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FIDUCIARY DUTIES IN INTERNATIONAL LITIGATION AND ARBITRATION

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What are fiduciary duties and when do they arise?

The traditional categories

1. Whilst some people have argued that there should be, in English law there is no principle of good faith of general application in the law of contracts. Outside the law of contract, it is only some relationships which give rise to a duty of care in tort and compensation for loss suffered by any breach. Lawyers become adept at searching for ways to enlarge the situations to which a party may be subject to legal obligations which are not rooted in, say, strict property rights. The equitable doctrine of fiduciaries has proved to be one of the most flexible and useful tools in modern commercial law.

2. The purpose of this part of the present session is to examine when fiduciary duties arise. We will examine briefly what fiduciary duties are and the classic or traditional situations in which they arise. We will then look at some of the more unusual contexts in which fiduciary duties arise and will examine how the court goes about deciding whether a fiduciary duty arises on the facts of a case.

3. You will be hearing later directly from John McGhee QC, the current editor of the leading text Snell's Equity (33rd ed) on the incorporation of the English doctrine of fiduciaries into Chinese law and no talk on fiduciary duties would be possible without reference to this seminal work.

4. As he puts it at [7-001], fiduciary relationships are concerned with the inappropriate use of a position of superiority over another person. The duties may arise because of a contract but the existence of the contract is merely incidental to the imposition of duties which arise from the nature of the relevant relationship. Whilst there are some settled categories of fiduciary relationship, which we will return to below, the categories are not closed.

5. In the leading case of *Bristol & West v Mothew* [1998] Ch 1 at 18 Millett LJ said:

   "*A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must*

act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal. This is not intended to be an exhaustive list, but it is sufficient to indicate the nature of fiduciary obligations. They are the defining characteristics of the fiduciary. As Dr. Finn pointed out in his classic work Fiduciary Obligations (1977 ed p. 2), he is not subject to fiduciary obligations because he is a fiduciary; it is because he is subject to them that he is a fiduciary."

6. This passage is important also for identifying some of the significant consequences which flow from establishing that someone is a fiduciary but a core principle is "*one person is in a relationship with another which gives rise to a legitimate expectation, which equity will recognise, that the fiduciary will not utilise his or her position in such a way which is adverse to the interests of the principal*" - see *Arklow Investments Ltd v Maclean* [2000] 1 WLR 594 at 598G.

7. We turn now to consider some of the paradigm or settled categories where a fiduciary relationship has been held to arise. As you will see they all have the hallmark of situations where one party (the fiduciary) is required to subjugate his or her own interests for the benefit of his principal.

8. The first and most obvious example of a fiduciary relationship is that which arises between a trustee and beneficiary. The trust in question may be an express trust or a trust which arises by operation of law (such as a resulting trust or constructive trust) although, unlike some other jurisdictions, English law has generally rejected any notion of a remedial constructive trust. So, a trustee of a parcel of land who has undertaken to the settlor, to hold the land for the benefit of another (perhaps the settlor's children) is not allowed to put himself in a position where his interests conflict with those of the beneficiaries, for example by selling the property to himself. Lots of examples of trusts arise in international commerce: for example, asset managers, the managers of pension plans and endowment plans will all be examples where a fiduciary relationship arises. The administrator or executor of an estate will also owe fiduciary duties.

9. The next example arises commonly in a commercial context. An agent will owe fiduciary duties to her principal. If the agent acts for two principals with potentially conflicting interests without obtaining the informed consent of each, she will act in breach of fiduciary duty. That was the context of the *Mothew* case itself which concerned the obligations owed by a solicitor who was acting in a mortgage transaction on behalf of both mortgagor and mortgagee. The relationship between solicitor and client is a classic example of a relationship where fiduciary duties will be owed.

10. It is also well established that in company law that a director, including shadow directors (see the recent decision in *Instant Access Properties Ltd (In Liquidation) v Rosser* [2018] EWHC 756 (Ch)) and *de facto* directors) of a company owes fiduciary duties to the company of which he is a director and a promoter of a company owes such duties to the company he is promoting. Although in England and Wales, the law on directors' duties has been largely codified in Chapter 2 of Part 10 Companies Act 2006 (sections 170 to 181), the duties are framed in terms which mirror the language of those equitable duties. In some rare situations, a director may owe fiduciary duty to the shareholders of the company.

