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Litigation and Dispute Resolution

Review

EDITORIAL

Our final edition of 2014 draws together 14 developments in the litigation and regulatory sphere.

We cover Laing J's decision in *Acer Investment Management Ltd & anr v Mansion Group Ltd* in which the court firmly rejected an argument that a simple agency agreement gave rise to an implied duty of good faith. The judgment joins the line of cases post *Yam Seng* where the English court has refused to imply an obligation of good faith (see **Contract**).

Professional third party litigation funding is an increasingly prominent feature of the modern litigation landscape. In *Excalibur Ventures LLC v Texas Keystone Inc & ors* third party funders were found liable for indemnity costs in a high value claim brought before the English Commercial Court. The conduct of the claimants and their legal representatives was heavily criticised by Christopher Clarke J (as he then was) and the court found the funders should be jointly and severally liable for the costs of the claim on an indemnity basis. Whilst this was clearly an exceptional case, the decision does serve as a warning that the conduct of claimants and their legal representatives can have a direct adverse financial impact on funders themselves (see **Costs**).

On the regulatory front, we report on the Treasury's latest consultation in relation to the proposed new senior managers and certification regime and on *Connaught Income Fund, Series 1 v Capita Financial Managers Ltd & anr*, where the High Court confirmed that claims brought under s138D FSMA can be assigned (see **Regulatory**).

Finally, the revised (Recast) Brussels Regulation will come in to force on 10 January 2015 and applies to legal proceedings instituted on or after that date. For commentary on the key changes see "Brussels Regulation (recast): are you ready?" http://www.allenovery.com/publications/en-gb/Pages/BRUSSELS-REGULATION-(RECAST)-ARE-YOU-READY.aspx

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Competition

RETAILERS' CLAIMS AGAINST VISA TIME-BARRED

Arcadia Group Brands Ltd & ors v Visa Inc & ors [2014] EWHC 3561 (Comm), 30 October 2014

The Commercial Court has struck out a substantial damages claim for alleged breaches of competition law on the basis that it was time-barred, granting summary judgment in favour of the defendants. The claimants sought to rely on allegations of deliberate concealment of relevant facts in order to extend the limitation period. Simon J held that the relevant facts for the purposes of the Limitation Act 1980 are only those facts which are sufficient to plead a *prima facie* case. In this case, such facts were in the public domain prior to 2007.

The claimants, who included Arcadia Group Brands, Asda, Morrisons, Argos and other retailers, were alleging that a particular charge, the multilateral interchange fee (**MIF**), levied by Visa when a customer paid by credit or debit card, was inflated and amounted to a restriction of competition in breach of various competition laws. They sought damages in respect of this overcharge going back as far as 1977.

Limitation Periods

The defendants argued that the claims were time-barred, relying on s2 Limitation Act 1980 (**Act**) which provides a defence to tort claims brought after the expiration of six years from the date on which the cause of action accrued, or on s9, which applies to claims for sums recoverable by statute, on materially similar terms. Accordingly, they applied to strike out those parts of the claimants' claims which alleged infringements occurring before certain relevant limitation dates in 2007. In response, the claimants sought to rely on s32(1)(b) Act pursuant to which a limitation period may be postponed where any facts relevant to a claimant's right of action have been deliberately concealed from him by the defendant. In such circumstances the limitation period will only begin once the claimant has discovered the concealment, or could with reasonable diligence have discovered it.

The claimants argued that key facts relevant to the breaches of statutory duty had been concealed, including the manner and mechanisms by which the multilateral interchange fees were set, and indeed the actual levels that were applied.

The claimants' reliance on s32(1)(b) was based on the fact that these key facts were neither discovered nor discoverable with reasonable diligence at the time proceedings were commenced but were highly relevant to the issue of whether the multilateral interchange fees restricted competition.

When deciding whether the claimants could rely on s32(1)(b), Simon J emphasised that s32(1)(b) is a provision whose terms are to be construed narrowly rather than broadly. A distinction must be drawn between facts which found, or are essential to complete, the cause of action, and facts which merely improve or enhance a claimant's prospect of success, but without which the claim can still be properly pleaded. If a claimant is in possession of facts which are sufficient to enable a cause of action to be pleaded, the limitation period will not be suspended. Section 32(1)(b) therefore cannot apply to new facts which might make a claimant's case stronger. Similarly, facts which remain unknown and are not essential to complete the cause of action cannot amount to relevant facts for the purpose of s32(1)(b).

Competition Cases

The claimants contended that as stand-alone competition cases require complex analysis of both legal and economic factors, they should be treated as a distinct and exceptional category of claim. They also argued that such claims fall within an area of law that is still developing and emphasised the repeated warnings

about deciding cases in developing areas of law on a summary basis. Simon J rejected both of these arguments. While acknowledging that competition cases may be particularly complex, he did not consider that they fell within an exceptional category of claims that would require a different approach to the application of s32(1)(b). Also, while he recognised that caution should be exercised where the court is considering issues at the margins of the developed law, the applicable law in these circumstances was clear and well established.

Judgment

In considering the extent of contemporaneous knowledge, Simon J held that, while there was no doubt that the full picture was not available, the claimants had failed to identify any concealed facts which had disabled them from pleading their cause of action. The allegedly concealed facts were deemed to be matters of detail rather than core issues, and further, could have been discovered with reasonable diligence. With reference to contemporaneous events, including investigations by the European Commission and the Office of Fair Trading, he found the defendants to have successfully demonstrated that the particulars of claim derived from material which was available before the relevant limitation dates.

COMMENT

This case is a helpful reminder of the rationale behind s32(1)(b) Act, namely that while there is an important public interest that claimants should not be prejudiced where they lack sufficient information to advance a claim, this must be balanced against the public interest in ensuring certainty and finality in litigation. Claimants need to carefully scrutinise whether the facts known to them, or discoverable by the exercise of reasonable diligence, are sufficient to plead a statement of claim which will establish a *prima facie* case.

The state of the law in respect of competition cases is expected to change with the recent adoption of Directive 2013/0185, Article 10 of which provides that limitation periods will not begin to run until the infringement of competition law has ceased and will only be triggered when the claimant knows or can reasonably be expected to know of the behaviour and the fact that it infringes competition law, the harm he has been caused, and the identity of the infringer. In this case, Simon J emphasised that this was not the present state of the law and so would not affect his reasoning. It therefore remains to be seen whether the Directive will pave the way for a more generous approach to claimants seeking to rely on postponed limitation periods in competition claims.

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DISCLOSURE OF CONFIDENTIAL VERSION OF EUROPEAN COMMISSION DECISION IN FOLLOW-ON CLAIM

Emerald Supplies Ltd v British Airways plc & Air Canada & 17 ors [2014] EWHC 3513 (Ch), 28 October 2014

In relation to a follow-on private damages action arising from an air freight cartel, the High Court recognised that when a European Commission cartel decision is disclosed, the '*Pergan'* principle gives certain protections to non-addressees of the decision against whom no finding has been made but who are nevertheless mentioned in it. However, the court held that it was not obliged to follow the EC procedure, when publishing the non-confidential version of its decision, of redacting any reference to such non-addressees. Instead the court ordered the decision be disclosed without the so-called '*Pergan'* redactions, but imposed a confidentiality ring and barred the claimants from using the unredacted decision to commence further proceedings.

Application for disclosure of European Commission air freight cartel decision

This decision arose in a follow-on action concerning alleged loss resulting from an air freight cartel. In November 2010 the European Commission (**EC**) made a decision (the **Decision**) finding that the addressees of the Decision (which included British Airways (**BA**)) had breached article 101 of the Treaty on the Functioning of the European Union and article 53 of the European Economic Area Agreement by colluding to overcharge for air freight. The claimants, who were customers of air freight services, issued an application to inspect the Decision.

The EC has not yet issued the non-confidential version of its Decision. The EC prepares these non-confidential versions by redacting (i) material prepared as part of any leniency applications, (ii) material over which legal professional privilege was claimed and (iii) materials protected from inspection by the principle identified in *Pergan Hilfsstoffe Fur Industrielle Prozesse GmbH v Commission* [2007] ECR II-4225 (**Pergan**). The "*Pergan* redactions" are intended to protect the presumption of innocence, trade secrets and the confidentiality of non-addressees of the Decision, against whom no finding has been made. This protection is achieved by redacting any references in the EC's decision to such non-addressees. This case was about whether the English courts were obliged to follow the EC's redaction policy to protect *Pergan* rights.

The court first ordered that the defendants and other concerned parties (such as other addressees of the Decision joined as Part 20 defendants and non-addressees of the Decision who were concerned non-parties to these proceedings) prepare a redacted version between them. The result was a heavily redacted Decision which the court held was "completely useless because so much has been redacted". This led to the present application.

Peter Smith J was particularly persuaded of the need to take action as "[d]espite the Decision having been issued merely 4 years ago the Commission has been unable to agree what part or parts of the Decision should be made public". The court found that the EC had taken no steps to speed up the process or to indicate when the process of preparing the Commission's own redacted version of the Decision would be finished. The court concluded that the EC had left it to the court to decide the appropriate measures.

Peter Smith J rejected the claimants' application that he himself should read the unredacted Decision and decide which parts should be redacted. The court did not have the resources, information or background knowledge to undertake such a task.

Confidentiality ring

There was an inequality between the parties, with some having access to the unredacted Decision (by virtue of

being addressees of it) and others not. Peter Smith J stated that disclosure of the Decision into a confidentiality ring, combined with a bar on the claimants using the Decision to commence other proceedings, would allow the dispute to proceed on an equal arms basis while still providing adequate protection of *Pergan* rights.

The court recognised that *Pergan* means that it would be contrary to a non-addressee's entitlement to the presumption of innocence and legitimate interest in protecting professional secrecy for its name to be disclosed in a decision it had not had the opportunity to dispute. However, in all manner of cases, a party's confidential business is regularly protected by a confidentiality ring and *Pergan* did not create a different class of protection. The judge found that there had been a "fundamental failure" of the EC redaction process and that the court was not bound to follow the EC's procedure in applying *Pergan*, so long as the court devised procedures with the same effect. He described the redaction process as a "hopeless exercise".

The court therefore ordered that an un-redacted Decision, minus leniency materials and material for which legal professional privilege was claimed (but not redacted for *Pergan* principle material), be disclosed to all parties, subject to a confidentiality ring and subject to the bar on the claimants mentioned above.

COMMENT

Disclosure into a confidentiality ring is a significant departure from the procedure envisaged by the *Pergan* decision. In a confidentiality ring, the court order establishes arrangements for confidential, unredacted, versions of documents (in this case the Decision) to be provided to representatives of the parties and their external counsel and solicitors. It provides that the parties may disclose confidential documents and information only to the named advisers. The named advisers in the confidentiality ring must give an undertaking not to disclose the confidential versions of the documents to anyone outside the confidentiality ring, and to use the confidential information only for the purposes of the proceedings.

