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Speakers

Thomas Lowe KC
Tom has acted in numerous reported and high-profile cases and cross-border disputes before a large variety of tribunals in a number of different jurisdictions. Much of his work stems from collapses of complex investment structures and from high-value cross-border private client disputes. He has developed a substantial offshore practice and is one of very few barristers who have had full and not merely ad hoc practising certificates in both the BVI and the Cayman Islands. The Legal 500 2024 describes Tom has "*an incredibly gifted advocate with unparalleled experience of Cayman Islands insolvency, company law and commercial disputes*". Chambers & Partners 2024 says Tom is *"extremely good on his feet*".

Fenner Moeran KC
Fenner has a broad-based chancery/commercial practice, which spans trusts, civil fraud and asset recovery work. With regard to asset recovery cases, Fenner has extensive experience of obtaining and defending freezing, search, disclosure (including third party disclosure) and gagging orders. His clients range from international financial institutions, to regulatory bodies to individual financial traders and customers. The Legal 500 2024 says "*Fenner is excellent all round. He is superb on the technical detail, but also a first-rate advocate and brilliant with clients*". Chambers & Partners 2024 says that Fenner's "*deep knowledge of the law, combined with his meticulous analysis, sets him apart".*

Tim Penny KC
Tim was awarded '**Chancery Silk of the Year**' at the Chambers & Partners UK Bar Awards 2023. He is a specialist in high-value multi-jurisdictional commercial litigation, WFOs, Search Orders, commercial fraud and asset tracing, shareholder disputes, court-appointed receiverships, banking and financial services related claims, commercial arbitration, breach of confidence, 'soft' intellectual property and more recently cryptocurrency disputes. Tim is called to the Bar in the BVI, and regularly litigates not only in the London Commercial Court and the BVI but also in Cayman and other offshore jurisdictions. Tim is ranked in the directories in both commercial chancery and civil fraud. Chambers & Partners 2024 describes Tim as "*a charming advocate who captivates even when dealing with difficult points*". The Legal 500 2024 praises Tim as "*thorough in his approach, covering cases from all angles*".

James Bailey KC
James has developed a successful practice focused on commercial chancery, civil fraud, international arbitration, insolvency and company matters. James is said to be "*absolutely outstanding, his advocacy in particular and the way he deals with issues on his feet*" (Chambers & Partners 2024). James's work has a significant international dimension including cases relating to the Cayman Islands, the Bahamas, the B.V.I., the U.S., Switzerland, Slovenia, North Macedonia, Italy, South Korea, Hong Kong and Japan. He has also been instructed as an expert on matters of English law in courts abroad. He is often involved in obtaining worldwide freezing order and passport orders. The Legal 500 2024 describes James as "*an outstanding advocate who has the ear of the bench from the moment he steps into the courtroom, and he is tactically brilliant*".

Graeme Halkerston
Graeme is a specialist in offshore litigation and is ranked in Tier 1 by both Legal 500 and Chambers & Partners for offshore law. Offshore vehicles, offshore litigation and onshore cases involving offshore legal issues are his bread and butter. Many of his matters involve parallel onshore and offshore litigation, particularly disputes pending in Cayman or the BVI and the United States. He also has a substantial expert evidence practice on issues of Cayman or BVI law pending in the US courts. Prior to joining Chambers, Graeme was litigation partner in one of the leading offshore firms. Chambers & Partners 2024 praises Graeme for his "*fantastic ability to unpick and understand everything very fast*" and for his "*encyclopaedic knowledge of all the latest updates*". The directory also describes Graeme as a "*technically brilliant, responsive, and a fearless advocate*".

Tara Taylor
Tara has developed a broad commercial chancery practice, with a particular focus on general commercial disputes including civil fraud, insolvency, shareholder disputes and offshore work. She is frequently instructed in high-value commercial matters with significant offshore and multi-jurisdictional dimensions, as well as those involving complex trust structures, claims for breach of fiduciary duty and breach of trust. Tara has previously spent time on secondment in the dispute resolution team at a leading international law firm in the Cayman Islands, where she worked on a number of commercial, company and insolvency related matters. The Legal 500 praises Tara for being *"able to succinctly outline complex legal questions for the court"*.

Daniel Petrides
Described as "*a real star in the making*" (Chambers & Partners, 2024), and already ranked as a leading junior in The Legal 500, Daniel has a thriving commercial chancery practice spanning property, commercial, insolvency and trusts disputes. He frequently appears as sole counsel in both the High Court and the County Court, as well as retaining a focus on drafting and advisory work. Many of his cases have an international dimension and he has experience of ADR procedures, including arbitration. He is equally comfortable acting alone or as part of a larger team. Daniel is described in the directories as being "*very clever and hardworking*" (Legal 500, 2024), "*able to pick up esoteric areas of law very quickly*" and "*happy to get stuck in and assist wherever a job needs to be done*." (Legal 500, 2023). He has also been praised as a "*confident advocate*" (Chambers and Partners 2024) and "*a strong advocate despite his recent call*" (Legal 500, 2024).

James Man
James has developed a broad civil practice and accepts instructions across a wide range of business law and private client cases. He is ranked as a leading junior in both Chambers & Partners and The Legal 500, where he is described as "*outstanding*", "*commercially minded*", and an "*effective and versatile advocate*". A past edition of Chambers & Partners cited him as "*one of the most user-friendly junior counsel*". James has appeared as an advocate (either in his own right and as a led junior), including in the Hong Kong Court of Appeal and the Hong Kong Court of Final Appeal. Chambers & Partners Asia Pacific 2024 says James "*has a real skill in drawing together many different layers of fact and legal information to present the best arguments for clients*".

The BHS litigation and the Carillion discontinuance: Directors' duties in the spotlight

James Man

1. The collapses of the UK retailer British Home Stores (**“BHS”**) in 2016, and the construction giant Carillion Group (**“Carillion”**) in 2018, remain two of the most high-profile corporate insolvencies in recent times.