11. Partners in a partnership owe fiduciary duties to one another. In the new form of entity, the Limited Liability Partnership the members owe fiduciary duties to the LLP (see *F & C Alternative Investments (Holdings) Ltd v Barthelemy (No 2)* [2012] Ch 613 at [219] and *Jeremy*

Hosking v Marathon Asset Management Ltd [2016] EWHC 2418 (Ch) which concerned the principles on forfeiture of fees).

12. In the context of insolvency and restructuring, a receiver of property owes fiduciary duties to the mortgagee when appointed under a power contained in the mortgage – see *Medforth v Blake* [2000] Ch 86.

13. Finally, an unusual example of a fiduciary duty arose in *Attorney General v Blake* [2001] AC 268 which concerned the notorious George Blake who was held to owe fiduciary duties to the Crown in regard to the book he published about his life and work as a spy.

Ad-hoc fiduciary duties arising as a matter of fact

14. In other contexts, there may be no presumption of a fiduciary relationship although one may be established on the facts. It is one of the great strengths of the English judicial tradition that the law can adapt to new situations in this way, but the flip side of this is that it can be difficult to predict whether the court will hold that fiduciary duty exists.

15. A fiduciary expectation will normally be inappropriate in the context of a commercial arrangement; it would be unusual to expect a commercial party to subordinate its own interests to those of another commercial party.

16. However, it is possible for fiduciary duties to arise in such circumstances, including as between joint venturers, if, after an examination of the facts of the case, a fiduciary expectation is found to be appropriate in the circumstances (*Arklow,* above). Whether a fiduciary relationship arises will always be a fact-sensitive enquiry.

17. Two Australian authorities show how difficult it is to draw the line between when a duty will and will not arise.

18. *Hospital Products v USSC* (1984) 156 CLR 41 concerned an exclusive distributorship under which the distributor was to make "*best efforts*" to distribute the manufacturer's products. Instead the distributor copied the manufacturer's products and started competing against it. Did it owe a fiduciary duty not to do so (with the consequence, under Anglo-Australian law that the manufacturer could claim the profits made by the distributor in so doing rather than merely the losses that flowed from the breach of contract)? One might argue that the manufacturer reposed trust and confidence in the distributor to advance its economic interest, and was vulnerable to the distributor's superiority in that respect and so a fiduciary duty arose. Ultimately though, the majority of the High Court was not persuaded, and held that the relationship was regulated exclusively by contract. That the parties dealt commercially at arm's length and on an equal footing seemed to be decisive. In layman's terms, the purpose of the deal included the distributor making a profit from selling the manufacturer's wares, so the manufacturer should have included contractual terms regulating the distributor's conduct, rather than seek to rely on equitable principles, if it was to be entitled to the relief it was seeking.

19. Yet in *UDC v Brian* (1985) 157 CLR 1 the court reached a different conclusion. The parties were in a joint venture to develop a property. UDC provided the finance and took a mortgage over the relevant property the terms of which allowed it to earn additional profit to that which it stood to earn in the joint venture more generally. Here, the High Court held there was a fiduciary relationship meaning that UDC had to account for these additional profits. Even though both sides were commercial parties, the court considered that the arrangements

resembled a partnership (one of the classic situations where fiduciary duties arise) with the attendant qualities of trust and confidence and imposed a fiduciary duty for that reason. This reasoning is not entirely satisfactory because a joint venture is not a partnership (the term "joint venture" has no technical meaning), and not all joint ventures give rise to fiduciary duties, so what aspects of the joint venture are decisive?

20. The English courts have grappled with this question, particularly *Ross River Ltd v Waverly Commercial Ltd* [2013] EWCA Civ 910 where Lloyd LJ identified three important cases which have considered the nature of the fiduciary obligations that can arise in the context of joint ventures (at [62]):

(a) *Murad v Al Saraj* [2004] EWHC 1235 (Ch): Etherton J (as he then was) found that the defendants owed the claimants fiduciary duties in connection with a joint venture to acquire a hotel. The fiduciary duties were held to arise because the parties were in the position of joint venturers, the relationship was one of trust and confidence, the defendant had taken on a number of responsibilities in connection with the joint venture, in some respects acting as the claimants' agent, the claimants had no relevant experience, they had no knowledge of the arrangements made by the defendant with third parties and they trusted the defendant with extensive discretion to act in relation to venture which affected the claimants' interests. Lloyd LJ also observed at [36]:

"It is to be noted that the fiduciary obligation was held to be owed by Mr Al-Saraj even though the joint venture was carried out through a jointly-owned company, Danescroft Ltd, and even though Mr Al-Saraj was not a shareholder in Danescroft, shares being held instead by a company wholly owned by him, Westwood Ltd."