While confidentiality rings have often been used to protect confidential information and trade secrets, the disclosure of the Decision also raises questions of the protection of the entitlement of the non-addressees to the presumption of innocence. The non-addressees could not participate in the EC process and did not have an opportunity to address any references to them in the Decision. It is understandable that non-addressees of an EC Decision would object to potential references to their involvement being disclosed to claimants or potential claimants, or any erosion of the protection of the presumption of innocence. However, the restraint on the claimants using the unredacted Decision to bring further actions should provide some comfort.

There is, of course, a risk that the confidentiality ring will not be respected, especially where there are large numbers of parties, which is often the case in claims of this sort. However, to assume that the order will be flouted is a counsel of despair. The court is entitled to assume that its orders will be complied with. The fact that someone might breach an order cannot be an argument against making it.

This case is currently under appeal; Allen & Overy LLP is acting for one of the appellants.

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Contract

NO DUTY OF GOOD FAITH IN NON-EXCLUSIVE AGENCY AGREEMENT

Acer Investment Management Ltd & anr v Mansion Group Ltd [2014] EWHC 3011 (QB), 17 September 2014

The English High Court has once again been asked to address the question whether a particular contract – in this case, a simple agency agreement – gave rise to an implied duty of good faith. Giving the argument fairly short shrift, Laing J has answered in the negative. The case is – tentatively – a further illustration of the generally narrow and robust approach the English court takes to this issue and emphasises that there is no general duty of good faith in commercial contracts under English law.

The dispute in this case involved claims for unpaid commission and damages arising out of the alleged breach of an implied duty of good faith in an agency agreement.

Acer Investment Management Ltd (**Acer**) and Quantum Investment Management Solutions (**Quantum**) (together, the **claimants**) are distributors of financial products to independent financial advisers (**IFAs**). The two claimants were set up by Matthew Welsh and Paul Hilton, two former members of the UBS Wealth Management team. The defendant, The Mansion Group Ltd (**Mansion**), sets up and sells funds, including the Mansion Student Accommodation Fund (the **MSAF**). For the purpose of marketing the MSAF, the claimants introduced Mansion to an overseas distributor (**GWMS**).

Both parties understood that the claimants expected to be paid for the introduction to GWMS, but there were considerable negotiations over the appropriate level of commission and exchanges of several drafts to that end. At a meeting on 31 October 2011, it was claimed by Acer and Quantum that terms were agreed. Those terms were contained in a draft agreement, circulated by email to Mansion for signature on the same day. It was a matter of dispute whether this gave rise to a binding contract. Laing J held that they did (the **Agreement**).

There was no exclusivity in the Agreement – Acer and Quantum were at liberty to market funds other than the MSAF.

Around the same time, the claimants were introduced to Blackmore, with whom they signed a distribution agreement in November 2011 relating to a fund investing in hotels (**Blackmore fund**). The Blackmore fund competed with the MSAF. Mansion made clear that it did not want the claimants to market the Blackmore fund to IFAs – although Mansion had no contractual right to make that demand under the Agreement. The claimants confirmed to Mansion that they had not been marketing the Blackmore fund – a statement that was later, in court, admitted to be a lie.

The following issues arose for determination by the court in relation to the marketing of the Blackmore fund:

- Was it an implied term of the Agreement that the claimants owed a duty of good faith to Mansion (whether as a fiduciary or as incidental to the Agreement being a "relational" contract)?
- If so, did the claimants breach that term and repudiate the Agreement by lying about the fact that they had been marketing the Blackmore fund?

Was there an implied duty of good faith (and if not, why not)?

In arguing that the claimants owed a duty of good faith, Mansion advanced two alternative arguments: (i) that the claimants owed fiduciary obligations as agents (including the duty of good faith), and (ii) that in any event, the Agreement was a "relational contract" in the style of *Yam Seng Pte Ltd v ITC Ltd* [2013] EWHC 111.

Laing J noted as "instructive" the fact that in *Yam Seng*, the breach of the implied term of good faith arose out of a deliberate lie about a key aspect of the parties' relationship. Nevertheless, the judge dismissed both of Mansion's alternative arguments – that Acer was a fiduciary agent or that it owed a general duty of good faith – because they were "not grounded in the commercial reality of the relationship between the parties, or in the express terms [of the Agreement]".

Laing J accepted as "humbug" the suggestion that the parties were in a "relational contract" of the type envisaged in *Yam Seng*. The judge agreed that the claimants were "just selling" – "salesmen selling the funds", without the "to-ing and fro-ing of information exchange". Laing J was also guided towards this decision by the following facts:

- the relationship was not regarded by the parties as exclusive;
- there were no obligations or commitments one would expect in a "relational contract";
- the relationship was not longterm;
- either party could terminate on reasonably short notice (the period was unspecified in the judgment); and
- neither party was required to spend significant sums in reliance on the continuation of the relationship.

Laing J further concluded that even if she was wrong and Acer was a fiduciary, then the express terms of the Agreement would have excluded the implication of any associated fiduciary obligation of good faith.

Was the duty of good faith breached?

Laing J nonetheless proceeded to consider the question of repudiatory breach (in the event of being wrong about there being no implied duty of good faith on either ground) – in other words, did Matthew Welsh's dishonesty "go to the root of the contract", or did it "deprive the innocent party of substantially the whole benefit of the contract"?

Laing J found that it did not. In deciding that the lie was about a subject that was "not even peripheral to the contract" (because Acer was under no obligation of exclusivity), Laing J also considered the following two factors as relevant to her conclusion:

- the parties' Agreement was not "a moral code which required the Claimants to tell the truth to Mansion at all times"; and
- the lie was corrected (albeit not wholeheartedly) and Mansion in any event knew that Acer was marketing the Blackmore fund (so Mansion did not rely on the lie).

Laing J adopted as the relevant test for determining whether a good faith obligation had been breached the minimum requirement of "honesty", at the same time noting that what good faith requires is in each case sensitive to context.

COMMENT

The decision in *Acer v Mansion* provides some useful guidance in a number of areas on the question of "good faith" in English contract law.

First, while the case is evidence that parties increasingly rely on *Yam Seng* for the argument that a duty of good faith should be implied (in particular, where there has been some dishonesty between the parties), it also underscores the scrutiny to which the English court will generally subject that argument.

In *Acer v Mansion*, Laing J gave the argument fairly short shrift and was in no way critical of the claimants' assertion of "humbug" in relation to the contention that the Agreement was "relational" within the meaning of *Yam Seng*.

To the author's knowledge, there is only one other case to date – *Bristol Groundschool Ltd v Intelligent Data Capture Ltd & ors* [2014] EWHC 2145 (Ch) (on which we have commented previously, see *Litigation Review, September 2014*) – in which the English court has implied a duty of good faith into a commercial contract on the basis that it was "relational" in nature.[1]

Elsewhere and consistent with the notion that any implied duty of good faith is to be construed narrowly, the English court has been restrictive and robust in its approach (as it was in *Acer*) – for example, refusing to imply an obligation of good faith into a nascent joint venture relationship in *Hamsard 3147 Ltd v Boots UK Ltd* [2013] EWHC 3251 (Pat). Similarly, in *TSG Building Service PLC v South Anglia Housing Ltd*

[2013] EWHC 1151 (TCC), Akenhead J referred (perhaps euphemistically) to the judgment in *Yam Seng* as ”extremely illuminating and interesting” but concluded that it gave rise to no “principle … of general application to all commercial contracts”. He also confirmed that any implied duty cannot go beyond or circumscribe the parties’ express agreement.

Second, the case provides some useful – albeit fairly briefly stated – guidance on the factors that will be relevant to the consideration of whether a particular contract is “relational”. In an agency or similar relationship, “exclusivity” may well be determinative. The duration of the relationship and the ease with which parties can extract themselves from that relationship will also be relevant.

Third, the decision again underscores that “honesty’ is the core requirement of an obligation of good faith (as in *Yam Seng* and *Bristol Groundschool*) – but is again restrictive in its application of that principle.

Honesty was cited in *Yam Seng* as one of a number of “core expectation[s]” or “core value(s)” at the heart of the duty of good faith. This core requirement was briefly acknowledged by Laing J. However, the judge went on to make clear that in ordinary commercial dealings, parties are not generally required to be honest, in particular if: (a) the subject matter of the dishonesty is of “peripheral’ importance to the parties’ relationship (ie it does not go to the root of the contract), and (b) the other party did not rely on the dishonest statement to its detriment.

Finally, and in light of all these observations, *Acer v Mansion* is a further useful illustration of the importance of specifying with precision the parties’ expectations of each other in any long-term relationship (which may be viewed as “relational”). As the English court has now repeatedly made clear (consistent with the principles in the Privy Council’s decision in *Attorney General of Belize v Belize Telecom* [2009] UKPC 10), a duty of good faith will not be implied where it would contradict, circumscribe or go beyond the parties’ express agreement.

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[1] A duty of good faith was also implied in the case of *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd* [2014] EWHC 2104 (Comm). However, the term in that case was implied into an obligation to “first seek to resolve the dispute or claim by friendly discussion” before resorting to arbitration – an obligation that was held to be binding and to carry with it an implied obligation to do so in good faith. See Litigation Review Aug/Sept 2014 for an article on this decision.

Costs

PROFESSIONAL THIRD PARTY LITIGATION FUNDERS HELD LIABLE FOR INDEMNITY COSTS

Excalibur Ventures LLC v Texas Keystones Inc & ors [2014] EWHC 3436 (Comm), 23 October 2014

The professional third party funders of a losing claimant were subject to a costs order on an indemnity basis as a result of, *inter alia*, the poor conduct of the claimant and its instructing solicitors during the course of proceedings. The professional funders were held liable for the defendants' costs to the extent of the funding provided by each individual funder. No distinction was made regarding the mechanism through which the funding was provided.

The most recent development in the Excalibur litigation saga relates to a substantial costs order made against the third-party funders. The underlying litigation involved a claim made by Excalibur Ventures LLC (**Excalibur**) against Texas Keystone Inc and others (the **defendants**), in which Excalibur alleged that it was entitled to an interest in a number of profitable oil fields in Kurdistan and sought an order for specific performance of an agreement under which it could exercise this interest or damages in the sum of USD 1.6 billion.

At first instance, Christopher Clarke J (as he then was) dismissed all of Excalibur's claims and ordered that it pay the defendants' costs on an indemnity basis. An indemnity costs order was made to reflect Excalibur's poor conduct (and that of its instructing solicitors) during the course of the proceedings. Excalibur's legal costs had been funded by a number of independent third-party litigation funders (the **Funders**), who between them had provided funding for Excalibur's legal costs and GBP 17.5 million in security for costs as ordered by the court at first instance.

