīga, 1998, p. 282.

<sup>7</sup> Sinaiskis V. Latvijas civiltiesību apskats. Lietu tiesības. Saistību tiesības [Latvian Civil Law Overview. Law of Things. Liability Law]. Rīga: Latvijas Juristu biedrība, 1996, pp. 137, 202.

*from the beginning (see D.46, 3, 76), lawyers required the payer to conclude a contract of sale with the creditor before the act of payment, thus buying the creditor's claim against the debtor. Later (see D.46, 1, 36), the deed of payment was treated (by fiction) as a contract of sale. However, our civil law has not reciprocated the later – progressive – view, since our civil law requires the payer to agree on a cession of the claim before payment [Art. 3466 BCL, analogous to Art. 1797 CL – author's note]. The conclusion of the paper summarizes the insight gained, i.e. that forced assignment and its progressive form, cession ipso iure, are peculiarly constructive techniques, necessary in Justinian's statute (corpus iuris), but not in modern civil law. Erdmann is quite right to say that such a construction is a negation of forced cession.<sup>8</sup>*

With regard to subrogation, the legal scholar V. Sinaiskis<sup>9</sup>, referring to Article 1797 CL, has pointed out that our CL recognizes cession, but subrogation is unknown to it, while mentioning that subrogation exists in other European countries, for example in France – in particular with regard to the law of obligations whose object of performance is money. With regard to the provision in the second sentence of Article 1815 CL that any third party may perform an obligation on behalf of the debtor if the obligation is not connected with the personality of the debtor, the legal scholar points out that this thesis is inconsistent with the principle of autonomy, and that such performance can be explained only as a gift by the third party.<sup>10</sup> In his paper “The Legal Nature of Liability Law”, when discussing subrogation, V. Sinaiskis states:

*But there may be cases when it is desirable to store a monetary obligation, despite the payment of the debt, in such a way as to put a third party who has paid the debt in the place of the creditor. In such a case, there is an exchange of creditors, with the obligation on the active side being reversed in relation to the subject. Cases of transformation of monetary obligations which are provided for by law (legal subrogation) or which arise in connection with a contract (contractual subrogation) constitute the institute of subrogation. Contractual subrogation is generally based on the creditor's will (i.e. an agreement between the creditor and a third party), which is expressed in the contract at the same time as making the payment. Such subrogation is obviously very close to a cession, because here too the debtor's consent is not required. But contractual subrogation on the basis of the debtor's will (on the basis of a contract between the debtor and a third party) is also possible, where not only is the creditor's consent not required, but subrogation is also possible against the creditor's will. [...] As regards to contractual subrogation,*

<sup>8</sup> Vinzarajs N. Jautājuma par piespiestu cesiju [On the question of forced cession]. Jurists, December 1932, No. 9 (43).

<sup>9</sup> Sinaiskis V. 1996, pp. 137, 202.

<sup>10</sup> Ibid., p. 134.

*there is no reason to not recognize it in the law of the present (but the CL sticks to Roman law in this respect).*<sup>11</sup>

As can be seen from an analysis of the interwar legal literature, Latvian general civil law did not recognize legal subrogation in the past.

Subrogation has also been addressed in more recent legal literature. For example, the legal scholar A. Fillers has pointed out to Article 1797 CL (corresponding to Article 3466 BCL), Roman law sources indicate that it dealt specifically with the impossibility of automatic subrogation, which was justified by technical considerations. In particular, the Roman jurist Modestinus argued: if one pays the debt of another, this extinguishes the debt, and if it is not previously ceded (effectively purchased), then the payer has no right of recourse, since it has been extinguished. However, the sources for this Article do not indicate that these purely technical considerations have any effect on third-party claims arising from an authorization contract or an unauthorized management.<sup>12</sup>

Despite the discussion of Latvian legal scholars of the interwar period that the CL does not recognize legal subrogation, but other countries do, the Latvian legislator of the time, when adopting the Civil Law of 1937, did not provide for the institute of subrogation in Article 1815, which means that there is no legal deficiency in this matter, but rather a deliberate will of the legislator.