(b) In *JD Wetherspoon plc v Van de Berg & Co Ltd* [2009] EWHC 639 (Ch) the claim concerned two actions arising out of an arrangement between JD Wetherspoon (J) and Van de Berg & Co Ltd (V) under which the latter found properties for the former to acquire. Peter Smith J held that it was clear from the evidence of the relationship between J and V that there was a special relationship of trust and confidence between J's chairman and CB, a director of V. Accordingly, CB owed a fiduciary duty to the claimant (it was, on the other hand, found that two other directors, RH and GA did not owe any such duty, illustrating the proposition that the existence of fiduciary duty is highly fact-sensitive). In reaching his conclusions on the existence of a fiduciary relationship, Peter Smith J cited (at [76]) the following observations of the Court of Appeal in *Conway v Ratiu* [2006] 1 All ER 571 at 573:

"[78] There is, it seems to me, a powerful argument of principle, in this intensely personal context of considerations of trust, confidence and loyalty, for lifting the corporate veil where the facts require it to include those in or behind the company who are in reality the persons whose trust in reliance upon the fiduciary may be confounded…

[80] Nor in my view should it matter in principle where a fiduciary duty is engendered by a contractual relationship whether the client is entered into a direct contractual relationship with a fiduciary or through an agent or in the case of a corporate client through the use of a nominee company… as in this case."

(c) *John v James* [1991] FSR 397: In this case the claimant, Elton John, asserted fiduciary duties against his manager, publisher and associated companies under agreements

for the exploitation of compositions, accompanied by the assignment of the copyright in the compositions. The defendant was found to owe fiduciary duties to John even though the copyrights were assigned outright to the defendant and the defendant had its own interest in the exploitation of the compositions. Lloyd LJ found this, at [55] of *Ross River v Waverly*, to be:

> *"…a clear and instructive example of a transaction in the nature of a joint venture where the relevant assets belong legally and beneficially to one party, whose task it is to exploit them, but they are to be exploited for the common benefit of both parties, and where fiduciary duties arose from the situation despite the fact that the operator had its own personal interest in the exploitation to which it was entitled to have regard."*

21. It is suggested that the following general points can fairly be said to emerge from these authorities:

    (a) The nature of the fiduciary obligations owed is itself a fact-sensitive enquiry to be determined by the nature of the relationship before the court; not every fiduciary will owe the same obligations (*Ross River v Waverly* at [64]). In an appropriate context, the duties owed will extend beyond a fiduciary duty of good faith to include, for example, a duty not to profit from one's position as a fiduciary; or a duty not to place oneself in a position where one's interests conflict or might conflict with the duties owed to the principal; or a duty to provide full disclosure of dealings relating to the transaction in question and/or any potential issues of conflict.

    (b) Control of relevant matters, such as negotiation or ownership of assets, is a particularly strong indicator of the reliance likely to have been placed on one party by the other, and of the existence of a relationship of trust and confidence: *Ross River v Waverly* (at [60] to [63]); *John v James*. A fiduciary who has freedom to determine how the interests of a beneficiary are to be served requires the supervision of equity: see *Ross River v Waverly* at [51] to [52].

    (c) The closer the resemblance of the arrangements to one of the traditional categories of fiduciary duty the more likely that a court may find that one arises ad hoc.

    (d) In assessing the nature of the obligations assumed or owed by the parties, the court may well look through the structures established for the purpose of carrying out a joint venture, or holding an interest in it, to the underlying relationship between the claimant and defendant: *Murad v Al-Saraj*; *Wetherspoons v Van de Berg*; *Conway v Ratiu*.

22. At the time of this seminar, the decision of Nugee J in *Glenn v Watson* is awaited. That case concerned a property joint venture conducted via complex trust structures but where there was a long standing personal relationship between the two ultimate protagonists, Sir Owen Glenn (a wealthy New Zealand businessman, whose interests contributed materially all the money to the venture), and Eric Watson (another wealthy New Zealand businessman, who professed to be able to introduce investment opportunities to the joint venture). To vastly oversimplify the issues, it was alleged that Mr Watson was making secret profits from his own undisclosed interest in the opportunities he was introducing to the joint venture – in other words he was to take a profit from the joint venture itself, but was also alleged to be entitled to a profit share in the projects that the joint venture was investing in (unbeknownst, it was said, to Sir Owen). When the decision comes down, it is hoped that it will shed light on

whether a fiduciary duty is owed in such a situation and if so, how that squares with the ostensible arms' length commercial basis on which the deal was struck.