2. In the BHS trial, the joint liquidators claimed against two former directors (Mr Henningson and Mr Chandler) for wrongful trading and misfeasance under the Insolvency Act 1986 (**“IA 1986”**). On 15 May 2024, Leech J circulated a 533-page judgment, ruling in favour of the joint liquidators: [2024] EWHC 1417 (Ch). The two directors were ordered to each contribute on a several basis £6.5 million to the companies’ asset for the wrongful trading claim, and to pay various sums for the misfeasance claims: see [1154]-[1157]. This makes it one of the largest successful claims of its kind to date.

3. In the Carillion litigation, the non-executive directors (**“NEDs”**) secured a much better result. The Insolvency Service, acting on behalf of the Secretary of State for Business and Trade, brought disqualification proceedings in January 2021 against five NEDs of Carillion. The Insolvency Service sought to disqualify the five NEDs on a strict liability basis that they did not know the true financial position of Carillion at all material times, regardless of whether they had discharged their duty of care. The trial was scheduled to start on 16 October 2013 for 13 weeks. On the eve of trial, the IS discontinued the proceedings against the NEDs.

4. What legal/practical lessons can practitioners learn from the two cases? We address five key aspects in this paper:

   (i) The “Notional Director” standard – what does it really mean?

   (ii) Delegation to fellow directors or employees – is that a complete defence?

   (iii) Reliance on professional advice – how “safe” are the directors?

   (iv) Causation – counter-factual and points to note

   (v) Strict liability on NEDs? A welcomed discontinuance in Carillion

BHS – the basic facts

5. British Home Stores was a household name in the United Kingdom. Until 11 March 2015, the BHS Group was under the ownership of the Taveta group of companies. From 2009 onwards, it started to incur losses.

6. On 11 March 2015, the ownership of the BHS Group was transferred to Retail Acquisitions Ltd at a consideration of £1. Mr Chappell, Mr Henningson and Mr Chandler were appointed to be directors of the companies within the BHS Group.

7. After their appointments, the directors caused the group companies to enter into a series of transactions including new financial arrangements, which however resulted in further increase in net deficiency in the assets of the group companies. Despite the efforts to rescue the BHS Group, the group companies filed for administration in April 2016, and joint liquidators were appointed.

8. In December 2020, the joint liquidators commenced proceedings against Mr Chappell, Mr Henningson and Mr Chandler for wrongful trading and misfeasance under ss.214 and 212 of the IA 1986 respectively. The case against Mr Henningson and Mr Chandler culminated in a 5-week trial in late 2023, with judgment circulated on 15 May 2024. The case against Mr Chappel was, for special reasons, severed and adjourned after the trial.

9. There are no wrongful/insolvent trading provisions in the Cayman Islands, but directors owe a common law fiduciary duty to the company to act in its best interests, and they must have regard to the interests of creditor when they knew or ought to have known that the insolvency was imminent or that insolvent liquidation was probable: BHS at [539]-[543]. Further, "insolvency-deepening activity" can amount to a breach of duty by directors even though insolvent liquidation is not inevitable: BHS at [546]. As such the analysis of the statutory wrongful trading claim in BHS would remain relevant in Cayman.

The "Notional Director" standard – what does it really mean?

10. The statutory wrongful trading claim under s.214 of IA 1986 requires the plaintiff to prove that at some time before the commencement of the winding up of the company, the director knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation: s.214(2)(b).

11. In that regard, s.214(4) states the facts which a director ought to know or ascertain or the conclusions which he ought to have reached would be those known or ascertained by a reasonably diligent person having both:

    (i) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company; and

(ii) the general knowledge, skill and experience that that director has.

12. This sort of "hybrid" standard is, at first sight, confusing. Leech J provided some clarity to that in BHS at [479]:

(i) If the general knowledge, skill and experience of the director in question is higher than that of the reasonably diligent director carrying out the same functions, then he should be held to the higher standard.

(ii) However, if the general knowledge, skill and experience of the director in question is lower than that of the reasonably diligent director carrying out the same functions, then it is no defence that he did not have that knowledge, skill or experience.

13. The clarification is useful, as one reading of s.214(4) suggests that there is a significant subjective element which turns on the knowledge, skill and experience of the individual director. It is now clear that the contrary is true. The objective standard is the bare minimum standard; and if the individual director possesses a higher knowledge, skill and experience, the standard is elevated.

14. Leech J also usefully set out some general propositions on the application of the "Notional Director" test in [466] of his judgment:

(i) The "Notional Director" test is to be applied to each individual director, and not to the board of directors as a whole.

(ii) The court's enquiry into the functions performed by each director will go beyond the mere consideration of his title and will "examine the substance of what they actually do or did".

(iii) The standard to be expected of the Notional Director will also depend on the size and sophistication of the company.

(iv) In determining what a director ought to have known, the court is not limited to consideration of the material available to the director during the relevant period, but its consideration may extend to material to which the director could with reasonable diligence have access.

(v) A director is expected to obtain sufficient financial information to monitor the company's solvency.

(vi) A director is not liable simply for permitting a company to continue to trade at a time when they know that the company is insolvent either on the balance sheet test or the cashflow test. He may properly take the view that it is in the interests

of the company and of its creditors that, although insolvent, the company should continue to trade out of its difficulties. The critical question, therefore, is whether there was "*light at the end of the tunnel*".

(vii) The decision to put a company into liquidation is a difficult one and the court should be slow to encourage directors to put a company into liquidation or administration at the first sign of trouble. For this reason (if no other), the court should be very careful to avoid hindsight in scrutinising directors' decisions.

(viii) Nevertheless, if the directors appreciate that the company is insolvent but reach the conclusion that they can trade out of insolvency, there must be a rational basis for that conclusion.

(ix) Likewise, there must be something more than blind optimism or micawberism (meaning the unfounded and naïve belief that something will turn up in the future to conquer financial adversity) for a director to justify the company continuing to trade whilst insolvent.

15. The key takeaways from these propositions are as follows:

(i) Reasonableness is key: The court expects a director to act reasonably. Significantly, this is not limited to what were in fact available; the director is expected to use reasonable means to obtain information (and seek advice) in the discharge of his functions.

(ii) Substance over form: Title of the individual director in question does not matter; the court would examine what he actually did in the discharge of his functions.