The defendants sought an order that the Funders be held jointly and severally liable for the costs of the claim, assessed on an indemnity basis. Some of the Funders accepted liability for the costs but contested the claim that they should be liable for costs on an indemnity basis while others disputed liability or did not participate in the costs proceedings.

Should the Funders be ordered to pay any of the defendants' costs on an indemnity basis?

Christopher Clarke J held that the purpose of ordering indemnity costs was not to penalise the Funders. Indemnity costs were appropriate because this was an exceptional case due to the size of the damages sought, the fact that Excalibur's case lacked any real legal merit and the poor conduct of Excalibur and its legal representatives. In these circumstances ordering indemnity costs achieved justice for the defendants. Furthermore, the Funders had freedom of choice over whether or not to extend funding to Excalibur, but the defendants had no choice as to whether or not they were to be sued. Therefore, unless there were exceptional circumstances in favour of the Funders which dictated otherwise, their fate was tied to that of those they were funding. There were no exceptional circumstances applicable here in favour of the Funders, so the judge found that they had to pay costs on an indemnity basis, subject to the *Arkin* cap (which is discussed in more detail below).

Should a cap be applied to the defendants' costs?

The judge upheld the principle laid down in *Arkin v Borchard Lines Ltd (nos 2 and 3)* [2005] 1 WLR 3055, that a professional funder who financed part of an unsuccessful claim should only be potentially liable for the opposing party's costs to the extent of the funding provided. The judge noted that the Funders had not sought to exercise control over the litigation, nor had they

acted improperly. Therefore he found that there was no reason to depart from the principle laid down in *Arkin*.

Should the costs order differentiate between the various Funders who contributed to Excalibur's costs at different stages of the proceedings?

One of the peculiarities of this case was that some Funders had only provided funding for security for costs orders made during the course of the proceedings, whereas other Funders had provided funding to cover both security for costs orders and legal costs generally. The question before the Court was whether the *Arkin* cap should be measured by reference to the amount contributed to Excalibur's ordinary legal costs or to that amount plus the amount contributed to satisfy security for costs orders. The judge held there was no distinction to be drawn between the two, and the mechanism by which the funding was provided was irrelevant and that to have found otherwise would have been to protect the funder who contributed to a security for costs order to the detriment of a funder who contributed to normal legal costs.

How should costs be apportioned between the various Funders?

The judge held that the timing of a Funder's contribution to the case was a relevant factor when considering the amount of costs that that Funder was liable for. Funders should not be liable for costs that were incurred prior to the date on which they contributed to the funding of the case. The rationale was that it would be unjust for a Funder to be liable for costs which that Funder played no part in causing the defendants to incur. The judge did not think that the fact that these Funders inherited the earlier work product was a sufficient reason to make them liable for costs incurred prior to the date on which their funding contribution was made.

COMMENT

This case has an important impact on the development of professional litigation funding, and such funders should be aware that the actions of the claimants they are funding and their respective legal representatives may make the funders liable for indemnity costs. Having said that, it is worth bearing in mind that the Excalibur case was an exceptional case, in terms of the size of the damages being sought, the lack of legal reasoning underpinning Excalibur's claims and the consistently poor conduct of Excalibur and its legal representatives, which had a significant impact on the decision reached (most notably the decision to award indemnity costs). The judge was clearly alive to the need to balance justice to the defendants in this particular case against the need to ensure that the case did not give rise to legal principles which would discourage professional funders from providing funding as this could lead to problems with access to justice more generally. Indeed, the judge noted that, due to the exceptional nature of the Excalibur case, he did not believe that the principles introduced in this case would affect the majority of professionally funded cases.

The decision is also important as it upholds previous authorities such as the *Arkin* cap and the principle that a professional funder will not be liable for costs incurred prior to its contribution, which provides welcome certainty to this area.

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COURT OF APPEAL REINFORCES TRIAL JUDGE'S "WIDEST DISCRETION" WHEN AWARDING COSTS UNDER CPR 44

Coward v Phaestos Ltd & ors [2014] EWCA Civ 1256, 2 October 2014

The defendants were awarded their costs, having obtained significantly more in their counterclaim than that provided for by the claimant's rejected *Calderbank* Offer. The Court of Appeal dismissed the claimant's appeal that the judge erred, holding that trial judges are afforded wide discretion in ordering costs under CPR 44 which is in no way constrained by the costs rules under CPR 36. The issue arose in the context of an intellectual property dispute concerning highly valuable quantitative trading software.

In 2010, the claimant, Dr Martin Coward, commenced proceedings against the defendants (referred to collectively as IKOS), seeking declarations that he was the owner of copyright and database rights in the software and databases used by IKOS in their quantitative trading business. Dr Coward, a mathematician and computer programmer, had recently acrimoniously split from his wife and business partner Ms Elena Ambrosiado. Together, they started and ran an extremely successful quantitative trading business whose success was founded on highly valuable computer software protected by copyright, database and confidential information.

Following Dr Coward's resignation from IKOS, he founded a competing business. A year later, Dr Coward commenced proceedings in the English High Court seeking declarations that he was the owner of copyright and database rights in the software and databases used by IKOS. IKOS counterclaimed for declarations that those rights were not owned by Dr. Coward. They also counterclaimed that Dr Coward had retained IKOS's valuable confidential information and trade secrets and was infringing its copyright in using the software code.

In March 2013, Asplin J dismissed Dr Coward's claims. The judge held that the software written by Dr Coward was owned by the partnership, not Dr. Coward. Asplin J also held that Dr Coward had infringed copyright in certain software. Other software which had been in dispute had been settled before trial.

Arguments on costs at trial

Prior to the trial, in July 2012 Dr Coward made a without prejudice save as to costs offer (the **Calderbank Offer**) to settle the case. IKOS rejected the offer. At the costs hearing following trial, Dr Coward argued that the *Calderbank* Offer provided substantially all that was subsequently achieved by IKOS at trial. Dr Coward argued that the introduction of CPR r36.14(1) had not overridden the Court of Appeal decision in *Carver v BAA Plc* [2009] 1 WLR 113. CPR r36.14 states that costs should be awarded where a claimant fails to obtain a judgment "more advantageous than a defendant's Part 36 Offer". Dr Coward argued that despite this provision, Lord Justice Ward's dicta in *Carver* remained relevant in that "one must consider in an open-textured way whether the fruit of the litigation was worth the fight." Dr Coward argued that the case had not been worth the fight, especially in circumstances where IKOS had incurred approximately GBP 13 million in costs in comparison to Dr Coward's of GBP 6 million. IKOS argued that Carver had been superseded by r36.14(1) and, in any event, the outcome of the trial had significantly beaten the *Calderbank* Offer.

The judge held that *Carver* was not relevant because it addressed cost consequences under Part 36. Asplin J's discretion on costs fell under the ambit of CPR 44.2, which affords judges a wider discretion as to costs orders. She held that IKOS had materially beaten the *Calderbank* Offer in four respects. The judge therefore did not award Dr Coward costs. Dr Coward appealed.

Decision

The Court of Appeal dismissed Dr Coward's appeal, holding that the trial judge's exercise of her discretion could not be faulted. In reaching its decision, Richard LJ, giving judgment of the court, held that:

- Decisions on costs are a matter of discretion for the trial judge who is best placed, having sat through the trial, to determine whether and what costs should be granted.
- The approach of the appellate court in relation to costs is clear: the appellate court may only interfere with the trial judge's decision on costs if it is wrong in principle, has taken into account a matter which should not have been considered or is plainly unsustainable (*F&C Alternative Investments (Holdings) Ltd v Barthelemy* [2013] 1 WLR 584).
- The judge was right to conclude that IKOS had achieved a significant advance at trial on the terms of the *Calderbank* Offer. Two main reasons were cited by the court to support this view. First, at a post-trial hearing, when it had become clear the court was going to order an injunction to stop Dr Coward from using software code that he had downloaded from IKOS in November 2009, he reluctantly agreed to an undertaking in similar terms. Second, shortly before the trial Dr Coward agreed to delete code that had been written by his employees during their gardening leave periods while they had been employed by IKOS. These factors pointed to IKOS having obtained a result at trial that was a significant advance over the *Calderbank* Offer.
- The decisions in *Fulham Leisure Holdings Ltd v Nicolson Graham & Jones* [2006] EWHC 2428 and *Walker Construction (UK) Ltd v Quayside Homes Ltd* [2014] EWCA Civ 93 were not relevant to this case. In those cases, the courts considered that even though a claimant was strictly successful, their success was so insignificant in comparison to the costs of the action that this should be a factor for the court when ordering costs. Unlike those parties, IKOS had succeeded in the entirety "of its defence of the claim and to a very substantial extent in its counterclaim". Further, those offers had provided the parties with everything that they subsequently recovered (save for a trivial sum in *Fulham Leisure*). IKOS had obtained a significant improvement on the *Calderbank* terms at trial. Finally, although IKOS obtained a majority of the terms of the *Calderbank* Offer at trial, "it is not disproportionate for a claimant to pursue a claim for substantial relief to which it is held at trial to be entitled".
- Even if Dr Coward had been successful, the rules on Part 36 are not relevant in the consideration of costs under a *Calderbank* Offer. Part 36 and Part 44 are separate regimes with different purposes. Part 36 is a highly prescriptive and self-contained code dealing only with offers made under those rules. Any discretion by the judge as to those costs is highly restricted. Part 44 confers on the court "discretion in almost the widest possible terms" as to whether costs are payable by one party or another. It would be contrary to import the rigidity of CPR r36.14 into Part 44. The Court of Appeal accepted that the discretion conferred by Part 44 can come at the price of certainty on arguments as to costs, but that is the nature of costs being a discretionary remedy dependent on circumstances.

COMMENT

The English court will be reluctant to interfere with a trial judge's discretion in ordering costs save for the specified circumstances set out in *F&C Alternative Investments (Holdings) Ltd v Barthelemy* [2013] 1 WLR 584, nor will it adopt a Part 36 style analysis when determining costs awards under CPR 44. For Calderbank Offers to be strategically effective in putting costs pressure on the other side, litigants must ensure that the terms of their offers limit the ability for a party to obtain significantly better results at trial. Otherwise, on the question of costs, the fruit of the *Calderbank* Offer may be proven to be worth the fight.

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Enforcement

NO FREEZING ORDER AGAINST SUBSIDIARY OF ARBITRATION AWARD JUDGMENT DEBTOR

Cruz City 1 Mauritius Holdings v Unitech Ltd & 7 ors [2014] EWHC 3704 (Comm), 11 November 2014

In an important decision for anyone trying to enforce an arbitration award, Males J ruled that the English court did not have jurisdiction to make a freezing order against subsidiaries of the judgment debtor, to further aid enforcement of the award, in circumstances where the subsidiaries had not been party to the arbitration agreement or the arbitration proceedings, and there was no substantive claim against the judgment debtor (just a claim for ancillary relief). Males J noted the need for caution in the exercise of the *Chabra* jurisdiction, which applies with even greater force when the third party is a foreigner with no presence or assets within the jurisdiction.