23. In summary, it seems that whether these "ad hoc" fiduciary duties arise is a combination of factors such as the vulnerability of one side to the other in the performance of the project, how closely the facts in question resemble one of the "classic" situations in which a fiduciary duty arises, how reasonable it was for the parties to act to protect their own interests, what the unspoken mutual expectations of the parties were, and even an overall sense of fairness of outcome. English courts always try to decide new cases logically and with the application of principle derived from precedent, rather than a raw appeal to the merits – but at the boundaries of the law of fiduciary duties it remains exceptionally difficult to determine where the line will be drawn.

Remedies for breach of fiduciary duty against perpetrators and third parties

Introduction

24. In this section, we consider the remedies for breach of fiduciary duty against perpetrators and third parties.

25. In particular, we consider the important role of facilitators and intermediaries in a fraudulent breach of trust/fiduciary duty. Facilitators and intermediaries such as banks, lawyers, providers of fiduciary/company administration services and trust companies play a critical role because their services enable fraud to occur and without them, in many cases, the relevant fraud would not succeed.

26. We will first of all consider the remedies for breach of fiduciary duty against the perpetrators themselves. We will then go on to consider what remedies are available against third parties. Personal claims against third parties require proof of a particular state of mind, and we will round off the session by looking at that question in particular.

Remedies for breach of fiduciary duty against perpetrators

27. It is always important to remember that a breach of duty by a fiduciary is not necessarily a breach of a fiduciary duty. The fiduciary may well owe some duties which are not fiduciary in nature, in addition to those that are.

28. In the New Zealand case of *BNZ v NZ Guardian Trust Co Ltd* [1999] 1 NZLR 664 at 687 Tipping J stated that:

> "*Breaches of duty by trustees and other fiduciaries may broadly be of three different kinds. First, there are breaches leading directly to damage to or loss of the trust property; second, there are breaches involving an element of infidelity or disloyalty which engage the conscience of the fiduciary; third, there are breaches involving a lack of appropriate skill or care. It is implicit in this analysis that breaches of the second kind do not involve loss or damage to the trust property, and breaches of the third kind involve neither loss to the trust property, nor infidelity or disloyalty.*"

29. It is the second category on which we are going to concentrate in this talk. Tipping J referred to this category as "what might be called a true breach of fiduciary duty" (at 687).

30. The remedies which we will discuss are:

(a) Rescission.

(b) Account of profits.

(c) Proprietary constructive trusts.

(d) Equitable compensation.

(e) Forfeiture of fees.

(f) Removal (i.e. injunction).

Election

31. With such a list of potential remedies, it is necessary to consider whether all or some of these remedies can be claimed at the same time.

32. Where there are inconsistent remedies a claimant must make an election. If the remedies sought are cumulative, then no issues arise and multiple remedies can be obtained. But that election need not be made at the outset of his claim.

33. The issue of when an election should be made was debated in *Tang Min Sit v Capacious Investments Ltd* [1996] 2 WLR 192, a case which originated in Hong Kong and proceeded to the United Kingdom Privy Council via the Court of Appeal in Hong Kong. A landowner had agreed to assign some properties to the plaintiff. But the landowner subsequently let the properties without the plaintiff's consent. The plaintiff sued the landowner's personal representatives. He obtained an order for both an account of profits and damages. He sought and initially received sums reflecting the landowner's profits. He then sought, in an assessment of damages, damages for loss of use and occupation, giving credit for sums already received. In other words, he tried to substitute a claim for the defendant's profits with a claim for his losses. He succeeded at first instance. However, the defendant was partly successful in his appeal to the Hong Kong Court of Appeal on the basis that the plaintiff had made an election. He could not seek damages for loss of use and occupation after already receiving monies representing the landowner's profits, though he was entitled to seek damages for diminution in value to the property. His appeal to the Privy Council succeeded because, whilst the remedies sought were inconsistent, and he should have been required to make an election when he obtained the original order, in fact he had obtained an order for both an account of profits and damages. In that context, the plaintiff's actions in pursuing the landowner's profits were not to be construed as making an election.