(iii) No hindsight, but things have to be done with proper reasons: The court would avoid hindsight in scrutinising directors' decisions, but there must be a rational basis for any decision made.

<u>Delegation to fellow directors or employees – is that a complete defence?</u>

16. The law on delegation was set out by Leech J in <u>BHS</u> at [480]-[481]:

(i) The duties and responsibilities of a company director are personal and cannot be delegated. However, management functions may be delegated to other directors or company employees. There is a difference between proper delegation and division of responsibility, on one side, and total abrogation on the other.

(ii) Where directors delegate management functions to other directors or employees, it remains their duty to monitor and supervise the discharge of those functions.

(iii) The balance between the personal duties of a director and the reliance on other directors or employees was expounded in Madoff Securities International Ltd (in liquidation) v Raven [2014] Lloyd's Rep FC 95:

(a) It is legitimate, and often necessary, for there to be division and delegation of responsibility for particular aspects of the management of a company. Nevertheless each individual director owes inescapable personal responsibilities. He owes duties to the company to inform himself of the company's affairs and join with his fellow directors in supervising them. It is therefore a breach of duty for a director to allow himself to be dominated, bamboozled or manipulated by a dominant fellow director where such involves a total abrogation of this responsibility.

(b) In fulfilling this personal fiduciary responsibility, a director is entitled to rely upon the judgment, information and advice of a fellow director whose integrity skill and competence he has no reason to suspect. Moreover, corporate management often requires the exercise of judgement on which opinions may legitimately differ, and requires some give and take. A board of directors may reach a decision as to the commercial wisdom of a particular transaction by a majority. A minority director is not thereby in breach of his duty, or obliged to resign and to refuse to be party to the implementation of the decision. Part of his duty as a director acting in the interests of the company is to listen to the views of his fellow directors and to take account of them. He may legitimately defer to those views where he is persuaded that his fellow directors' views are advanced in what they perceive to be the best interests of the company, even if he is not himself persuaded. A director is not in breach of his core duty to act in what he considers in good faith to be the interests of a company merely because if left to himself he would do things differently.

(c) Where a director fails to address his mind to the question whether a transaction is in the interests of the company, he is not thereby, and without more, liable for the consequences of the transaction. In such circumstances the court will ask whether an honest and intelligent man in the position of a director of the company concerned could, in the whole of the existing circumstances, have reasonably believed that the transaction was for the benefit of the company.

17. In BHS, one of the directors submitted that his functions were limited to introducing financial contacts and dealing with the international side of the business. Leech J, however, found that it was not open for him to leave to his fellow directors those decisions which were required to be made collectively by the relevant company board: [482].

18. The upshot:

(i) Delegation is <u>not</u> a complete defence. There is always an overarching monitoring and supervisory duty.

(ii) But while there cannot be a total abrogation of duties, deferring to fellow directors and employees and relying on their judgment and views are legitimate.

(iii) In short, a balance has to be struck. A director, having delegated his management functions to others, still has to be involved in some sense so as to avoid total abrogation (or perception of total abrogation). If that is done, he may safely rely on his fellows.

<u>Reliance on professional advice – how "safe" are the directors?</u>

19. In <u>BHS</u>, Leech J accepted as a general proposition that if directors commissioned and relied on professional advice in the context of their decision-making, they will *prima facie* have fulfilled their duties: [483].

20. The weight the court will attach to the professional advice will depend on various factors. These include the scope of the engagement, the instructions the adviser was given, the knowledge the adviser had or the assumptions they were asked to make, the advice they gave (or did not give), and the extent to which the directors relied on that advice (or not). If the substance of a director's defence is that the professional adviser did not advise the board to put the company into administration or liquidation, the weight to be attributed to the absence of that advice will depend on a detailed assessment of the facts. See [485].

21. Applying these principles on the facts in <u>BHS</u>, Leech J held that:

(i) The directors had failed to adequately consider the external legal advice they had received prior to approving a loan facility, which had raised various points for consideration by the directors. The advice was in fact never tabled or discussed at a board meeting before the decision was taken: [906].

(ii) Had the directors properly considered that advice, they would have concluded (based on a proper consideration of the issues raised in that advice) that there was no reasonable prospect of the company avoiding insolvent liquidation or administration: [907].

(iii) Separately, Grant Thornton had been responsible for producing weekly cashflow updates in connection with the BHS Group's turnaround plan. Leech J held that a reasonably diligent director would fully have understood that the assumptions underpinning those cashflow updates (and the turnaround plan more generally) were unreasonable: [910].

(iv) It was irrelevant that the advice did not say whether the companies had a reasonable prospect of avoiding insolvent liquidation or administration. This was not something which the advisers could or should have been expected to express an opinion. Rather, this was a question of individual judgment for the directors and the advisers could not have been expected to do more than identify the legal issues for the directors to consider: [912].

22. The lessons learned:

(i) It is not completely safe for directors to say they had relied on external professional advice.

(ii) BHS provide a good example, where the court said a reasonably diligent director should have noticed that the factual assumptions underpinning the external advice were unreasonable. In those circumstances, the commissioning and reliance on the advice by the directors would not fulfil their duties.

(iii) Further, the *absence* of a specific advice has to be distinguished with a specific opinion advising the directors *not* to take a certain course of action. The court would attach more weight to the latter (again, depending on all the circumstances).

(iv) The court also took a strict view as to what an external adviser could and could not advise. Matters which fell within the individual judgment for the directors, such as whether the companies had a reasonable prospect of avoiding insolvent liquidation or administration, were regarded as something on which the external adviser could not be expected to express an opinion. The court appeared to have drawn a distinction between primary opinion on legal and financial matters, and the inferential conclusion that should be drawn from those matters by the directors.

Causation – counter-factual and points to note

23. On the question of causation, Leech J held at [1108]-[1109] that:

(i) The appropriate counter-factual is to consider what would have happened if the directors had complied with their duties.

(ii) As to other directors which were not the subject of the proceedings, the court is not required to assume they would have complied with their duties. The appropriate course is to decide as a matter of fact on a balance of probabilities how other directors would have acted if the directions in question had complied with their duties.