In last month's Review, we covered a decision of Males J, who exercised his jurisdiction to appoint receivers by way of equitable execution over a judgment debtor's shareholdings in four subsidiary companies for the purposes of enforcement of a London arbitral award (*Cruz City Mauritius Holdings v Unitech Ltd & ors* [2014] EWHC 3131 (Comm)). In these related proceedings, Males J was asked to determine whether the English court has jurisdiction to make a freezing order against those subsidiaries to further aid enforcement of the award in circumstances where no substantive claim is asserted against the subsidiaries and none has any presence or assets within the jurisdiction.

In July 2012, the claimant, Cruz City Mauritius Holdings (**Cruz City**), obtained an LCIA arbitration award, now worth more than GBP 350 million (the **Award**), against the defendant, Unitech Ltd (**Unitech**). Since then, the parties have been embroiled in litigation across a number of jurisdictions as Cruz City attempts to enforce the award and Unitech (in the words of Males J) does whatever it can to avoid having to meet its liabilities. In these proceedings, Cruz City sought to obtain a freezing order against five of Unitech's subsidiaries (the **Subsidiaries**) in aid of enforcement of the Award. The complications for Cruz City were twofold: (1) the freezing order was sought against third parties; and (2) none of those third parties has officers, assets, or conducts any business, in England and Wales. The judgment focuses on the latter complication, with Males J not required on this occasion to consider the merits of the former. He nonetheless provided a useful summary of what is known as the *Chabra* jurisdiction.

The *Chabra* jurisdiction: freezing injunctions against third parties

Where a claimant can show a good arguable case that assets apparently owned by a third party are in fact beneficially owned by the defendant against whom there is a cause of action, it can obtain a freezing injunction against that third party (*TSB Private Bank International SA v Chabra* [1992] 1 WLR 231). That jurisdiction has been extended over time such that a freezing order may be granted to preserve assets that are or may be available to the judgment creditor, if necessary by the appointment of a liquidator or receiver, by exercising the rights of the judgment debtor to compel the third party to disgorge property or otherwise contribute to the funds or property of the judgment debtor.

Males J emphasised that this is "an unusual jurisdiction" in that it involves the exercise of the court's compulsive powers against a party against whom no cause of action is asserted. Its effect in cases such as this – where the exercise of the jurisdiction is based not on beneficial ownership but on the possibility of the judgment creditor

being able to exercise rights of the judgment debtor – is to restrain the third parties from dealing with assets over which they have both legal and beneficial ownership. For that reason, Males J noted the need for caution in the exercise of the jurisdiction, which applies with even greater force when the third party is a foreigner with no presence or assets within the jurisdiction.

The jurisdictional gateways

Because the Subsidiaries were all incorporated outside England and Wales, conducted no business here, and had no assets, directors, officers or other presence within the jurisdiction, Cruz City could only obtain the freezing order if it first satisfied the requirements of one of the "jurisdictional gateways" for service of a claim form out of the jurisdiction.

Ultimately, and having conducted a lengthy review of the relevant authorities, Males J accepted the Subsidiaries' argument that Cruz City's claim for *Chabra* relief did not fall within either gateway that it relied upon. In doing so, he had reference to one of the "cardinal principles" of construction: any doubt as to the correct construction of the jurisdictional gateways ought to be resolved in favour of the foreign defendant.

The gateways relied upon by Cruz City, and Males J's reasoning in relation to them, were:

(1) **CPR 62.5(1)(c)**: a court may give permission to serve an arbitration claim form out of the jurisdiction if the claimant seeks a "remedy…affecting an arbitration…, an arbitration agreement or an arbitration award".

It was clear on the authorities, Males J held, that service out of the jurisdiction pursuant to this gateway is permissible only against a party to the arbitration agreement or arbitration proceedings in question. The Subsidiaries were party to neither the arbitration agreement nor the arbitral proceedings, thus the gateway did not apply.

(2) **CPR PD 6B, para 3.1(3)**: a court may give permission for service out of the jurisdiction on C where there is a claim made by A against B and: (a) there is between A and B a "real issue which it is reasonable for the court to try"; and (b) C is a "necessary or proper party to that claim".

To satisfy this gateway, Cruz City first had to establish that there was a "claim" made against Unitech as the "anchor defendant". However, recent case law established that this requirement is satisfied only where there is a "substantive dispute" between the claimant and the anchor defendant before the English court. Cruz City's claim for a freezing order sought only ancillary relief. Accordingly, there was no "claim" against the anchor defendant before the English court and the prerequisite to reliance upon this gateway did not apply.

In support of that view, Males J made reference to the specific terms used in the Rule (a "claim", a "real issue" and a trial ("reasonable for the court to try")), all of which he took to suggest that a substantive claim is required. In his view, relief that is ancillary to the enforcement of a judgment or award does not fit naturally into that language. His Honour also relied upon the "long-standing approach to construction of the rules for service out of the jurisdiction", which requires that the rules are generally to be construed as relating to claims which involve the determination and enforcement of legal rights, and not to applications for interim relief that involve no process of adjudication upon substantive rights: *Mercedez Benz AG v Leiduck* [1996] AC 284.

Even if a "substantive claim" was not required, Cruz City was unlikely to have satisfied the requirements of this gateway because Males J did not consider there to be a "real issue" between the parties that it was "reasonable for the court to try". The freezing order sought would, he observed, add nothing of substance to the relief already obtained by Cruz City (namely, a worldwide disclosure order, worldwide freezing order, and receivership order). It was not sufficient to establish jurisdiction that there was a mere possibility that a need for the additional freezing order may arise in the future.

COMMENT

For parties attempting to enforce arbitral awards, this decision is significant. It appears to render highly unlikely that an award creditor could obtain a freezing order against a non-party outside the jurisdiction, where

that order is sought in aid of enforcement of an arbitral award. Males J was alive to the fact that such a result is contrary to the English court's much touted policy that it should do what it properly can to assist in the enforcement of arbitral awards, but held that the policy cannot justify construing the jurisdictional gateways in a manner that extends their scope beyond their proper bounds.

The decision therefore gives some protection to an award debtor's subsidiaries that were neither a party to the arbitration agreement nor a participant in the arbitral proceedings, and suggests that an award creditor may be more successful in enforcement by use of a strategy that focuses on the pursuit of measures against the debtor itself, which could also extend to its subsidiaries (for example, the appointment of receivers).

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Immunity

INTERNATIONAL ORGANISATIONS: IMMUNITY FROM SUIT AND LEGAL PROCESS

Assuranceforeningen Gard Gjensidig v International Oil Pollution Compensation Fund [2014] EWHC 3369 (Comm), 17 October 2014

An international organisation is not a State, and is only afforded immunity to the extent granted by statute. It is relatively uncommon for international organisations to come before the English courts, though economically and politically they can be very influential. This case is a rare example of how the courts will interpret immunity legislation in the context of international organisations.

The claimant (**Gard**) is a P&I club and the insurer of a vessel. The International Oil Pollution Compensation Fund (the **Fund**) is an international legal organisation created under the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage 1971. It is part of an international compensation scheme for oil pollution damage. Under the scheme, a claimant will first seek compensation from the shipowner or insurer, who is obliged to pay claims up to a certain limit of liability. The claimant is then entitled to turn to the Fund for any outstanding amounts of compensation in excess of that limit.

The Fund was given the status of a corporation under English law by the International Organisations Act 1968[1] (the **1968 Act**) and in particular the accompanying International Oil Pollution Compensation Fund (Immunities and Privileges) Order 1979 (the **1979 Order**). The 1968 Act is the mechanism under English law by which a number of international organisations are granted the status of a corporation, each requiring a specific statutory instrument. The 1979 Order grants the Fund immunity from suit and legal process, with the exception of certain specified circumstances, including in relation to "any loan or [any] other transaction for the provision of finance" (Article 6(1)(c)).

[1] The United Nations and the International Court of Justice have also been granted this status under the same Act.

In 1997, a ship registered with Gard grounded in the Maracaibo Channel, Venezuela, resulting in a large oil spill. The Venezuelan courts subsequently held that the shipowner and Gard were liable to pay approximately USD 60 million to the Republic of Venezuela for damage suffered. This was significantly in excess of the shipowner and insurer's limits under the international compensation scheme.

Gard brought claims against the Fund in England and in Venezuela to recover the money, alleging that Gard and the Fund had entered into a contract for funding in 1997, pursuant to which Gard had agreed to pay claims up to a limit and the Fund had agreed to pay claims in excess of that – which included the claim of the Republic of Venezuela. In May 2014, the English court was asked to grant a freezing order against the Fund in support of Gard's claim in the Commercial Court; Hamblen J did so, finding that Gard had a "good arguable case" that a contract for a loan or for the provision of finance (falling within an exception to immunity in the 1979 Order) did in fact exist. This part of the proceedings, relating to the freezing order, has been appealed.

Application

The Fund sought a declaration that the English court had no jurisdiction to hear the claims bought by Gard on the basis that it was immune from jurisdiction under Article 6 of the 1979 Order and the alleged agreement did not constitute "a contract for the provision of goods and services, [a] loan or [a] transaction for the provision of finance" and as such did not fall within the express exceptions from immunity under the 1979 Order. The challenge raised two key questions: (i) was there a contract between the parties at all?; and (ii) if so, did it fall within one of the exceptions to immunity under the 1979 Order?

Was there a contract?

Hamblen J emphatically rejected the existence of any contract. Notwithstanding this, he went on to examine *obiter* whether, if there had been a contract, it would have fallen within the exception to immunity from suit and legal process granted by Article 6(1)(c) of the 1979 Order. It is this aspect of his decision which is of most interest.

Did the alleged contract fall within one of the exceptions to the Fund's immunity under the 1979 Order?

The Fund argued that there was a strong presumption in favour of its immunity from suit, citing an analogy with the State Immunity Act 1978, the reasons why Parliament had conferred immunity on the Fund, the distinction between "public" and "commercial" acts, and the fact that the Fund's activities in this particular case had the character of so-called *acta jure imperii* ("imperial" or public acts of a State which qualify for State immunity) rather than so-called *acta jure gestionis* (commercial acts of a State which do not qualify for State immunity).

Gard countered that the Fund's case was misconceived and based on a false elision between an international organisation and a sovereign State.

Hamblen J agreed with Gard that there is an important distinction between an international organisation such as the Fund and a sovereign State: "The Fund was not a state. States have long had a right to immunity […] Organisations such as the Fund have no such historic right and only have immunity if and to the extent that it is granted by statute". As such, the doctrine of *acta jure imperii* did not apply to the Fund, given that it is by definition not a State. Hamblen J quoted the distinction made by Bingham J (as he then was) in *Standard Chartered Bank v International Tin Council:* "international organisations […] have never so far as I know been recognised at common law as entitled to sovereign status. They are accordingly entitled to no sovereign or diplomatic immunity in this country save where such immunity is granted by legislative instrument, and then only to the extent of such grant, […] no more and no less".