### **3. The institute of legal subrogation in recent Latvian case law**

When assessing the application and interpretation of Article 1815 CL in Latvian case law, contradictory approaches can be found. For example, the Supreme Court in Case No. SKC-267/2015<sup>13</sup> has indicated that there is a dispute in case, whether the actions of one joint debtor, whereby he pays the purchase price debt instead of all the debtors, in itself creates legal effects of cession [legal subrogation – author’s note]. In this case, the Supreme Court analysed Article 1797 of the CL, stating that this provision applies to the cases where the third party who has satisfied the creditor in the debtor’s place has also agreed for the cession of the right to claim, that is to say, has concluded a cession agreement with the creditor, either before or at the time of satisfaction. The Supreme Court also stated that it agreed with the view expressed in legal doctrine that if such acts [payment of the debt in place of the debtor without first concluding a contract of cession – author’s note]

<sup>11</sup> Sinaiskis V. Saistību tiesību juridiskais raksturs [The legal nature of contract law]. Jurists, 1936, No. 01-02. Available: <http://www.periodika.lv/periodika2-viewer/?lang=fr#panel:pa|issue:209079|article:DIVL31> [viewed 24.08.2023.].

<sup>12</sup> Fillers A. Galvnieka un kilas deveja regresa tiesību regulejums Latvijas civiltiesības [Regulation of the right of recourse of the guarantor and the pledgor in Latvian civil law]. In: 78<sup>th</sup> International Scientific Conference of the University of Latvia. Riga: University of Latvia Press, 2020, pp. 259, 260.

<sup>13</sup> Judgment of the Supreme Court, Department of Civil Cases of 10 December 2015 in Case No. SKC-267/2015, p. 10.2. Available: <https://manas.tiesas.lv/eTiesasMvc/lv/nolemumi> [viewed 08.01.2024.].

in themselves had the legal effect of a cession, then it would be a *de facto* transfer of the debt, which would go against the personal nature of the right of obligation. However, under the CL, a transfer of the debt is possible only by concluding a novation contract, in which the creditor must be present. Such a thesis is, however, unfounded, since the transfer of debts is also possible on the basis of law and the existence of a contract of novation is not always necessary.

On the other hand, in Case No. SKC-27/2022<sup>14</sup>, the Supreme Court formulated its position on the question whether a third party who has paid the purchase price to the seller instead of the buyer for immovable property is entitled to recover it from the latter. The Supreme Court analysed Article 1815 and Article 2014 of the CL in the context of this question. Commenting on Article 3487 of the Compendium of Baltic Local Civil Laws, which is analogous to Article 1815 of the Civil Law, the Court referred to legal scholar Vladimir Bukovsky<sup>15</sup>, who has stated that when a third party fulfils an obligation in place of the debtor, an obligation relationship arises between them, and if the debtor does not prove that the third party paid the debt for the purpose of gifting him (making him richer), then the latter is obliged to reimburse the third party for the costs of fulfilling the obligation. In that case, the Supreme Court held that the use of the creditor's money, rather than the buyer's own, to pay the purchase price created a legal relationship of obligation between the parties and gave the creditor the right to recover from the buyer the purchase price paid on his behalf. The Supreme Court therefore concluded that the second sentence of Article 1815 CL contains a legal subrogation. Although the Supreme Court concluded that legal subrogation follows from Article 1815 CL in this case, the judgment did not at all analyse Article 1797 CL, which imperatively requires a cession, nor did it analyse the conclusions of legal scholars of the inter-war period that there is no legal subrogation in Article 1815 CL.

A similar judgment in which the Supreme Court pointed to the existence of the institute of legal subrogation in Article 1815 CL was later adopted in case No. SKC-263/2022.<sup>16</sup> The Court held that it had no reason to doubt the interpretation of the above-mentioned legal provisions, i.e. that by using not the buyer's own money for the purchase price but the money of his creditor, a legal relationship of obligation is created between the parties and the creditor acquires the right to recover the purchase price paid by the creditor on buyer's behalf from the buyer. Although the court did not refer to judgment No. SKC-27/2022 in its reasoning part of judgement, the reasoning of the judgment was identical.

<sup>14</sup> Judgment of the Supreme Court, Department of Civil Cases of 22 February 2022 in Case No. SKC-27/2022 (C29542517), p. 74. Available: <https://manas.tiesas.lv/eTiesasMvc/lv/nolemumi> [viewed 08.01.2024.].

