CHANCERY BAR

Response of the Chancery Bar Association to the Law Commission's Consultation on its Twelfth Programme of Law Reform

Introduction

1. The Chancery Bar Association is one of the longest established Bar Associations and represents the interests of over 1,100 members handling the full breadth of Chancery work at all levels of seniority, both in London and throughout England and Wales. It is recognised by the Bar Council as a Specialist Bar Association. Full membership of the Association is restricted to those barristers whose practice consists primarily of Chancery work, but there are also academic and overseas members whose teaching, research or practice consists primarily of Chancery work.

2. Chancery work is that which is traditionally dealt with by the Chancery Division of the High Court of Justice, which sits in London and in regional centres outside London. The Chancery Division attracts high profile, complex and, increasingly, international disputes. The Companies Court itself deals with some 12,000 cases each year.

3. Our members offer specialist expertise in advocacy, mediation and advisory work including across the whole spectrum of company, financial and business law. As advocates members are instructed in all courts in England and Wales, as well as abroad.

4. This response is the response of the Association to the Law Commission's Consultation on its Twelfth Programme of Law Reform. This response has been led by John Machell QC, Tim Fancourt QC, Andrew Twigger QC, Andrew Francis and Alana Graham. The topics set out below have been selected following a request for suggestions made to all members of the Association. The authors of the sections below are shown in the footnotes.

Rectification[1]

5. The Law Commission's suggested projects include reference to the question of whether pre-contractual negotiations ought to be admissible as an aid to construction of contracts. We agree that this is a topic which merits consideration but wonder whether it could be expanded

[1] Andrew Twigger QC

to cover the related subject of when a contract can be rectified as a result of a mistake made by one, or both, of the parties. This subject was considered by the House of Lords in *Chartbrook Ltd. v. Persimmon Homes* [2009] 1 AC 1101, the same case which gives rise to the issue about pre-contractual negotiations. In practice, the two areas frequently arise for consideration together because it is accepted that pre-contractual negotiations are admissible in a claim for rectification.

6. The decision in *Chartbrook* concerning rectification has also been the subject of academic and judicial criticism. Lord Hoffmann held that a document could be rectified to bring it into line with what an objective observer would think the parties' intentions were, having regard to what they did and said before the agreement was made. This has the potential to result in one party being held to the other party's intended meaning, even though the first party had not subjectively made any mistake at all (as happened on the facts of the *Chartbrook* case). In *Daventry District Council v. Daventry and District Housing Ltd.* [2012] 1 WLR 1333 Toulson LJ doubted the correctness of the *Chartbrook* principle (paras 179-175) and Lord Neuberger said that it "*may have to be reconsidered or at least refined*" (para 195), whilst Etherton LJ considered the principle was correct but would require refinement (para 104).

7. We suggest that this is an area in which the law is complex, hard to understand, and has the potential to cause substantial unfairness where a party who was not mistaken is treated as if he had been.

Attribution of knowledge to a company[2]

8. The Law Commission suggestions refer to corporate liability. We understand that this refers to the issues surrounding when a company is criminally liable. We suggest that a consideration of corporate criminal liability might usefully be combined with the issue of when fraudulent intentions are to be attributed to a company under the civil law. There are currently a number of different mechanisms by which the law attributes guilty knowledge or fraudulent acts to a company. These include principles of agency, the "directing mind and will" principle and the identification doctrine considered in *Meridian Global Funds Management Asia Ltd. v. Securities Commission* [1995] 2 AC 500. There is no consistency in the result of applying these different mechanisms.

[2] Andrew Twigger QC

9. The problem is exacerbated further by the exception to the normal principles of attribution which potentially arises where the person whose knowledge or conduct is sought to be attributed to the company is acting to defraud the company (the so-called rule in *In re Hampshire Land Co*. [1896] 2 Ch. 743). This exception was the subject of consideration by the House of Lords in *Stone & Rolls Ltd. v. Moore Stephens* [2009] 1 AC 1391. Unfortunately, it is difficult to distil a clear ratio on the point because each of their Lordships reached his decision for different reasons, some of which depended on the unusual facts of that particular case. Subsequent recent decisions of the Court of Appeal (*Bilta (UK) Ltd. v. Nazir* [2013] 3 WLR 1167) and the Commercial Court (*Madoff v. Raven* [2013] EWHC 3147 (Comm)) have had to grapple with the questions whether the Hampshire Land exception applies to claims against the company, as well as to claims by the company, and whether it is necessary that the company is capable of being regarded as a victim of the fraud for the exception to apply.

10. We suggest that, despite the recent decisions, the position remains unclear and this is another area in which the law is highly complex and hard to understand.

Tracing and following[3]

11. The rules which determine when someone is entitled to claim the return of his property from someone into whose possession it has come ("following"), or to claim other assets for which that property has been substituted ("tracing"), have widely been recognised as complex and out of step with modern standards. Much of the difficulty arises because there are two sets of rules: one applicable at common law and the other in equity. The common law rules do not enable property to be traced or followed once it has become mixed with property belonging to someone else. The equitable rules do allow tracing or following in such circumstances, but those rules are only available where the claimant has a distinct equitable title to the relevant assets, that is where the property is held subject to some fiduciary relationship. This has led to a somewhat artificial principle that a thief holds stolen property on trust so that the victim can rely on equitable tracing rules.