24. At [1110], Leech J adopted a step-by-step analysis in considering what would have actually happened had Mr Henningson and Mr Chandler complied with their duties. He considered that they would have persuaded their fellow directors to vote in favour of an immediate resolution to put the companies into administration (and Mr Chappel would have accepted the "inevitable"). The court also had regard to the witness's evidence in answering the counter-factual and deciding what would have happened, even though that was not evidence of primary fact.

25. Points to note:

    (i) Issues of causation involve a careful construct and analysis of each possible counter-factual had there been no breach. They are often neglected in witness statements, as they are not primary facts.

    (ii) But it is now clear that in determining the appropriate counter-factual, the court would have regard to what the witness would say about what would have happened. For practitioners acting for the directors, it would be sensible to address the causation issues in written statements, exploring each possible counter-factual insofar as practicable.

<u>Carillion - the basic facts</u>

26. The Carillion Group operated a leading construction, project finance and support services business in the UK and across a number of other jurisdictions. It had over 350 subsidiaries, with Carillion PLC as their listed parent.

27. In July 2017, Carillion plc issued a profit warning, causing its share price to plummet. Shortly afterwards in January 2018, the Carillion Group went into compulsory liquidation.

28. The circumstances of Carillion's collapse and its consequences were investigated by the Financial Conduct Authority, the Financial Reporting Council, the National Audit Office and the Official Receiver. The regulatory authorities concluded that Carillion PLC had published misleading information about its financial performance between July 2015 and July 2017.

29. In January 2021, the Insolvency Service brought disqualification proceedings against five NEDs of Carillion pursuant to the Company Directors Disqualification Act 1986 (**"CDDA"**).

Strict liability on NEDs? A welcomed discontinuance

30. The key allegation against the NEDs – described to be novel by the Insolvency Service themselves – is that they failed to know Carillion's true financial position, and they breached their duty "*per se*", viz. on a strict liability basis. The Insolvency Service did not allege any breach of the duty to exercise reasonable skill, care and diligence under s.174 of the Companies Act 2006: see [2022] EWHC 922 (Ch), at [5] and [27].

31. The Insolvency Service argued that, by reason of the breach of the strict duty, the NEDs were – without more – unfit to be involved in the management of any company pursuant to s.6 of the CDDA.

32. It was also at one stage alleged this "failure to know" meant that the NEDs ought to be held responsible for the unfit conduct of the executive directors and disqualified on that basis: see [5]. But that allegation was later not pursued.

33. The implication of this alleged breach of strict duty, if successful at trial, would be very far-reaching:

    (i) At common law directors owe a series of fiduciary duties as well as duty of care to the company (codified in England and Wales), which depend on the *bona fides* of the directors and what a reasonably diligent director would be expected to act.

    (ii) While the duties imposed by the law on executive directors and NEDs are the same, NEDs are expected to carry out a supervisory role and participate in decisions of the board on broad strategy. They are not expected to have day-to-day management of the business. The common law duty of care requires a director to do what would have been done by a reasonably diligent director having the skill, knowledge and experience carrying out the same functions as are carried out by that director in relation to the company. Thus, the substance of the NEDs' duty is different in that sense.

    (iii) The alleged strict duty, therefore, does not align with the general law. It is incompatible with the concept of non-executive directorship, and practically impossible to be complied with.

    (iv) Were the onerous duty be imposed, it would virtually eradicate the role of NEDs in corporate governance. It is doubtful if anyone would be willing to undertake the NED role if he is expected to know on a strict basis what an executive director should know about the true financial position of the company.

34. The discontinuance of the disqualification proceedings by the Insolvency Service is a sigh of relief for the NEDs. From a Cayman perspective, a lot of companies incorporated in Cayman are listed in other jurisdictions where the NEDs or INEDS would have never expected themselves to be subject the alleged onerous duty. For example, the regulatory regime in Hong Kong in which a lot of Cayman companies are listed does not impose such duty. A negative outcome in the Carillion would have meant that the NEDs need to manage their role as if they have a full-time post of executive directors, and the ramification of that can be extreme on corporate governance.

Concluding notes: the practical considerations for directors

35. Legal advisors should always advise their corporate clients to convene proper board meetings, prepare proper board minutes and adequately obtain and consider professional advice where necessary.

36. Corporate minute-taking is fundamentally important, and a set of adequate board minutes can significantly reduce the risk of liability of directors' negligence. The minutes should, insofar as possible, document: (1) the reasons and rationale underpinning the particular proposed board resolution; (2) the information provided to the board attendees; (3) the questions asked by the directors and any response to those questions. In practice, board minutes are rarely *verbatim* records of what was said or discussed at the board meeting, and that could be disadvantageous to the directors when litigation arises.

37. NEDs should be visibly diligent in discharging their monitoring and supervisory role. In reality, we have seen NEDs not participating or not actively participating in board meetings, and that can be detrimental when allegations are made against NEDs.

38. When a company is experiencing financial difficulties, extra caution is needed as the duty to creditors may come in. The board's understanding of the company's financial situation will be assessed on both a subjective and objective basis, based on what the director knew or ought to have known. It would be prudent to seek external advice – even though (as illustrated in BHS) that does not provide a complete safety net.

Developments in Tracing

James Bailey KC and Daniel Petrides

Introduction

1. Sophisticated (and even unsophisticated) fraudsters invariably seek to dissipate their ill-gotten gains. Accordingly, the ability of the law to locate the value which they have misappropriated is frequently fundamental to the practical success or failure of a claim in fraud.

2. In *Foskett v McKeown* [2001] 1 A.C. 102 at 127–128 Lord Millett provided the canonical exposition of tracing's role in the law of asset recovery:

   > "*Tracing is…neither a claim nor a remedy. It is merely the process by which a claimant demonstrates what has happened to his property, identifies its proceeds and the persons who have handled or received them, and justifies his claim that the proceeds can properly be regarded as representing his property. Tracing is also distinct from claiming. It identifies the traceable proceeds of the claimant's property. It enables the claimant to substitute the traceable proceeds for the original asset as the subject matter of his claim. But it does not affect or establish his claim. The successful completion of a tracing exercise may be preliminary to a personal claim (as in* El Ajou v Dollar Land Holdings plc *[1993] 3 All ER 717) or a proprietary one, to the enforcement of a legal right (as in* Trustees of the Property of F C Jones & Sons v Jones *[1997] Ch 159) or an equitable one.*"

3. It is important to note that following and tracing are technically distinct processes: following involves following a particular asset from hand to hand (e.g. a painting as it is sold and re-sold), while tracing involves identifying the substitutes for the original property in the hands of the same party (e.g. a claimant could trace into a car which a thief acquired using the proceeds from the sale of the painting). So, while it is common to speak of tracing 'into' an asset this is, strictly speaking, inaccurate; as Lord Millett explained in *Foskett*, it is really the value of the asset which is traced.