<sup>15</sup> Bukovsky V. *The Compendium of Civil Laws of the Baltic Provinces with the Continuation of 1912–1914. yr. and with explanations in 2 volumes. Volume II, containing the Law of Requirements.* Riga, G. Gempel & Co, 1914, p. 1449.

<sup>16</sup> Judgment of the Senate of the Republic of Latvia, Department of Civil Cases of 14 December 2022 in Case No. SKC-263/2022 (C73294318). Available: <https://manas.tiesas.lv/eTiesasMvc/lv/nolemumi> [viewed 08.01.2024.].

Similarly, in Case No. SKC-255/2022, the court assessed a situation in which the purchase contract indicated that a third party was the payer of the purchase price, and this third party transferred the entire purchase price to the seller one month before the conclusion of the purchase contract. The third party subsequently brought an action against the buyer named in the contract, seeking a declaration that the payment of the purchase price by the claimant had been made without lawful basis, fraudulently, while also asking for order that the defendant pays the claimant the amount of the purchase price. The Supreme Court held that in the present case it was not important to address the validity of the contract of sale, which was at issue, but whether the defendant was obliged to reimburse the plaintiff for the money used to purchase the immovable property belonging to the defendant. In its reasoning, the Supreme Court referred to the judgment in Case No. SKC-27/2022, reaching the identical conclusion that there is no reason to doubt the interpretation of Articles 3487, 3847 of the Compendium of Baltic Local Civil Laws, that is to say, that the use of the creditors money for the purchase price, rather than the purchaser's own, creates a legal relationship of obligation between the parties and entitles the creditor to recover from the purchaser the purchase price paid in his place.<sup>17</sup>

In assessing these Supreme Court judgments, it must be concluded that, from the point of view of legal theory, the Court's approach is feasible and modern, albeit different from the earlier approach as to whether there is legal subrogation in Article 1815 CL. From a theoretical point of view and abstracting from the outdated approach of the CL and the earlier legal literature, this position of the court is justified, as the majority of European Union countries, including Lithuania, Estonia and the German legal framework on obligations, which is similar to the Latvian legal system, recognizes statutory subrogation.

#### **4. Legal subrogation in the civil codes of Lithuania, Estonia and Germany**

The right of a third party to perform an obligation in place of the debtor is provided for in Article 6.50 of the Lithuanian Civil Code.<sup>18</sup> The first part of this Article provides that the third party may perform the obligation either partially or fully, except in cases where the obligation is related to the personal activity of the debtor. The second part of the Article states that the creditor may not accept the performance offered by the third party if the debtor has notified the creditor of his objections to the third party performing the obligation in his place, except in the case referred to in the first part of Article 6.51 of the Civil Code.

<sup>17</sup> Judgment of the Senate of the Republic of Latvia, Department of Civil Cases of 21 July 2022 in Case No. SKC-255/2022 (C73429419), p. 8. Available: <https://manas.tiesas.lv/eTiesasMvc/lv/nolemumi> [viewed 15.06.2023.].

<sup>18</sup> Civil Code of the Republic of Lithuania. Available: <https://e-seimas.lrs.lt/portal/legalAct/lt/TAD/TAIS.245495> [viewed 19.12.2024.].

The exception described above provides that, where the creditor seeks money recovery proceedings against an object belonging to the debtor, anyone who risks losing the right to the object as a result of the recovery proceedings is entitled to satisfy the creditor's claim. The same right also applies to the possessor of the thing if he risks losing possession as a result of the performance. On the other hand, Article 6.50(3) of the Lithuanian Civil Code provides that a third party who has performed an obligation acquires the rights of a creditor against the debtor, thus recognizing the existence of the institution of legal subrogation in the Lithuanian legal system.

Article 78(1) of the Estonian Act on Obligations<sup>19</sup> states that if the debtor is not obliged to perform the obligation personally by law, the transaction or the nature of the obligation, the obligation may be performed in whole or in part by a third party. If a third party fulfils the obligation, the debtor is discharged from the obligation. The second part of the article states that the creditor is entitled not to accept performance by a third party if the debtor objects. The third part of the Article states that if the debtor has objected to the performance of the obligation by a third party in his place, the creditor may not refuse such fulfilment in two situations. First, where the third party performs the obligation in order to avoid performance in respect of an object which belongs to the debtor but which is in the third party's lawful possession or to which the third party is otherwise entitled and which would lose such possession or rights if enforced. Secondly, where the third party has another legitimate interest in the performance of the obligation and the debtor has failed to perform the obligation when due or it is obvious that the debtor will fail to perform the obligation when due, or where the right from which the obligation arises is mortgaged or arrested and the failure to perform the obligation may jeopardize the enjoyment of the right. Finally, the fourth paragraph of the Article states that the third party who has performed the obligation may bring an action for recovery or claim reimbursement of the costs incurred in performance only if this arises from the law or from the relationship between the debtor and the third party, inter alia, as a result of unjust enrichment or unauthorized management.