12. There has been much criticism of the existence of two separate sets of rules, most notably by Lord Millett in *Foskett v. McKeown* [2001] 1 AC 102, who said (at p. 128), "*There is certainly no*

[3] Andrew Twigger QC

logical justification for allowing any distinction between them to produce capricious results in cases of mixed substitutions by insisting on the existence of a fiduciary relationship as a precondition for applying equity's tracing rules."

13. Furthermore, even where equitable tracing rules apply, the principles which determine what share the claimant has in a fund in which his property was mixed with that of other innocent parties are unnecessarily complex. Where the mixture happens in a current bank account, the rule is normally said to be "first in, first out", whereas in other cases, the rule contemplates a pari passu allocation between the contributors to the fund. These rules are out of step with modern standards, have the potential to cause substantial unfairness and make it difficult to advise clients as to their entitlements.

Formalities for executing wills and rectification[4]

14. Several Commonwealth countries have 'substantial compliance' provisions, allowing the court to dispense with the need for formalities in cases where it is satisfied that a document represents the testator's intentions. The reasons given against such a power by the Law Reform Committee in their 22nd report in 1980 are, we would respectfully suggest, somewhat lacklustre, and we consider it may now be time for the question to be reconsidered. The risk of excessive litigation is smaller now than it was, in that there is a body of Commonwealth jurisprudence as to how such powers are to be exercised by the Courts. Indeed, it would in many cases reduce litigation: it would reduce the need for claims in professional negligence; it would be likely to reduce, on balance, the need for claims under the Inheritance (Provision for Family and Dependants) Act 1975; it would obviate the need for proprietary estoppel claims where wills were not properly executed such as *Powell v Benney* [2007] EWCA Civ 1283, (2007) 151 S.J.L.B. 1598, [2008] 1 P. & C.R. DG12; and other attempts to circumvent the formality requirements, such as *Marley v Rawlings* [2012] EWCA Civ 61, [2013] Ch. 271 where the disappointed would-be beneficiaries have tried to rely on rectification.

Arbitration clauses in trusts[5]

15. Arbitration for trusts disputes was considered for inclusion in the 11th Programme, of Law

[4] Alexander Learmouth and Kevin Shannon
[5] John Machell QC

Reform but was rejected only for lack of capacity: see paragraphs 3.69 and 3.70.

16. We would suggest that the matter is considered for inclusion again and refer to a paper produced by the Executive Committee of the Trust Law Committee which can be found at www.step.org/arbitration-trust-disputes.

IP rights and insolvency[6]

17. Licences relating to the use of intellectual property rights ("IPRs") (for example, patents, trade marks and copyright) are already very common. As commerce becomes more dependent upon IPRs due to its increasing sophistication, such licensing activity is likely to increase. Also, insolvency is, of course, not uncommon in the business world. At present, when either the licensor or the licensee become insolvent, it is not clear what happens to the license or the goods or services that formed the subject matter of that licence. The situation is complicated further when sub-licences have been granted, and an intermediate member of the chain becomes insolvent. Further, complications arise if the various parties are located in different jurisdictions.

18. It would facilitate the smoother running of trade if clear rules were enacted that struck a fair balance between the rights holder and the exploiter of those rights, with suitable provision being made for any goods or services that are in the process of being made or provided during the insolvency process. At present, each case is resolved individually in a manner that often reflects the perceived bargaining position of the parties involved, which means that the weak, but meritorious, party is often disadvantaged.

Landlord and Tenant – assignment of leases[7]

19. The decision of the Court of Appeal in *K/S Victoria Street v House of Fraser* [2011] EWCA Civ 904 causes substantial problems in practice. As well as deciding the question in issue, namely whether an agreement by an existing guarantor of a tenant to enter into a guarantee of the tenant's assignee's obligation was enforceable (No), the Court expressed views on the operation of the authorised guarantee agreement provisions of the Landlord and Tenant

[6] Michael Edenborough QC
[7] Timothy Fancourt QC

(Covenants) Act 1995 and other issues that might arise. Although obiter, these observations were made after full argument in some cases and by an extremely authoritative Court. It is not clear that all the views expressed are correct.

20. The effect of the dicta is that even where a guarantor *has voluntarily* signed a new guarantee of an assignee tenant, that guarantee is unenforceable; and that a tenant cannot assign a lease to a guarantor. This cuts across very common property transactions within groups of companies, and it is doubtful whether the draftsman of the Act intended that consequence. There should be no bar on a tenant or a guarantor actually standing as guarantor of an immediate or subsequent assignee of the term of years, though whether or not a pre-existing obligation to do so should be enforceable is a more debatable point.

21. There is also a lack of clarity in section 15 of the Act in relation to concurrent leases – which of the original landlord and the concurrent lessee is able to take the benefit of the tenant covenants during the term of the concurrent lease? See in this regard Megarry & Wade (8th ed), paras 17-135, 20-115, and the views expressed by Lightman J in *First Penthouse Ltd v Channel Hotels and Properties (UK) Ltd* [2004] 1 EGLR 16.

John Machell QC

Andrew Twigger QC

Alana Graham

Andrew Francis

Timothy Fancourt QC

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