34. Giving the opinion (i.e. judgment) of the Privy Council board, Lord Nicholls said that a plaintiff was required to choose his remedy only at the time of the judgment. Sometimes it might be appropriate for a claimant to be afforded more time after judgment had been handed down. Examples given by the court of when more time might be appropriate were where the judgment in question was a default or summary judgment and a claimant had not had an opportunity to consider how much money a defendant has made from a wrongful act. In such a case a court could make an order for disclosure or further evidence, to assist a claimant in making a decision about which remedy to pursue.

Rescission

35. Turning firstly to rescission, a principal can rescind a transaction which was entered into by his fiduciary in breach of the self-dealing or fair-dealing rule. The transaction will be voidable, as

opposed to void. Rescission is not possible if the principal has, in full knowledge of the breach of duty, affirmed the transaction.

36. Both sides of the transaction must be undone.

Account of profits

37. A fiduciary is obliged to account for profits made in breach of fiduciary duty. It does not matter whether the principal would have consented to the steps which in fact led to that profit. That might be relevant when considering what loss, if any, the principal suffered. But it does not assist with what profits the fiduciary has wrongfully made in breach of fiduciary duty.

38. Taking an account may in practice be a procedural step. It is something which a principal is entitled to as of right as part of a fiduciary's duty towards him. There is no need to prove a breach of fiduciary duty first (*Libertarian Investments Ltd v Thomas Alexej Hall* [2013] HKCFA 93, (2013) 16 HKCFAR 681, [2014] 1 HCK 368 at para 167 per Lord Millett NPJ), though as a matter of its discretion the court may decline to order an account if there has been no breach. Therefore, in directing an account a court is not granting a remedy but enforcing the performance of an obligation.

39. Once an account has been taken, a claimant can falsify it or surcharge it. To falsify means to ask for an unauthorised disbursement to be disallowed from the account, which will produce a deficit which the fiduciary must then make good. A claimant will want to do this if the unauthorised disbursement has been loss making. But if the disbursement was profit making, rather than seeking restitution of the sum wrongfully paid out, he will seek to follow or trace the money.

40. To surcharge means to ask for the property to be treated as if the fiduciary had performed a duty properly so as to obtain a benefit for the principal when in fact that duty was not so performed. The fiduciary must then replenish the account accordingly.

41. It may in practice not be necessary to seek an account or inquiry. "The amount of any unauthor*ised disbursement is often established at trial, so that the plaintiff does not need an account but can ask for an award of the appropriate amount of compensation*" (*Libertarian Investments* at para 172 per Lord Millett NPJ).

Proprietary remedies

42. A fiduciary who receives a bribe or secret commission holds it with the beneficial ownership vested in the principal. The principal has the ability to follow or trace those sums but has to choose between personal and proprietary remedies.

Equitable compensation

43. A claimant may seek equitable compensation, which bears some similarities to a common law claim for damages. However, the common law rules requiring the loss to be foreseeable and not too remote do not apply. The court is entitled to assess compensation with the full benefit of hindsight (*Libertarian Investments* at para 90 per Ribeiro PJ). However, a form of causation does apply. If the loss would have occurred in any event, the claimant will not be able to make a recovery.

Forfeiture of fees

44. Where a fiduciary acts dishonestly or accepts secret profits from a third party which is directly related to performance of the duties in respect of which the fees were payable by the principal, those fees may be forfeited.

Removal (i.e. injunction)

45. It is possible to prevent a fiduciary from taking a certain step by seeking an injunction. There must be a reasonable apprehension of a potential conflict before an injunction will be granted.

Remedies for breach of fiduciary duty against third parties

46. The claimant may also able to seek recovery for loss against third parties. We am not here considering the situation where there may be a claim in tort against the wrongdoer, say in deceit where the third party may be jointly liable with the perpetrator. Rather we are concerned about when a third party becomes liable as an accessory to the breach of duty.

47. Just as when considering the liability of perpetrators, it is important to bear in mind the distinction which English law draws between proprietary or *in rem* remedies and personal remedies. If the breach of fiduciary duty consists of the misapplication of trust assets because the trustee has transferred trust property to a third party, the claimant may be able to recover the property directly from the third party. The claimant in that situation is relying on her equitable beneficial ownership of the property. An essential first question is, who has the relevant trust asset or money?

48. In this session, we are rather considering the personal liability of third parties for breach of fiduciary duties, where liability comes about in two principal situations:

    (a) Knowing receipt or inconsistent dealing with the trust property or its proceeds;

    (b) Dishonest assistance in a breach of trust or fiduciary duty.