4. The first step in any tracing claim is, of course, for the claimant to show that they originally had title to the property in question. Next, it is necessary that the original property – or its substitutes – remain clearly identifiable/can be identified across a connected series of unbroken transactions. Finally, it is necessary for the claimant to show that their interest in the property has survived that process of transmissions (e.g. the transferee is not equity's darling).

5. Although the basic principles are well-settled, in the face of increasingly complex global financial systems and sophisticated fraudsters, tracing remains a lively area in both academic debate and caselaw. This paper, and the associated talk, will consider three

recent cases illustrative of the law's attempts to navigate a path for this ancient process through novel fact-patterns.

***Lapome Ltd v Kemp* [2023] EWHC 1564 (Ch)**

6. Unsurprisingly, misappropriated trust funds are rarely kept neatly segregated from other assets; instead, a wrongdoing defendant will frequently mix the trust funds with his own money, or that of other innocent third parties.

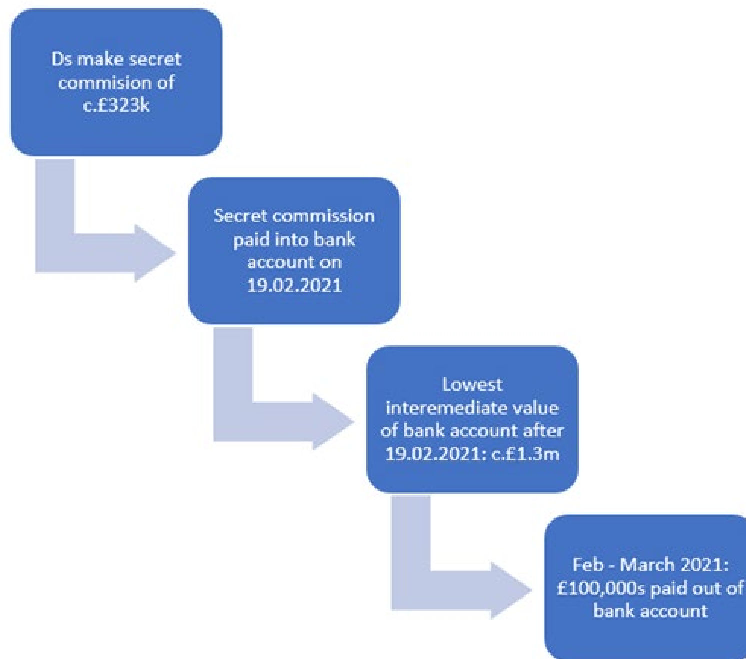
7. The process of tracing through mixed funds is subject to a number of rules, two of which are relevant for present purposes:

   a. Where trust funds are mixed in a trustee's personal account, any expenditure is presumed to deplete the trustee's own funds before those of the beneficiary: *Re Hallett's Estate* (1880) 13 Ch D 696. However, this is subject to the 'lowest intermediate balance rule', whereby if the balance of the account falls below the sum to which the beneficiary is entitled, equity limits a beneficiary's claim to the lowest balance which the account reached between the date of the wrongful deposit and the date of the claim: see *Roscoe v Winder* [1915] 1 Ch 62.

   b. Where mixed funds are used to purchase an asset and the remainder of the mixture is dissipated, the wrongdoer is deemed to have used the trust funds to purchase the asset so that the claimant is able to trace into it: *Re Oatway* [1903] 2 Ch 356.

8. In *Lapome Ltd v Kemp*, the question arose of whether a claimant is entitled to 'cherry pick' between these two rules so as to trace into assets acquired by the mixed fund despite the lowest intermediate balance remaining higher than the value of the claim. If possible, this may be a particularly potent remedy for a claimant if an asset acquired by the wrongdoer has since appreciated in value, as a claimant with a proprietary claim would be entitled to the benefit of any increase in the value of the trust property.

9. The facts, as illustrated below, arose in circumstances where the lowest intermediate balance of the bank accounts into which a secret commission had been paid (which were treated as a single account for the purpose of the defendants' summary judgment application) had always been considerably higher than the secret commission said to have been received, but the defendants had also paid significant sums out of those accounts which, it was inferred, had been used to acquire assets of appreciating value. The claimants, unsurprisingly, sought to trace into these assets.



10. The defendants argued that, following the decision of Patten J in *Turner v Jacob* [2006] EWHC 1317 (Ch), the claimant was not entitled to 'cherry pick' in this way.

11. The Master declined to grant summary judgment on this basis. In particular, he noted that Patten J had not been taken to *obiter dicta* of Lord Millett in *Foskett v McKeown* [2001] 1 AC 102 at 132 and Rimer J in *Shalson v Russo* [2005] Ch 281 at [144] suggesting that a beneficiary is entitled to trace through whichever part of the mixture he chooses: as Rimer J put it, "*if the beneficiary is not entitled to do this, the wrongdoing trustee may be left with all of the cherries...*". He further noted that a lively academic debate exists, with the majority of commentators preferring the approach in *Shalson v Russo* (although the textbook on which he was himself an editor, *Lewin on Trusts*, adopts a more sceptical view). In those circumstances, it was not appropriate to summarily determine the claim while the law remained in flux.

12. The debate is therefore one which will have to be determined by a future court. This may involve a court grappling with the following issues.