Hamblen J held that the 1979 Order must be construed according to its terms in the context of its legislative purpose and scheme. Further, while there should be no presumption in favour of or against the Fund's immunity, the 1979 Order and the exceptions to immunity should be construed purposively.

Applying the guidance in the authorities on what constitutes a loan or a transaction for the provision of finance to the facts of the case, Hamblen J held that the

alleged contract between the parties was neither a loan nor a transaction for the provision of finance. As such, even if there was a contract, it was not one that would fall within the exception to immunity from suit and legal process under Article 6 of the 1979 Order.

Therefore, the Fund would be immune from Gard's suit and the English court had no jurisdiction over the claim.

COMMENT

This case offers useful, albeit *obiter*, guidance on the approach a court is likely to take when determining whether an international organisation is afforded immunity, as a matter of English law, from suit and legal process. Hamblen J confirmed that the strict approach to the extent of an organisation's immunity taken in the *International Tin Council* case in 1986 remains good law.

It follows that when contracting with an international organisation, it is important to verify as a matter of English law whether there is relevant enabling legislation that has been enacted as this will ultimately determine:

- the legal capacity of the organisation to enter into commercial contracts and submit to the jurisdiction of national courts or an arbitral tribunal;
- the legal personality of the organisation to sue and be sued before national courts or an arbitral tribunal; and
- the privileges and immunities of the organisation and appropriate waiver of those immunities.

For further guidance please see Allen & Overy LLP publication "Why contracting with an international organisation is different", available on www.allenovery.com.

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Privilege

"WITHOUT PREJUDICE" COMMUNICATIONS AND RETROSPECTIVE DISPUTES

Avonwick Holdings Ltd v Webinvest Ltd & anr [2014] EWHC 3322 (Ch), 10 October 2014; *Avonwick Holdings Ltd v Webinvest Ltd & anr* [2014] EWCA Civ 1436, 17 October 2014

Correspondence regarding a proposed debt restructuring between the parties headed as "Without Prejudice and Subject to Contract" was admitted into evidence. The "Without Prejudice" privilege did not apply to the communications despite the notation, as there had been no existing dispute between the parties as to the borrower's liability to pay, or quantum of the debt, at the time of the restructuring proposals. The case is a reminder that the use of the "without prejudice" notation, absent any underlying dispute raised between the parties, is itself insufficient to attach any privilege to the communications. In such circumstances, an express contractual agreement may extend the "Without Prejudice" privilege to those communications.

In 2010, Avonwick Holdings Ltd (**Avonwick**) lent USD 100 million to Webinvest Ltd (**Webinvest**) under a loan agreement, secured by a personal guarantee given by a Mr Shlosberg (the guiding mind behind Webinvest). The sum had not been repaid, and Avonwick claimed money allegedly due and owing under those agreements. In resisting the claim, Mr Shlosberg had alleged that the loan agreement was subject to a collateral oral arrangement that Avonwick would only be entitled to be paid when Webinvest itself was repaid by the sub-borrower, a third party to whom the USD 100 million was on-lent, which was owned or controlled by a business associate of Mr Shlosberg.

In April 2014, the parties (immediately following the issuance of demands under the terms of the loan agreement and guarantee) exchanged correspondence about a proposed restructuring of Webinvest's debt. In general, that correspondence, in particular involving draft heads of terms proposed by Avonwick, was marked "Without Prejudice and Subject to Contract". Avonwick sought to have the correspondence admitted into evidence at trial.

First Instance decision: no privilege

For a document to be inadmissible on the basis of the "without prejudice" privilege, it must form part of a genuine attempt to resolve a dispute – that is, there must be both a genuine dispute to be resolved, and a genuine attempt to resolve that dispute.

Richards J at first instance noted that where there was no dispute about a liability, but only negotiations as to how and when an admitted, existing, liability should be discharged, then those negotiations (and therefore any associated communications) were not covered by the privilege.

Richards J held that, at the time of the communications, there was no dispute about either Webinvest or Mr Shlosberg's liability *per se*. This was because the allegation of a collateral agreement that affected liability was first raised in a witness statement of Mr Shlosberg on 30 May 2014 (some two months after the relevant correspondence) in support of Webinvest's application to restrain Avonwick from presenting a winding-up petition and to set aside a statutory demand.

Richards J discussed *Bradford & Bingley plc v Rashid* [2006] 1 WLR 2066, which involved a similar factual scenario with the parties communicating about a restructuring proposal (without any dispute as to liability or quantum of the debt). The key distinguishing fact was that in *Bradford*, the communications had not been marked as "without prejudice". Ultimately, the House of

Lords had held that the "without prejudice" privilege did not apply to those communications, on the basis that it would be a "very substantial enlargement" of the scope of the privilege if it applied to discussions as to how an admitted liability was to be paid.

However, Lord Brown and Lord Mance had given two different interpretations as to the implications of applying the phrase "without prejudice" to a communication. Richards J followed Lord Mance's view, commenting that "[m]arking a document as "without prejudice" is a strong indication that there is a genuine dispute and a genuine attempt to settle the dispute, but it is not conclusive". The fact that the relevant communications between Avonwick and Webinvest were marked as "without prejudice" was therefore not determinative, as there was no underlying dispute as to the liability or the quantum of the debt subject to the restructuring proposal and negotiations. The communications could not retrospectively be made subject to the "without prejudice" privilege where a dispute as to the liability or quantum was subsequently raised, but had not existed at the time of the communications.

Court of Appeal upholds decision

The Court of Appeal upheld the decision. Lewison LJ gave the principal judgment, with Sharp LJ and Burnett LJ agreeing. Lewison LJ held that there were two bases for the operation of the "without prejudice" privilege. The first was the public policy interest in encouraging people to settle their difference, which required there to be a dispute to enliven the prejudice. His Honour noted that the concept of a "dispute" had a very wide scope, such that even the "opening shot" communications in negotiation may still be subject to the "without prejudice" privilege as in, for example, where a person "puts forward a claim and in the same breath offers to take something less in settlement" (applying *Standrin v Yenton Minster Homes Ltd* (1991) The Times, 22 July 1991, CA).

In order to determine whether the "without prejudice" privilege applied, the Court was therefore required to determine (on an objective basis) whether there was a dispute or issue to be resolved. On this point, the Court of Appeal upheld Richard J's finding that there was no dispute at the time of the relevant correspondence.

Lewison LJ also recognised that there was a possible contractual basis for the "without prejudice" privilege, such that parties could extent the usual ambit of the "without prejudice" rule through contract. However, on the facts, Lewison LJ found that there was no contract to the effect that the relevant communications would not be used in civil proceedings in court. Rather, the use of the phrase "without prejudice" was interpreted in accordance with common usage, since the maker of the communication did not intend to give up any pre-existing rights. In addition, it was noted that the relevant communications (and not solely the draft restructuring agreement), were titled "subject to contract" as well as being titled "without prejudice", leading to the conclusion that the communications themselves did not amount to any kind of contract.

COMMENT

It is common practice in restructuring negotiations with defaulting borrowers to head communications with the standard protection of "Without Prejudice and Subject to Contract". However, it is always necessary to consider whether the ostensible protection of the "without prejudice" privilege in fact operates in the circumstances of a particular communication. A dispute between the parties may not yet exist (as the restructuring negotiations may at least initially be on friendly terms): nevertheless, either party may wish to actively enliven the privilege. To do so, it will be necessary to either directly raise an actual dispute with the other party, which is to be resolved by the communications, or expressly agree that the privilege will apply to the communications (even absent a dispute). The use of the header "Without Prejudice" itself did not amount to such a contractual agreement in this case, in part because (presumably through oversight) the standard "subject to contract" reservation was also included on the communications as well as the draft restructuring agreement.

It will be interesting to see if a different approach would be adopted to construing communications expressed to be "without prejudice" but not themselves "subject to contract", and whether this itself in a series of communications could provide the necessary contractual force.

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Real Estate

VALUER NOT NEGLIGENT WHERE REPORT RELIED ON FOR PURPOSE OUTSIDE SCOPE OF INSTRUCTION

Freemont (Denbigh) Ltd v Knight Frank LLP [2014] EWHC 3347 (Ch), 14 October 2014

Where a valuer had been instructed by the claimant landowner to prepare a valuation report for the purpose of securing lending to facilitate the development of the land, there was no express or implied term that the claimant could rely on in the report when forming its plans for the future of the redevelopment land.

The defendant valuer, Knight Frank LLP, had been instructed in August 2006 to value development land for secured lending purposes. Knight Frank's report, which had been provided to the claimant landowner, Freemont (Denbigh) Ltd, valued the land at GBP 17 million with outline planning permission and GBP 18.7 million with detailed planning consent. Freemont Denbigh claimed that the report had also been commissioned to enable it to assess whether or not to sell the land and, in the months and years that followed, it had relied on the valuation report for the purposes of deciding whether to sell. However, on the basis that none of the offers received had matched Knight Frank's valuation, Freemont Denbigh had declined all offers for the land. In the event, no detailed planning was obtained and no development took place at the site. The listed buildings on the land had fallen into such bad disrepair and the likely costs of reinstatement were so high that Freemont Denbigh considered the whole site to be worthless. In 2012, just before expiry of the limitation period, Freemont Denbigh brought proceedings against Knight Frank claiming that, had the valuation not been negligent and too high, it may have accepted one of the offers. Freemont Denbigh sought damages for its lost profits, as well as other substantial costs and expenses. The court was asked to rule on five preliminary issues.

Report only for lending purposes

The preliminary issues were determined in Knight Frank's favour by Stephen Smith QC sitting as Deputy Judge in the High Court, who held as follows:

– A contract of retainer came into existence between Freemont Denbigh and Knight Frank in relation to the valuation.

– The critical term of the contract was that Knight Frank would provide a valuation report for financing or secured lending purposes. There was no basis for the submission that the contract contained an express or implied term to the effect the report was to be provided for Freemont Denbigh to rely on in the future when forming its plans for the redevelopment of the land.

- Knight Frank owed Freemont Denbigh a duty of care in tort (in addition to a contractual duty of care) to exercise reasonable care and skill in the valuation and preparation of the report, but that duty of care extended only to the provision of a report for secured lending purposes. It would be remarkable if the duty of care owed by Knight Frank in tort were more extensive than its contractual duty of care. There was no warrant for an extension of the duty in this case.
- Freemont Denbigh was not precluded from relying on the report for the purposes for which it was provided ie to enable it to try to obtain the financial support it required. However, if it relied on the report in the months or years ahead for other purposes for which the report was not provided, it was not entitled to bring a claim against Knight Frank in respect of any loss it suffered in consequence of that reliance.
- The heads of loss claimed were not capable of falling within the scope of duties owed by Knight Frank to Freemont Denbigh. The further questions of remoteness or foreseeability therefore did not arise.