49. When dealing with the knowing receipt category, especially in relation to banks which receive deposits of trust monies, a distinction has to be drawn between ministerial receipt (the situation where the bank receives money merely as agent for its customer) and receipt for its own benefit – see *The High Commissioner of Pakistan in the United Kingdom and The 8th Nizam of Hyderabad and others* [2016] EWHC 1465 (Ch) and *Marsfield Automotive INC v Siddique* [2017] EWHC 187 (Comm).

50. In the case of ministerial receipt, the liability is for inconsistent dealing with the equitable rights of the beneficiary in the trust property. The liability is to account to the claimant as if the third party was a constructive trustee – see *Uzinterimpex JSC v Standard Bank plc* [2008] EWCA Civ 819.

51. In the case of beneficial receipt, unless he is able to rely on the defence of a bona fide purchaser for value without notice (so-called "*Equity's darling*") the third party is liable in restitution to account for the benefit wrongly received i.e to restore its value to the claimant. The touchstone of liability is that the third party has received the trust property in circumstances where it is unconscionable for him to retain the benefit of the receipt – see *Sinclair Investments (UK) Ltd v Versailles Trade Finance group* [2011] EWCA Civ 347.

52. Liability for dishonest assistance depends on establishing that the third party has wrongly participated or lent assistance in a primary breach of trust on the part of the trustee. As this is

purely an accessory liability, if there is no primary breach then there is no liability for dishonest assistance. However, there is no need for the primary breach to involve dishonesty or fraud (*Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378) or a misapplication of property by the fiduciary (*Novoship (UK) Ltd v Mikhayluk* [2014] EWCA 908). What constitutes assistance is a question of fact but examples include a solicitor drafting an agreement used by others in an improper scheme (*Dubai Aluminium Co. Ltd. v Salaam* [2002] UKHL 48) and a party who carried out research, submitted invoices and collected cheques (*Madoff Securities International Ltd (In Liquidation) v Raven* [2013] EWHC 3147) and someone who made false representations intended to disguise the destination of funds (*Latchworth Ltd v Dryer* [2016] EWHC 3424).

53. The remedy for dishonest assistance is either that the third party accounts for the profits which he has received as a result of his dishonest assistance or that he be liable in equity to compensate the claimant for his losses.

54. We will now deal with the required state of mind in relation to recovering against third parties.

Required state of mind for recovery against third parties

Introduction

55. As discussed already, where there has been a breach of fiduciary duty, there are two main routes to personal recovery against third parties such as bankers, lawyers and agents. The first route is to bring a claim for dishonest assistance. The second is a claim for knowing receipt. As to the second, the English Court of Appeal have said that there is a single test, which is that the recipient's state of mind must have been such that it was unconscionable for him to retain the benefit of the property (*Bank of Credit and Commerce International (Overseas) Ltd v Akindele* [2001] Ch 437 per Nourse LJ, with whom Ward and Sedley LJJ agreed).

56. In the remainder of this talk, we are going to focus on the state of mind required for dishonest assistance, first by introducing the test itself and then looking at two recent applications of it.

Dishonest assistance

57. *Ivey v Genting Casinos (UK) Ltd t/a Crockfords* [2017] UKSC 67 was a case about cheating at cards. Each card in a pack will usually have the same design but that design will often not be symmetrical. As a result, it is possible to arrange cards so that specific cards can be identified as falling into a certain category (such as "high cards") even when face down, by rotating some of the cards by 180 degrees. This process is known as "edge sorting".

58. Mr Ivey and his associate Ms Sun took advantage of this asymmetry in a casino when playing Punto Banco. They did this by having Ms Sun pretend to be superstitious, and asking for the "good cards" to be turned, so a particular long edge would be visible when the cards were in the card shoe. This theoretically gave Mr Ivey an advantage of about 6.5% over the house, as opposed to a disadvantage of about 1%. After two days, Mr Ivey won nearly £8m. The casino did not want to pay, considering Mr Ivey to have cheated. It was agreed that it was an implied term of his contract with the casino that cheating was prohibited. Mr Ivey argued that the meaning of the word "cheating" included the concept of dishonesty. If that was right, he said, then he had to consider himself dishonest to be found dishonest because that

was part of the test in English criminal law. But given he had not considered what he had done to be cheating, but instead deploying a perfectly legitimate advantage, he could not be found dishonest, and therefore could not be found to have cheated.

59. Having won repeatedly in the casino, Mr Ivey lost repeatedly in the courts, at first instance, in the Court of Appeal, and in the Supreme Court. The judges found Mr Ivey had cheated and was therefore in breach of the implied term prohibiting cheating.