13. First, it may involve a fundamental reconsideration of the basis of the rules in *Re Hallett* and *Re Oatway.* Consistently with the view that tracing is itself an evidential process, rather than a substantive remedy, these have generally been explained as rules of evidence whereby any evidential doubt is resolved against the wrongdoer. But the types of evidential presumption which it is desirable to draw must depend to some extent on the injustice being addressed. If the concern is simply to reverse the beneficiary's primary loss, there may be little injustice in confining the beneficiary to the rule in *Re Hallett* in circumstances where there is sufficient money for this to provide an adequate remedy. If, on the other hand, the intention is to protect the integrity of the fiduciary relationship, or to vindicate the property rights of the beneficiary, it is perhaps easier to see why the

wrongdoer should not get the benefit of any profit made from a mixture in which misappropriated trust funds formed an inherent part.

14. Secondly, the question arises of where the limits of the presumptions lie.

    a. In *Re Hallett* itself it was held that evidence that the errant fiduciary intended to spend trust money first would disapply the presumption. But what sort of evidence might suffice? For example, would it be sufficient to show that the trustee would not have spent the sum in question without the cushion of the misappropriated trust funds in his account? This type of approach derives some support from the caselaw on backwards tracing (discussed below).

    b. What role does temporality play? In *Lapome* itself at [34] the Master suggested that the true ratio of *Turner v Jacob* may be that the claimant is not entitled to trace into property other than that first acquired from the mixed fund after the date of the wrongdoing.

    c. In *In Re Tilley's Will Trusts* [1967] Ch 1179 it was suggested that a beneficiary may be entitled to elect to trace into a rateable proportion of property acquired from a mixed fund, thereby entitling them to the benefit of a proportionate part of any increase in value.

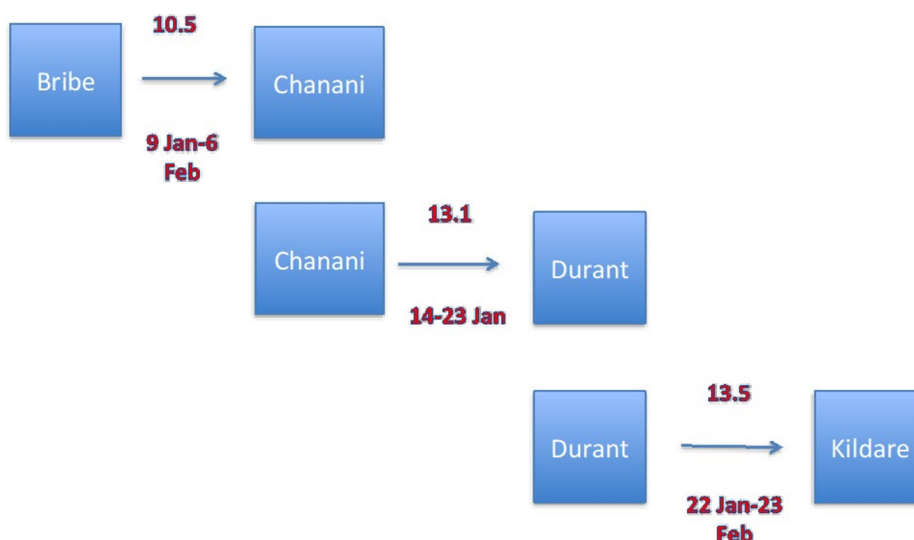
    d. Do different rules apply in the context of mixtures of physical goods? (see e.g. *Lupton v White* (1808) 33 ER 817).

15. Thirdly, whilst the defendants in *Lapome* were errant fiduciaries, should cherry-picking be permissible against innocent recipients, such as those in *Re Diplock* [1948] Ch 524?

Federal Republic of Brazil v Durant [2016] AC 297 and backwards tracing

16. Although long regarded as heretical, the existence of backwards tracing was explicitly recognised for the first time by the Privy Council in *The Federal Republic of Brazil v Durant International Corporation* [2015] UKPC 35.

17. The case concerned the misappropriation of funds by the former mayor of Sao Paulo in connection with a major public infrastructure project which had been passed through a series of overdrawn bank accounts. The links in the chain were as follows, with a large part of the bribe being paid into the Chanani account *after* the payments out of the Chanani account had been paid to Durant:



18. In permitting the claimant to trace into the hands of the defendant company, Kildare, Lord Toulson at [38] held that (emphasis added)

> *"The development of increasingly sophisticated and elaborate methods of money laundering, often involving a web of credits and debits between intermediaries, makes it particularly important that a court should not allow a camouflage of interconnected transactions to obscure its vision of their true overall purpose and effect. <u>If the court is satisfied that the various steps are part of a co-ordinated scheme, it should not matter that, either as a deliberate part of the choreography or possibly because of the incidents of the banking system</u>, a debit appears in the bank account of an intermediary before a reciprocal credit entry… <u>the availability of equitable remedies ought to depend on the substance of the transaction in question and not on the strict order in which associated events occur</u>…"*

19. Lord Toulson continued at [40] that in order to trace backwards, a claimant "*has to establish a co-ordination between the depletion of the trust fund and the acquisition of the asset which is the subject of the tracing claim, looking at the whole transaction, such as to warrant the court attributing the value of the interest acquired to the misuse of the trust fund.*"

20. In *Durant* itself, the Privy Council warned of the need to exercise caution in extending the scope of proprietary rights which could prejudice unsecured creditors. The courts have generally heeded this warning, by carefully circumscribing the circumstances in which backwards tracing will be permitted. In *SFO v Hotel Portfolio II UK Ltd* [2021] EWHC 1273 (Comm), Foxton J held that the present state of English law was that backwards tracing

was only permitted in certain very narrow and exceptional circumstances, and that those exceptions included:

> "*i) cases where the payment of money through the banking network for the purpose of effecting a payment from A to B involves credits occurring before debits;*
> *ii) cases in which the debit of trust property and the credit to be traced into were effected as part of a single transaction intended to achieve that outcome through a series of co-ordinated elements, whatever the chronological ordering of those elements…;*
> *iii) cases of anticipatory substitution…where an asset is acquired on the basis of an undertaking that the trust property will be exchanged for it (as, in due course, it is); and*
> *iv) conventional bilateral exchange transactions where the respective transfers are not simultaneous (e.g. Professor Smith's example of the car sale where the price is payable after property in the car passes).*" ([46])

21. In practice, the greatest hurdle that most backward tracing claims will face is demonstrating a sufficient connection between the transactions. In simple cases it may be easy to draw the inference that they were connected: e.g. *Relfo v Varsani* which concerned just two payments of almost identical amounts on the same date. In a more complex case, recourse might be had to the 'maelstrom' approach first recognised by the English Court of Appeal in *Sinclair Investments (UK) Limited v Versailles Trade Finance Limited* [2011] EWCA Civ 347. This operates where money has been paid into a mixed account from/into which a 'maelstrom' of 'cross-firing' transactions are made to obscure the true source of any of the money in the account and therefore render tracing through it practically impossible.