Summary of the common law duty of care owed by a valuer

There is a useful summary of the common law duty of care in the judgment.

- A duty of care in tort was likely to be owed to the person for whom the report was prepared (even though a contractual duty of care may also be owed to the same party).
- The duty of care was likely to be limited to the purposes for which the report was prepared.
- A duty of care in tort may also be owed by a valuer valuing premises for mortgage purposes (at least if they are modestly valued residential premises) to the purchaser of those premises if: (i) the valuer knew that his report was likely to be shown to the purchaser, and (ii) the purchaser intends to use the premises for his own residential purposes, not to let them, and (iii) the valuer knows that his report is likely to be relied upon by the purchaser for the purpose of deciding whether to purchase the premises.
- However, a duty of care in tort is unlikely to be owed by a valuer instructed to produce a report for a lender for security purposes, to an investor who relied on the report for other purposes.

Stephen Smith QC stated that the first three propositions were settled law (*Smith v Eric Bush* [1990] 1 AC 831; *Caparo Industries Plc v Dickman* [1990] 2 AC 605). However, the last proposition could not have been viewed as being settled before the decision in *Scullion v Bank of Scotland plc* [2011] 1 WLR 3212. In *Scullion*, a valuation (both capital and rental) was carried out for the benefit of an intended lender in respect of a buy-to-let flat. At first instance, the purchaser, who failed to achieve the projected rental value and consequently sold up, was awarded damages against the valuer for the deficiency in rent. The Court of Appeal reversed the decision, holding that the valuer had not owed a duty of care to the purchaser.

COMMENT

The decision in this case builds on the distinction made in *Scullion* between the scope of the duty of care owed to those who buy property as a commercial investment and those who buy to occupy a modest property as their residence. In *Scullion*, it was held that a purchaser could not rely on a valuation provided for lending purposes when deciding whether to invest in a buy-to-let property. This was expanded on in *Freemont* so that a report provided for security purposes cannot be relied on in a situation where a commercial investor is deciding how to deal with its property. The rationale behind this is that a valuer would expect an investor in commercial property to obtain its own advice and, if the valuation were commissioned for investment purposes, it is likely that the report would need to be more extensive to cover any additional factors which are relevant.

If investors in commercial property wish to protect their position on valuation, they will be well-advised to obtain their own valuation report. Having said this, there may still be some scope for a duty of care to be owed where a valuer can be shown to have known that an investor would rely on his valuation for purposes in addition to obtaining secured lending. No doubt the decision is welcomed by valuers and their insurers alike.

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Regulatory

ASSIGNMENT OF FSMA CLAIMS BY PRIVATE PERSONS

Connaught Income Fund, Series 1 v Capita Financial Managers Ltd & anr [2014] EWHC 3619 (Comm), 5 November 2014

The High Court has allowed the assignment of claims by private persons under s138D Financial Services and Markets Act 2000 (**FSMA**). The decision highlights the possibility of claims being assigned to, for example, a hedge fund or litigation funders who might use this as a mechanism to collect a number of claims and seek to bring proceedings against a financial institution for breach of its statutory obligations.

The claimant, The Connaught Income Fund, Series 1 (the **Fund**), was an unregulated collective investment scheme established as a limited partnership. The defendants, Capita Financial Managers Limited (**Capita**) and Blue Gate Capital Limited (**Blue Gate**), were the Fund's operators from its launch in April 2008 and from September 2009 respectively, until the Fund was wound up by order of the High Court on 3 March 2012 and joint liquidators appointed.

In the underlying claim, the Fund sought compensation on the basis that Capita and Blue Gate unlawfully promoted the Fund to the investors, some of whom became partners in it (in breach of s238 and s214 of FSMA) and that they were responsible for misleading promotional literature. The Fund brought the claim in its capacity as legal assignee of over 1,000 retail investors' claims under s138D FSMA (formerly s150 FSMA).

Capita asserted that the proceedings were a nullity because, *inter alia*, the assignments to the Fund were invalid. Capita contended that the assignments were a device to circumvent the limitations set by the Financial Services and Markets Act 2000 (Rights of Action) Regulations 2001 (the **RAR**) on claims under FSMA being maintained for the benefit of persons other than "private persons". In response to these challenges the Fund made an application for summary judgment against both Capita and Blue Gate, to which this judgment of Judge Mackie QC relates.

Assignment of a section 138D FSMA claim to persons who are not "private persons"

Under s138D FSMA, a contravention by an authorised person of a rule made by the FCA or PRA is actionable "at the suit of a private person" (as defined by RAR reg 3 and RAR reg 6(1)) who suffers loss as a result of the contravention, subject to certain exceptions.

A contravention by an authorised person is also actionable by a person (X) who is not a "private person"

if the following three conditions are satisfied (RAR reg 6(3)(c)):

(a) that person X is acting "in a fiduciary or representative capacity" on behalf of another person (Y);

(b) any remedy would be "exclusively for the benefit" of person Y; and

(c) any remedy "could not be effected through an action brought otherwise than at the suit" of person X.

The defendants argued that the RAR reg 6(3)(c) conditions were not satisfied because: (i) the recoveries would be pooled as an asset in the winding up rather than being "exclusively for the benefit" of each assigning investor; and (ii) the investors could bring the claims themselves without assigning the right to the Fund. Further, the defendants submitted that the assignments were a device designed to circumvent the criteria set out in the RAR and must be impermissible on the grounds of public policy. They also contended that the words "at the suit of" in s138D FSMA indicated that the suit must be brought by the private person and that the exception in the RAR presupposes this rule.

The claimant separated the issues raised by the defendants into two separate questions: firstly, who enjoys a cause of action under s138D FSMA; and secondly, whether that cause of action is assignable. The claimant argued that s138D FSMA was concerned solely with the former issue, and the section contains no express prohibition on assignment, in contrast to explicit language used in, for example, s187(1) of the Social Security Administration Act 1992.

Citing *Norglen Ltd. v. Reeds Rains Prudential Ltd* [1999] 2 AC 1 (HL) in support, the claimant argued that the fact that s138D FSMA conferred rights on a limited class of persons did not impose either an implied statutory bar on assigning to persons outside that class, or imply that proceedings premised on such assignments were somehow an abuse of the court. The defendant distinguished *Norglen* on the basis that the fulcrum issue of that case was whether an assignment from a legal person to a natural person was invalid because it was done to overcome the restriction on a legal person obtaining legal aid; the cause of action was one which could, however, be brought by both legal and natural persons. By contrast, a claim under s138D FSMA could only be brought by a "private person".

The claimant also argued that RAR reg 6(3)(c) has nothing to do with assignment and relates not to transmissibility but to a situation in which relevant investments are held through a professional trustee and where the beneficiary cannot get redress by suing in his or her own name. The claimant pointed to the FSMA Part XV Financial Services Compensation Scheme (the **FSCS**) and submitted that the defendants' reading of RAR reg 6(3)(c) would undercut the FSCS's established practice of taking general assignments of the claims enjoyed by the investors and depositors whom it compensates, which will include s138D FSMA claims.

Decision

Judge Mackie QC held that the words "at the suit of" did not remove a claimant's right to assign his or her claim; where Parliament intends to exclude such a right, it can say so clearly. He held that there was nothing offensive about permitting the assignment of these rights, commenting that it may be desirable to assign so as to make it easier and cheaper for private persons to assert their rights. He agreed with the defendants that the *Norglen* case should be distinguished. The judge also held that RAR reg 6 did not apply since an assignee is not, unless there are additional circumstances, a fiduciary or someone acting in a representative capacity.

Further arguments raised by the defendants

The law of partnership

The defendants asserted further reasons why the proceedings should be considered a nullity, including that, following the dissolution of the Fund, the members were only able to bind the firm so far as was necessary to wind up the affairs of the partnership and the partnership had no authority to take assignments from investors after its dissolution.

Capita attempted to argue that s38 of the Partnership Act 1890 (the **1890 Act**) acted to restrict the powers of the liquidator to those which are "necessary to wind up the affairs of the partnership, and to complete transactions

begun but unfinished at the time of the dissolution but not otherwise…". It also submitted that an insolvent partnership which has been ordered to be wound up on the grounds of insolvency no longer satisfies the definition of a partnership in s1(1) of the 1890 Act because the partners are no longer carrying on business with a view of profit, and thus s38 of the 1890 Act is a special provision required to expressly continue the partners' authority.

Judge Mackie QC quickly dismissed this point on the basis that the action was not being brought by former partners under s38 of the 1890 Act, but by the liquidators on behalf of the Fund, as pointed out by the claimant.

Paragraph 5A of CPR Practice Direction 7A

Capita argued that Paragraph 5A of CPR Practice Direction 7A (**Paragraph 5A**) means that the Fund could not pursue the causes of action because they accrued to investors in their personal capacities, not as partners in the Fund.

Paragraph 5A provides that:

"**5A.1** Paragraphs 5A and 5B apply to claims that are brought by or against two or more persons who

(1) were partners; and

(2) carried on that partnership business within the jurisdiction, at the time when the cause of action accrued.

5A.2 For the purposes of this paragraph, 'partners' includes persons claiming to be entitled as partners and persons alleged to be partners.

5A.3 Where that partnership has a name, unless it is inappropriate to do so, claims must be brought in or against the name under which that partnership carried on business at the time the cause of action accrued."

Capita submitted that the 'partnership criteria' had to have been met before Paragraph 5A could be used, and that they were not met in this case. The cause of action accrued to an investor who invested in the limited partnership at the point of doing so and thus became a limited partner, but it did not accrue to the investor as, or in the capacity of, partner. The claimant argued that there is no good reason to read Paragraph 5A restrictively, and Judge Mackie QC agreed with this, reading it in accordance with the overriding objective of the CPR, to deal with cases justly and at proportionate cost. He held that Capita's approach would add expense, uncertainty and risk to litigation for no advantage.

Capita further argued that Paragraph 5A derogates from the principle that proceedings must have a claimant who is a legal person, since it permits a partnership to bring proceedings using its trading name. Judge Mackie QC disagreed on the basis that the Fund did not lack personality since it was an insolvent partnership acting through its liquidator which could sue in the name of the Firm or in the names of the partners.

Liquidators' powers

Blue Gate argued that the liquidator had no power to accept the purported assignments of the investors' claims since a liquidator is given no express power by the Insolvency Act 1986 (the **1986 Act**) to accept assignments. The Fund contended that schedule 4, paragraph 4 of the 1986 Act gives the liquidator the power to bring or defend any action or other legal proceeding in the name and on behalf of the company, with sanction, and that this section does not distinguish between claims vested in the company before or after the date of winding-up. Further, the Fund argued that the liquidator has the power under paragraphs 7 and 13 of schedule 4 of the 1986 Act to acquire property, after winding-up, for the benefit of the estate.