60. Though the Supreme Court did not agree with Mr Ivey that dishonesty was a necessary component of cheating, it took the opportunity to clarify the test for dishonesty in any event. It said that whilst a dishonest state of mind is a subjective matter, it is to be determined objectively. Whilst practitioners had always been fairly confident that this was the position in civil law, despite some earlier confusion, it had not previously been understood to have been the position in criminal law (*R v Ghosh* [1982] EWCA Crim). Instead, in criminal law, there had been thought to be a further requirement, that the defendant himself must have considered his conduct to have been dishonest. This had the perhaps surprising consequence that someone who was so flawed in character as to think honest conduct which others would realise was dishonest, would not be found guilty. The criminal law would fail to ensnare those whose attitudes differed most from the society in which they found themselves.

61. The Supreme Court endorsed the following passage as representing the test for dishonesty (taken from Lord Hoffmann's speech in *Barlow Clowes International Ltd v Eurotrust International Ltd* [2005] UKPC 37 at pages 1479-1480):

"Although a dishonest state of mind is a subjective mental state, the standard by which the law determines whether it is dishonest is objective. If by ordinary standards a defendant's mental state would be characterised as dishonest, it is irrelevant that the defendant judges by different standards."

62. At paragraph 74 of *Ivey*, Lord Hughes summarised the relevant steps, in applying the test of dishonesty, as follows:

"When dishonesty is in question the fact-finding tribunal must first ascertain (subjectively) the actual state of the individual's knowledge or belief as to the facts. The reasonableness or otherwise of his belief is a matter of evidence (often in practice determinative) going to whether he held the belief, but it is not an additional requirement that his belief must be reasonable; the question is whether it is genuinely held. When once his actual state of mind as to knowledge or belief as to facts is established, the question whether his conduct was honest or dishonest is to be determined by the fact-finder by applying the (objective) standards of ordinary decent people. There is no requirement that the defendant must appreciate that what he has done is, by those standards, dishonest."

63. That means that a defendant's assessment of their own conduct is not relevant to whether he has been dishonest.

64. So much for whether the defendant's own assessment is relevant.

65. But what about the meaning of dishonesty? It "*means simply not acting as an honest person would in the circumstances*". "*Honesty, indeed, does have a strong subjective element in that it is a description of a type of conduct assessed in the light of what a person actually knew at the time, as distinct from what a reasonable person would have known or appreciated.*

Further, honesty and its counterpart dishonesty are mostly concerned with advertent conduct, not inadvertent conduct. Carelessness is not dishonesty. Thus for the most part dishonesty is to be equated with conscious impropriety". "*In most situations there is little difficulty in identifying how an honest person would behave. Honest people do not intentionally deceive others to their detriment. Honest people do not knowingly take others' property. Unless there is a very good and compelling reason, an honest person does not participate in a transaction if he knows it involves a misapplication of trust assets to the detriment of the beneficiaries. Nor does an honest person in such a case deliberately close his eyes and ears, or deliberately not ask questions, lest he learn something he would rather not know, and then proceed regardless*." *Royal Brunei Airlines v Tan* [1995] 2 AC 378, per Lord Nicholls at page 389B-G.

66. Interestingly, recklessness is not *per se* dishonesty, but it may be evidence of dishonesty – *Clydesdale Bank PLC v Workman* [2016] PNLR 18. This contrasts with the fact that recklessness is sufficient for the tort of deceit.

67. Whilst carelessness and recklessness might not be enough, a clear suspicion of wrongdoing is. This may amount to turning a blind eye, which is not something an honest person would do.

68. A motive is not a necessary ingredient for a finding of dishonesty, but a court will require compelling evidence to conclude there has been dishonesty if there is no motive (*Mortgage Agency Services Number One Ltd v Cripps Harries LLP* [2016] EWHC 2483 (Ch) at [88]).

69. There is no need for the dishonest assistant to know of the existence of the trust or fiduciary relationship the breach of which she has assisted (*Royal Brunei Airlines v. Tan* [1995] 2 AC 378; *Barlow Clowes International v Eurotrust International Ltd* [2005] UKPC 37). It is enough for the assistant to know he or she is involved in a misappropriation of assets.

70. Although it is now easy to say with precision what is means to be dishonest, it still requires careful attention to say when someone will be held to be dishonestly assisting a breach of trust or fiduciary duty.