22. The scope of this principle was a subject of the long-running *AHAB* litigation in the Cayman Islands. At first instance it was held that in order for the principle to apply, the purpose of the maelstrom must have been to prevent tracing – as such, on the facts of that case where the maelstrom had been for the purpose of defrauding certain financial institutions by allowing for the provision of false accounts, it was refused. The Cayman Islands Court of Appeal held that this was too restrictive:

> *"In our judgment, the intention to assist in the commission of the frauds on the banks and the effect of making tracing impossible are two sides of the same coin. It would be wrong to disallow tracing of the proceeds of fraud simply because the fraudster has created a maelstrom and effected cross-firing to assist in his fraud which has the inevitable effect of subsequently defeating attempts to trace. It will, in any event, be impossible in many cases to determine the exact intention behind the fraudster's creation of a maelstrom and cross-firing."* ([914])

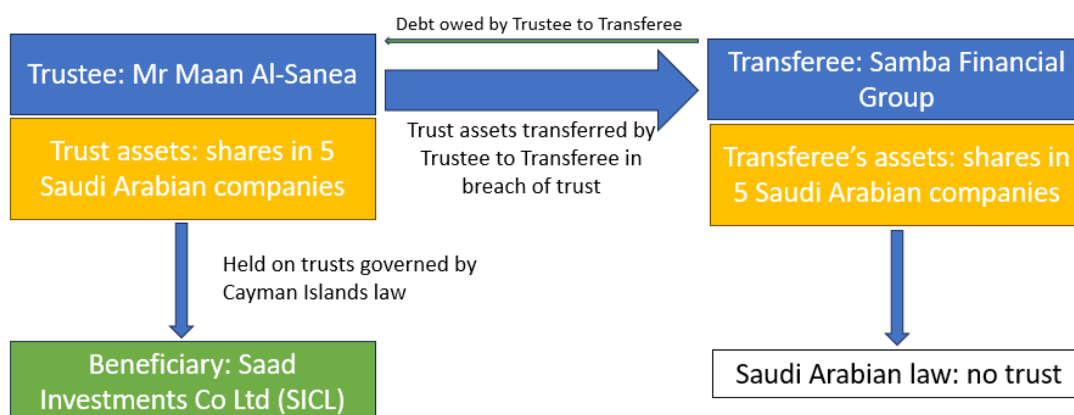
23. It was further held that the principle is not limited to cases where the wrongdoer mixes the misappropriated funds with his own money, but also with that of companies controlled by him which are to be fixed with his knowledge of the fraud: [916] – [929].

Tracing through non-trust jurisdictions: *Byers v Saudi National Bank* [2023] UKSC 51

24. Traceable assets are often subject to numerous transactions after the initial wrongdoing and before a claim is brought. Sometimes this will involve transfers which are located – as a matter of fact or law – in jurisdictions which do not have a law of trusts and do not recognise the concept of tracing or ownership in equity.

25. This gives rise to the question – recently considered by the Supreme court in *Byers v Saudi National Bank* – of whether the recipient in such a case can use the transfer through a non-trust jurisdiction to prevent the claimant from tracing.

26. This was what happened in *Byers v Saudi National Bank*:



27. The Appellant argued that a claim in knowing receipt did not require the existence of a continuing equitable interest; rather, it was sufficient that Samba knew that the assets had been transferred in breach of trust and therefore it would be unconscionable for them to be retained.

28. The Supreme Court rejected this argument. Lord Briggs, having conducted an analysis 'from first principles' and a detailed review of the authorities, trenchantly re-asserted the requirement for a continuing "*proprietary base*": [77].

29. The result is that transactions which have a foreign *situs* may well serve to defeat the ability of a claimant to trace as the equitable interest will 'overridden' by operation of law. English conflict of laws rules apply the *lex situs* to the proprietary effect of transactions. That can be a physical *situs* in the case of land and chattels. Shares have their legal *situs* in the jurisdiction of the company's incorporation. The *lex situs* may have different rules conferring an indefeasible title, and English law will (usually) recognise these, even if they have no English equivalent.

30. The Supreme Court also rejected the submission by the Respondents that, in allowing equitable interests to be destroyed by the mere fact of passing through a non-trust jurisdiction, they were in effect creating a "*money launderer's charter*". This was because the law of dishonest assistance (relied upon by Lord Briggs) and the criminal law (relied upon by Lord Burrows) would remain available to deter or pursue wrongdoers. Whether this will be the case in reality remains to be seen.

What's the matter? What's the remedy? A year of developments in stays and arbitrability

Fenner Moeran KC

1. Sometimes it feels like developments in a particular area of law are like buses – nothing for years, then three come along at once. This past year the question of arbitrability has seemed like that (at least in England). After a decade of stagnation this interesting but surprisingly rarely litigated issue has had three decisions on the topic:

    a. *FamilyMart China Holding Co v Ting Chuan (Cayman Islands) Holding Corporation* [2023] UKPC 33

    b. *Sian Participation Corp v Halimeda International Ltd* [2024] UKPC 16

    c. *Grosskopf v Grosskopf* [2024] EWHC 291 (Ch)

Preliminary issues

2. Before getting into the body of what these cases decide, it is worth briefly setting out the statutory background to them – in particular for the third case of *Grosskopf*, which deals with arbitration in the context of trusts. Whilst they come from different jurisdictions, the basic provisions are (perhaps unsurprisingly) strikingly similar, so I will just refer to the English legislation here. In England and Wales (and Northern Ireland), the legislative code relating to arbitration is found in the Arbitration Act 1996 (the "**1996 Act**").