The judge held that paragraph 13 is a "'sweep up'" provision, but nevertheless a self-standing and extremely wide one. It empowers the liquidator to do all other things "necessary" for winding up and distributing property. He viewed as an "unassailable justification" the argument proposed by the claimant, that if it chose to bring the claims "there was the prospect of making a substantial recovery, for the benefit of all creditors, and not just the assigning investors".

COMMENT

The confirmation by the court of the ability to assign claims brought under s138D FSMA raises important considerations for financial institutions. It suggests that private persons who would otherwise have been

prohibited by difficulty and cost are allowed to assign their claims and therefore gain redress indirectly. Assignment was not expressly limited to liquidators so a "private person" could, in theory at least, assign his or her claim to anyone willing to bring litigation against the relevant authorised person in question.

This decision therefore highlights the possibility of retail customers who do not wish to incur the considerable time and expense of litigation, selling their investment and the claims arising from that investment to third parties. Those third parties, whether hedge funds or litigation funders for example, might use this as a mechanism to collect a number of claims and seek to bring proceedings against a financial institution for breach of their statutory obligations.

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SENIOR MANAGERS REGIME: WIDENING THE SCOPE

The Treasury has issued the latest consultation in relation to the proposed new senior managers and certification regime which, when finalised, will replace the approved persons regime for banks, building societies and Prudential Regulation Authority (**PRA**) designated investment firms operating in the UK. The principal issue addressed in the consultation is widening the scope of the new regime to capture UK branches of overseas firms.

The consultation is another step along the road to reforming the existing approved persons regime in order to make it easier for the Financial Conduct Authority (**FCA**) and the PRA to hold to account individuals working in banks, building societies and investment firms.

A wider reach

The consultation briefly sets out the Treasury's proposed approach to extending the new regime to UK branches of overseas firms. The Treasury has also published a draft order which will be used to give effect to this extension, and on which the Treasury is also seeking responses (the **draft order**).

In particular, the Treasury has stated that:

- The PRA does not intend to designate any senior management functions for the UK branches of EEA firms as primary responsibility for prudential supervision of a UK branch of an EEA firm rests with the home state regulator of its parent entity.
- The PRA expects to specify significantly fewer senior management functions for the UK branches of non-EEA firms than for equivalent UK firms, and that UK branches of non-EEA firms may only require one individual approved by the PRA as a senior manager.
- The PRA is unlikely to designate a large number of roles within the UK branches of overseas firms as "significant harm functions" which will fall within the scope of the certification regime.
- The FCA expects that the implementation of the new regime in the UK branches of overseas firms will be broadly aligned with the implementation of the new regime in equivalent UK firms.

It is important to note that senior managers in the UK branches of overseas firms will not be caught by the new criminal offence relating to decisions that cause a financial institution to fail (s36 Financial Services (*Banking Reform*) Act 2013).

Possible delay?

The Treasury has requested responses to the consultation by 30 January 2015. This deadline suggests that there is likely to be a delay to the proposals for the new regime being finalised, as it was originally proposed by the FCA and the PRA that the finalised rules for the new regime would be published by the end of 2014.

We anticipate that the consultation will be followed by a more detailed joint FCA and PRA consultation paper, which will set out in more detail their proposed approaches to implementing the new senior managers' regime in practice in the UK branches of overseas firms.

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The consultation is at www.gov.uk/government/consultations/regulating-individual-conduct-in-banking-uk-branches-of-foreign-banks.

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Service

SERVICE OF PROCEEDINGS ON THE UK ESTABLISHMENT OF AN OVERSEAS COMPANY

Teekay Tankers Ltd v STX Offshore & Shipping Co [2014] EWHC 3612 (Comm), 6 November 2014

Service of a claim on an overseas company's registered UK establishment was valid service for the purposes of regulation 7 of the Overseas Companies Regulations 2009 and s1139(2) Companies Act 2006, even though the claim did not relate to the UK establishment itself.

In early 2013, Teekay Tankers Ltd (**Teekay**), a Marshall Islands incorporated shipping company and STX Offshore & Shipping Co (**STX**), a shipping company incorporated in the Republic of Korea, entered into a series of shipbuilding contracts, including an English law governed option agreement (the **Option Agreement**). A dispute arose under the Option Agreement, and Teekay issued a claim in the Commercial Court on 11 April 2014 claiming USD 179 million plus interest (the **Claim**).

STX's "London Address"

Since 3 March 2014, STX has been registered with Companies House as "having established a UK establishment in the United Kingdom" under s1046 Companies Act 2006 (**2006 Act**). Overseas Company Regulations 2009 No 1801 Reg 7 requires an overseas company to register particulars of "(e) the name and service address of every person resident in the United Kingdom authorised to accept service of documents on behalf of the company in respect of the establishment, or a statement that there is no such person …". When STX filed its particulars (using the prescribed form OS IN01) it gave the name of a Mr Kang and identified an address in London (the **London Address**) as his address for service.

The court considered three issues: (i) was STX validly served by Teekay within the jurisdiction?; (ii) if so, should the proceedings be stayed on *forum non conveniens* grounds?; and (iii) if not, should permission

be given to serve out of the jurisdiction? For the purpose of this article, we focus on the first question.

Service of the Claim by Teekay

Teekay served its claim form at the London Address, relying on s1139(2) 2006 Act:

"(2) A document may be served on an overseas company whose particulars are registered under section 1046-

(a) by leaving it at, or sending it by post to, the registered address of any person resident in the United Kingdom who is authorised to accept service of documents on the company's behalf, or

(b) if there is no such person, or if any such person refuses service or service cannot for any other reason be effected, by leaving it at or sending it by post to any place of business of the company in the United Kingdom."

For this purpose, the "registered address" is the current address in the register available for public inspection (s1139(3)).

STX argued that Mr Kang was not authorised to accept service of the Claim because Reg 7 and form OS IN01 refer to a "person resident in the United Kingdom… authorised to accept service of documents on behalf of the company in respect of the establishment" and that the Claim was not in respect of the business of the establishment itself.

In addition, STX contended that the London Address was not a "place of business" of the company because, among other reasons, the office was not in its own name and was not fully operational when the Claim was served.

Decision – good service

Hamblen J held that service on Mr Kang's registered address was good service under s1139(2)(a). Section 1139(2)(a) is expressed in general terms and is not limited to claims in respect of the UK establishment and s1056(a) is expressed in mandatory terms (the regulations must require the company to register details of persons authorised to accept service on behalf of the company). If the requirement had been intended to be limited to business carried on by the establishment, the regulations would have been express on the point.

In addition, none of the leading texts suggests that service on a registered person under the Companies Act 2006 provisions is limited to documents concerning the business of the UK establishment.

The court also considered that this interpretation was in line with the statutory and historical context, and concluded that it had long been the position that, in relation to service on overseas companies, it was not necessary to establish a link between that subject matter of the claim and the business carried out in the UK (s694 Companies Act 1985 was an anomalous exception to that general rule in that it expressly permitted service of process on a branch of an overseas company only "in respect of the carrying on of the business of the branch").

The court also found that the London Address was a "place of business" of the company at which STX was validly served under s1139(2)(b) Companies Act 2006 and/or CPR r6.9(2) paragraph 7 because: (i) registering a UK establishment involves opening a place of business in the UK, even if it is yet to start carrying on business; or alternatively, (ii) STX had a place of business in the UK as a matter of fact having regard to all the evidence (relevant factors included the submission of the OS IN01 form, the fact that Mr Kang had authority to negotiate the lease on that address and that the address was listed as an office on STX's website). In reaching this conclusion, Hamblen J reiterated earlier authority that an address with which a company has no more than a transient or irregular connection would not be sufficient to constitute a place of business.

For completeness, the court refused STX's application for a stay on *forum non conveniens* grounds and indicated that had Teekay required permission to serve the Claim out of the jurisdiction, it would have granted it.

COMMENT

Serving process out of the jurisdiction can be a complex, expensive and time-consuming process requiring claimants to navigate a combination of English law, international conventions and the laws of the jurisdiction(s) in which service is intended to be effected. This case provides welcome clarification that it is not necessary for the subject of a claim to relate to the

activities of an overseas company's registered UK establishment for the claim to be validly served at that address, allowing a broader selection of claims to be served within the jurisdiction. This makes the process of commencing a claim in England against a foreign-domiciled defendant more straightforward, efficient and cost effective for parties who are able to take advantage of this decision.

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Settlement

WITHDRAWAL OF PART 36 OFFER

Super Group plc v Just Enough [2014] EWHC 3260 (Comm), 27 May 2014

A defendant's Part 36 offer in respect of a claim and counterclaim could not be accepted once the defendant had withdrawn its offer. Despite alleged ambiguity, the withdrawal was valid as it was an express notice in writing in terms which made it clear to the offeree that the offer had been withdrawn. Further, the claimant could not accept a Part 36 offer in respect of a claim and counterclaim once it had discontinued its claim.

The claimant claimed for breach of contract and the defendant counterclaimed for repudiatory breach. On 26 November 2013 the defendant served a Part 36 offer in respect of settling both the claim and counterclaim. It was the only offer in discussion at the time.

On 25 April 2014 the defendant wrote to the claimant withdrawing the Part 36 offer (the **Withdrawal**):

"Needless to say, on the issue of costs we will further refer the court to the fact that our client made every effort to settle this matter, which was simply ignored by yourselves and your client which offers are, needless to say, withdrawn. The only basis upon which our client will settle the dispute is in terms if you meet our client's cost in full, both in respect of the High Court proceedings and American proceedings".

The letter also set out the terms on which the defendant was prepared to settle which were, in summary, for the defendant to be reimbursed for all of its costs and paid the full amount for the counterclaim.

On 8 May 2014 the claimant served a notice of discontinuance of its claim. Then, on 15 May 2014, the claimant attempted to accept the Part 36 offer.

The claimant argued that the withdrawal letter of 25 April 2014 was ambiguous because it was not a "formal notice of withdrawal" as referred to as a requirement of a Part 36 offer withdrawal in Rix LJ's judgment in *C v D* [2011] EWCA Civ 656. The claimant also argued there was ambiguity because later in the letter it made reference to the Part 36 offer, and subsequent correspondence also made reference to the Part 36 offer, both suggesting the offer was still on the table. The defendant argued that, properly construed, the letter of 25 April 2014 was not ambiguous and was a clear withdrawal of the Part 36 offer.