71. Take for example the recent case of *Group Seven v Nasir* [2017] EWHC 2466 (Ch), a decision of Morgan J that is currently on appeal. There, Group Seven had been tricked into lending £100m to a fraudster. That meant the loan agreement was void and as such the fraudster held the £100m on trust for Group Seven. The fraudster recruited a Mr Nobre and his company LARN to help launder the money. A classic means to launder money is to wash it through a solicitor's client account, so Mr Nobre approached a firm called Notable Services claiming to wish to use their services in connection with a property purchase. Thus he deposited the £100m into their client account.

72. However Mr Nobre was never going to purchase the property and instead directed the firm, and particularly one of the partners called Mr Landman, to pay out some of the money to various third parties. Using a client account in this way is prohibited under the Solicitors Accounts Rules in England, and Mr Landman knew it was. Some £15m was dissipated in this way. Luckily for the claimant the bank account was then frozen and they were able to get most of their money back. This is an example of the *proprietary* claim we discussed earlier – the claim to get the claimants' property returned. But what about the £15m that had been dissipated? There was no point going after Mr Nobre (by then in prison) or the principal fraudster, who had disappeared. So instead they targeted Notable and Mr Landman – a

personal claim (i.e. one requiring them to pay out of their own assets) for dishonestly assisting Mr Nobre.

73. Morgan J held that Mr Landman was dishonest. But what he did dishonestly was breach the Solicitors Accounts Rules. Mr Landman was held not to have sufficient knowledge that the money was not Mr Nobre's and accordingly the assistance he rendered was not dishonest. Morgan J said (at [470]-[471]):

"*…it is one thing to say that a wrongdoer is liable for the unforeseeable consequences of that wrongdoing and another to say that a wrongdoer who has committed one wrong is liable for the consequences of a different wrong, which he did not commit. The question for me is whether what [the defendant] dishonestly did was to assist a breach of trust when he did not have the relevant knowledge as to there being a breach of trust. I think that I would have to extend the basis of the liability for dishonest assistance of a breach of trust to hold him liable and I am not persuaded that such an extension is justified.*"

74. So in this case Mr Landman was both dishonest, and he assisted; but he did not dishonestly assist. The two must be connected for the claimant to succeed.

75. Contrast the position in the case of *UBS v KWL Kommunale Wasserwerke Leipzig GmbH* [2017] EWCA Civ 1567. In that case the merchant bank UBS had a corrupt arrangement with some financial advisers under which the financial advisers would advise their clients to enter into risky derivatives contracts with UBS regardless of whether it was in the interests of their clients to do so. Although UBS knew they were participating in this corrupt scheme, what they did not know was that the financial advisers (who owed fiduciary duties to their client KWL) were actually bribing directors of KWL (who also owed fiduciary duties to KWL) to enter into these agreements.

76. KWL entered into derivatives with UBS and lost millions of pounds on them. When UBS sued for the money due, KWL were permitted to rescind the agreements on the basis of UBS's dishonest assistance in the breach of fiduciary duty that procured KWL to enter into the contracts. (Interestingly this is a case where dishonest assistance was used as a defence to enable KWL to get out of contracts it had entered into rather than as a cause of action to recover misappropriated money).

77. The Court of Appeal held that it did not matter that UBS did not know about the bribes. They knew that they were participating in a dishonest scheme with the financial advisers, and that was enough, even if the scheme manifested itself in ways UBS did not realise.

78. The majority, Briggs and Hamblen LJJ held at [113]:

"*Where a party to an intended transaction deals with the other party's agent secretly and behind his back, and dishonestly assists that agent to abuse his fiduciary duties to the other party so as to bring that transaction about, then the first party's conscience may be affected not merely by the particular form of abuse by the agent of which it actually knew, but also by any other abuse which the agent chose to employ to bring about the transaction with the first party*"

79. This is not an uncontroversial stance. In a forceful dissenting judgment, Gloster LJ stated at [347]:

"*in order for the entitlement to rescind…to be workable, it must be confined to what that party knows, subject only to very limited qualification. In my view it is impracticable and*

unreal to introduce into commercial transactions the moral standards of the vicarage – or, put in legal terms, to impose on counter-parties the obligations of a trustee."

80. For the moment however, that represents the minority view. Synthesising these two authorities it seems to be the position that the dishonesty must be connected to the assistance in a breach of fiduciary duty before the third party will be liable; but once so connected it is not necessary for the third party to know every aspect of the breach of fiduciary duty to which it has become party.