Article 267 of the German Civil Code<sup>20</sup> states that if the debtor is not personally bound to perform the obligation, a third party may perform the obligation even without the debtor's consent, adding that the creditor may refuse to accept performance if the debtor objects. Article 268(1) of the Civil Code provides that if a creditor seeks money recovery against an object belonging to the debtor, anyone who risks losing his right to the object as a result of the recovery is entitled to satisfy the creditor's claim. The same right also applies to the possessor of the thing if he risks losing possession as a result of the performance. The third paragraph of that

<sup>19</sup> Law of Obligations Act. Available: <https://www.riigiteataja.ee/en/eli/ee/Riigikogu/act/524032023004/consolide> [viewed 22.12.2023.].

<sup>20</sup> German Civil Code. Available: [https://www.gesetze-im-internet.de/englisch\\_bgb/englisch\\_bgb.html#p0807](https://www.gesetze-im-internet.de/englisch_bgb/englisch_bgb.html#p0807) [viewed 19.07.2023.].



article provides that, to the extent that a third party satisfies the creditor's claim, he acquires a right of claim against the debtor, thus recognizing the existence of the institution of legal subrogation in Germany. In addition, however, it is pointed out that the transfer of the claim cannot be used to the detriment of the creditor.

## 5. Proposals to improve the legal framework

There is no doubt that the various and sometimes contradictory judgments of the Supreme Court in Latvian case law do not strengthen the principle of legal certainty. Therefore, in order to eliminate possible contradictions in the various judgments and to modernize the CL rules on legal subrogation, it is necessary to amend Article 1815 of the CL to provide for the following provisions regarding the right of a third party to perform an obligation in place of the debtor.

In order to avoid conflicting views on the existence of legal subordination in the CL and the legal consequences of a third party fulfilling a debt in place of the debtor, it is necessary to improve the CL by stating:

If a person performs an obligation in place of the debtor, he by law acquires a right of claim against the debtor to the extent of the performed obligation (legal subrogation),

- unless it can be established that such performance was not intended to gift the debtor, or
- unless it can be established that the debtor has objected to the third party's performance of the obligation in his stead (at the same time, this regime should provide for an exception that such objections should not be taken into account if the third party has a legitimate interest in the performance of the obligation).

The introduction of the abovementioned regulation would create and consolidate a clear idea of the legal consequences in Latvia in cases when a third party performs an obligation in place of the debtor, bring the content of the CL in line with modern private law theory, as well as put an end to almost 100 years of discussion in Latvian legal doctrine whether the second sentence of Article 1815 of the CL provides for legal subrogation or not.

## Conclusions

The existence of a legal subrogation regime in Latvian private law does not follow grammatically from the second sentence of Article 1815 CL, and is also denied by the content of Article 1797 CL, which imperatively requires the conclusion of a cession agreement in order for the person who has performed the obligation in place of the debtor to be able to claim for recovery.

Latvian case law contains various and sometimes contradictory judgments on the interpretation of the second sentence of Article 1815 CL and whether

the Latvian CL contains an institution of legal subrogation, which does not contribute to the observance of the principle of legal certainty.

It is necessary to improve the CL rules on legal subrogation by amending Article 1815 of the CL, providing for the institute of legal subrogation, and specifying precise legal consequences in cases where a third party performs an obligation in place of the debtor.

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18. Judgment of the Supreme Court of the Republic of Latvia, Department of Civil Cases of 14 December 2022 in Case No. SKC-263/2022 (C73294318).
19. Judgment of the Supreme Court, Department of Civil Cases, 22 February 2022, Case No. SKC-27/2022 (C29542517).
20. Judgment of the Civil Cases Department of the Republic of Latvia of 21 July 2022 in Case No. SKC-255/2022 (C73429419).