Requirements for withdrawal

Flaux J stated that an offeror may withdraw an offer after expiry of the offer's notice period if the offeree had not accepted by that point, by the offeror serving written notice on the offeree. Withdrawal of a Part 36 offer

"required express notice in writing in terms which bring home to the offeree that the offer has been withdrawn" (as per Moore-Bick LJ in *Gibbon v Manchester City Council* [2010] EWCA Civ 726). An implied withdrawal is insufficient.

Flaux J confirmed there is no prescribed form of wording to be used for a withdrawal of a Part 36 offer. Whilst Moore-Bick LJ in *Gibbon* said [at 17] that "in order to avoid uncertainty [a withdrawal] should include an express reference to the date of the offer and its terms, together with some words making it clear that it is withdrawn", Flaux J understood this to mean that it was preferable, but not mandatory, to include reference to the date of the Part 36 offer which is being withdrawn.

Had the defendant's Part 36 offer been withdrawn?

Flaux J held that the letter dated 25 April 2014 clearly withdrew the Part 36 offer. It was obvious that the wording referred to the defendant's Part 36 offer as this was the only offer to settle that was in discussion at that time.

Further, the terms on which the defendant sought the costs to be calculated were wholly inconsistent with any suggestion that the Part 36 offer remained on the table. Referring to the letter dated 25 April 2014, Flaux J stated that "… any reasonable solicitor would have understood that letter as withdrawing the Part 36 offer".

Flaux J also dismissed suggestions of ambiguity caused by the subsequent correspondence, stating that it is not possible to revive an offer or bring a Part 36 offer back into existence by subsequent correspondence.

***Obiter* – Part 36 offer cannot be accepted once a claim no longer exists**

Although Flaux J had found that the withdrawal letter dated 25 April 2014 had successfully prevented the claimant from accepting the defendant's now withdrawn Part 36 offer, he considered *obiter* the effect of the claimant's notice of discontinuance of their claim.

Flaux J said that a Part 36 offer can only be accepted where it is in respect of a claim which is in existence. This meant that once the claimant had served notice of discontinuance of its claim, there was no claim which the Part 36 offer could be in respect of. This also meant that the claimant could not accept the Part 36 offer in respect of the counterclaim only. Otherwise, claimants would be in a position where they could accept an offer effectively on different terms from the terms on which it was being offered.

COMMENT

A Part 36 offer is a useful tactic to help focus another party on settlement because if the offeree fails to obtain a judgment more advantageous than the offer at trial there can be serious cost consequences for the offeree.

The use of Part 36 offers can be very specific to each case. For example, more than one Part 36 offer can remain open at a time, and a Part 36 offer can be in respect of a whole claim or part of a claim and a counterclaim. Part 36 offers must specify a period of not less than 21 days within which the offeror will be liable for the offeree's costs and can only come to an end if validly withdrawn. The Part 36 offer can be accepted until the end of trial unless it has been validly withdrawn. It is important that each Part 36 offer and withdrawal made or received is recorded and that each withdrawal is drafted clearly.

Flaux J made useful comments on the requirements for an effective withdrawal of a Part 36 offer. A withdrawal of a Part 36 offer needs to make it absolutely clear that a particular Part 36 offer is being withdrawn, but there is no specific form of notice. Part 36 is intended to be a clear and concise set of procedural rules which do not incorporate all the rules of law governing the formation of contracts.

This case also strongly supports the natural interpretation of Part 36 that a Part 36 offer cannot be accepted once a claim no longer exists as a result of a validly served notice of discontinuance.

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Trust

SUPREME COURT CONFIRMS THAT TRUSTEES ARE LIABLE ONLY FOR LOSS CAUSED DUE TO BREACH

AIB Group (UK) Plc v Mark Redler & Co Solicitors [2014] UKSC 58, 5 November 2014

AIB sought to recover damages for breach of trust from its solicitors who had negligently acted on a secured lending transaction for AIB. The Supreme Court examined the principles applicable to equitable compensation as a remedy for breach of trust and, applying the decision of the House of Lords in *Target Holdings v Redferns* [1996] AC 421, confirmed that trustees are liable only for losses which directly flow from their breach.

Mark Redler & Co Solicitors (**Mark Redler**) acted for both the claimant bank, AIB Group (UK) Plc (**AIB**), and the borrowers on a GBP 3.3 million loan. In return for the loan, AIB was supposed to secure a first legal charge over the borrowers' property which was valued at GBP 4.25 million. The property was already subject to a first legal charge in favour of Barclays Bank plc (**Barclays**) for borrowings of GBP 1.5 million on two accounts. It was a condition of the AIB loan that the existing Barclays charge be redeemed on or before the advance. Barclays informed Mark Redler of a redemption figure for one of the accounts which Mark Redler mistakenly took to be the total figure necessary to redeem the Barclays charge. Due to Mark Redler's error, a debt of approximately GBP 300,000 was left secured by the Barclays charge. As a result, the amount which should have been passed on to Barclays went to the borrowers, who received GBP 300,000 more than they otherwise would have.

Subsequently, Barclays and AIB entered into a deed of postponement which recognised the primacy of the Barclays charge and agreed to the registration of AIB's charge as a second charge. Subsequently, the borrowers defaulted and the property was sold by Barclays for GBP 1.2 million (considerably lower than the valuation of the property). Out of this, AIB received GBP 867,697.78.

AIB brought proceedings against Mark Redler for, *inter alia*, negligence, breach of contract and breach of trust. It claimed that it was entitled to recover approximately GBP 2.4 million, the full amount of its loan minus the recovery from the sale of the property. Mark Redler contended that AIB was entitled to recover only the amount by which it had suffered a loss as compared to a situation where Mark Redler had ascertained and remitted the full amount of the Barclays debt to redeem the charge. According to Mark Redler, this amounted to around GBP 275,000.

At first instance, as preliminary issues, Cooke J had to decide whether Mark Redler had acted in breach of trust and what remedy (if any) AIB was entitled to. He held that Mark Redler was liable to AIB for the amount obtained by Barclays from the sale of the property which would otherwise have gone to AIB. The judge looked at what would have happened but for the breach of trust. He also noted that it was apparent that AIB was keen to lend to the borrowers and AIB would not have withdrawn from the transaction because of Mark Redler's failure to redeem the Barclays charge. Both the Court of Appeal and the Supreme Court agreed that Mark Redler was liable for the lower amount.

What losses are to be compensated?

The main issue in the present case was whether Mark Redler was liable to compensate AIB not only for losses caused by its breach but also for losses which AIB would

have suffered in any event, irrespective of the breach. The Supreme Court confirmed the basic principle was that AIB should be compensated for any loss it would not have suffered but for the breach. Lord Reed explained that according to this principle, he understood "loss" to mean "what the beneficiary has been deprived of as a result of the breach". It was concluded that, in the absence of fraud, it would not be right to compensate AIB for a loss which it would have suffered even if Mark Redler had properly performed its duties. Any remedy which reflected neither a loss caused nor a profit gained would be penal in nature.

On the facts of this case, Lord Toulson commented that AIB had taken the risk of a default by the borrowers and the fault of the solicitors lay in increasing the bank's exposure by releasing the loan funds to the borrower without ensuring that AIB had received the full security. Lord Reed said that AIB's case suffered from three fallacies. First, it assumed Mark Redler had misapplied the entire sum of GBP 3.3 million while only approximately GBP 309,000 had been misapplied. However, this was not a point of appeal and was not further discussed. Second, AIB assumed that the liability was fixed as on the date of the breach. This was incorrect and the liability was to be determined at the time of trial. Third, AIB's argument wrongly supposed that Mark Redler's liability did not depend on a causal link between the breach of trust and the loss.

The law relating to equitable compensation was succinctly summed up by Lord Reed: "[t]he measure of compensation should therefore normally be assessed at the date of trial, with the benefit of hindsight. The foreseeability of loss is generally irrelevant, but the loss must be caused by the breach of trust, in the sense that it must flow directly from it".

Equitable compensation and common law damages are different remedies with different rules

Lord Reed inspected the relationship between equitable compensation and common law principles. His Lordship commented that the loss resulting from a breach of duty has to be measured according to the legal rules applicable to the breach of that specific duty. In a similar tone, Lord Toulson stated that equitable compensation and common law damages are remedies which are based on separate legal obligations. The rules appropriate to a breach of duty by a trustee therefore had to be determined in light of the characteristics of the duty in question.

Primary remedy for breach of trust

Traditionally, the primary remedy for breach of trust has been reconstitution of the trust fund. In the present case, this would mean holding Mark Redler liable for about GBP 2.4 million to reconstitute the trust fund (GBP 3.3 million minus approximately GBP 868,000 that AIB recovered from the sale of the secured property). However, as per Lord Browne-Wilkinson in *Target Holdings*, in a situation where a beneficiary of a trust had become absolutely entitled to it, the normal order would be for compensation to be paid directly to that beneficiary. An obligation to reconstitute the trust fund once the transaction had been completed would be artificial. This view was reiterated by Lord Reed. AIB contended that in the present case, the "underlying commercial transaction" had never been completed because the shortfall required to redeem the Barclays charge had not been paid. However, the Supreme Court did not agree and stated that since the trust had come to an end, Mark Redler could be ordered to compensate AIB directly.

COMMENT

This decision confirms the principles laid down by the House of Lords in *Target Holdings* and clarifies the law relating to the liability for breach of trust and equitable compensation as a remedy. It is only fair that a trustee be held liable for the loss actually caused by its breach and not a loss which the beneficiary would have suffered in any case. The main proposition extends this instinctive understanding of loss and causation from the domain of common law to equitable compensation. It appears that in calculating the loss resulting from a breach of trust, the scope of the trustee's obligation, contractual or otherwise, would be considered.

In cases where they cannot proceed against borrowers (as in this case where the borrowers were bankrupt), lenders might turn to equity and breach of trust to attempt to recover more than they would have from valuers and solicitors if they proceeded solely on negligence and

breach of contract. This decision puts into doubt the viability of such a strategy in situations where the loss suffered does not directly flow from a breach by the valuer or solicitor.

This case will be of interest to solicitors who act, as is often expected in such transactions, for both lenders and borrowers and for the clients of such solicitors. It will also be of interest to practitioners for the clarity it provides regarding the assessment of equitable compensation as well as for the detailed examination of the relationship between common law principles and equity.

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EUROPEAN ACCOUNT PRESERVATION ORDERS (EAPOS)

Thursday 15 January 2015, 9.00 – 10.00am

Mona Vaswani, Partner – Litigation and Sarah Garvey, Counsel – Litigation

This seminar provides an update on the new legislation providing for a pan-European Freezing Order. Mona and Sarah explain the key provisions and assess the risks for commercial parties and highlight some of the practical implications for banks who will have to administer such orders. The UK Government has not opted in to this Regulation but for commercial parties (especially banks) operating across Europe and with bank accounts in Member States this new legislation will be of relevance.

Registration and buffet breakfast will take place from 8.30am; the seminar commences at 9.00am.

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