3. The foundation of an arbitral panel's jurisdiction is consent: in order for a dispute to be referred to arbitration, there must be an arbitration agreement. The definition of "arbitration agreement" is found in section 6 of the 1996 Act. It is:

    an agreement to submit to arbitration present or future disputes (whether they are contractual or not)

    and it must – pursuant to section 5 of the 1995 Act – be made or evidenced in writing.

4. The reference to "*present or future disputes*" draws out the distinction, in the context of fraud and asset recovery claims involving trusts, between:

    (a) arbitration provisions found in the governing instrument of the trust itself, which are intended to refer hypothetical <u>future</u> disputes to arbitration; and

(b) freestanding arbitration agreements to refer a specific present dispute to arbitration.

5. The governing instrument of the trust itself will commonly be either a deed poll, i.e. a self-declaration by the trustee of the terms upon which the assets are to be held, or a bilateral agreement between the settlor and the trustee. That gives rise to two issues regarding who will be bound by an arbitration clause. First, the beneficiaries are not usually parties and do not normally provide their consent to the terms of the governing instrument. Second, it is not uncommon for trustees to resign and new trustees to be appointed from time to time. With that in mind, are those two categories of person bound by the arbitration clause?

6. In relation to beneficiaries, the answer as a matter of English law is uncertain, and the Trust Law Committee has recommended legislative intervention to clarify the law. In New Zealand, applying materially identical statutory provisions, the High Court has found that if any of the beneficiaries is not a party to the trust instrument, then the arbitration clause is – as between them – "null and void": *Ryan v Lobb* [2020] NZHC 3085 at [109]. If that decision were followed in England, then it would follow that such an arbitration clause would not comply with the 1996 Act.

7. However, there are arguments in favour of non-party beneficiaries nevertheless being affected by such clauses, just as they are by jurisdiction clauses (see *Lewin on Trusts (20th ed.)* at 49-010 onwards). In very broad terms, those arguments centre around the beneficiaries being prevented from taking the benefit of the trust without accepting the corresponding burden, such that the court ought to exercise its inherent jurisdiction to stay proceedings brought in breach of the clause—as to the discretionary nature of that jurisdiction, in the context of jurisdiction clauses, see *Crociani v Crociani* [2014] UKPC 40 at [36] and [37].

8. In relation to successor trustees, the position is still uncertain – in the absence of English authority – but the arguments are perhaps stronger. Successor trustees may (for the purposes of section 82(2) of the 1996 Act) be regarded as claiming "under or through" their predecessor trustees and therefore be treated as parties to the relevant arbitration clause.

9. Separately, what about cases where the entire trust instrument is alleged to have been created in fraudulent circumstances? Is anyone bound by it? By section 7 of the 1996 Act, an arbitration agreement is treated as a distinct agreement, and so is vitiated only by factors which directly concern the arbitration clause itself rather than a more general challenge to the transaction of which it forms a part. The dividing line is vividly illustrated by *Premium Nafta Products v Fili Shipping Company* [2007] UKHL 40—the fact that the agreement was procured by bribery or entered into by an agent without authority does not vitiate the arbitration clause, while the fact that the whole document is a forgery does so.

10. However, more generally a freestanding arbitration agreement may be made by a trustee pursuant to the power of compromise conferred by section 15(f) of the Trustee Act 1925, which expressly authorises a submission to arbitration. If they do so, the effect is that all those interested in the trust property will be bound by the submission to arbitration and in turn the arbitral award. However, that statutory power of compromise only applies to disputes "external" to the trust, such as a dispute between a trustee as landlord and a third-party tenant—see *Lewin on Trusts (20th ed)* at 36-094 onwards. In the fraud context, it may for instance apply to a claim against the trustees that the trust was settled with misappropriated assets, or to a claim made by the trustees to recover trust assets—see for example *Re MF Global UK Ltd* [2014] EWHC 2222 (Ch).

11. More difficult is the scenario in which a dispute arises which is "internal" to the trust. Then, an arbitration agreement may only be entered into by those parties who are of full age and capacity (and so will not bind, for example, beneficiaries who are minors, unless perhaps they can be said to be persons "claiming through or under" the trustee—see section 58 of the 1996 Act). Whether or not that matters will – as observed in *Grosskopf*– depend on the particular relief sought.

12. I discuss the question of what relief may be sought below. Particular difficulties arise when the arbitral tribunal lacks the powers conferred upon the court by statute, such as the power to remove a trustee or to appoint a new one (although there are potential workarounds—see for example *Rinehart v Welker [2012] NSWCA 95* at [176]. Those powers may, of course, be of crucial importance to safeguard the trust fund when the existing trustee (or one of a number of existing trustees) is suspected of fraud.

Arbitrability - introduction:

13. Whether you have an arbitration agreement or not, there is still the question of whether the disputes can be subject to arbitration at all. This is the question of arbitrability. This question can arise in particular where the court has special powers not available to arbitrators – such as winding up a company, or the relief available in cases of unfair prejudice petitions (where the jurisdiction has such provisions). Equally, trust disputes often involve the exercise of the Court's inherent supervisory jurisdiction over trusts, and in particular can involve remedies – such as replacement of trustees – which cannot be granted by arbitral tribunals, not least because to do so could affect third party rights. This issue is expressly recognised under the Arbitration Act 1996 ss.9(4) and 81:

    9.(1) A party to an arbitration agreement against whom legal proceedings are brought (whether by way of claim or counterclaim) in respect of a matter which under the agreement is to be referred to arbitration may (upon notice to the other parties to the proceedings) apply to the court in which the proceedings have been brought to stay the proceedings so far as they concern that matter.

(2) An application may be made notwithstanding that the matter is to be referred to arbitration only after the exhaustion of other dispute resolution procedures.
(3) An application may not be made by a person before taking the appropriate procedural step (if any) to acknowledge the legal proceedings against him or after he has taken any step in those proceedings to answer the substantive claim.
*(4) **On an application under this section the court shall grant a stay unless satisfied that the arbitration agreement is null and void, inoperative, or incapable of being performed**.*

81.(1) Nothing in this Part shall be construed as excluding the operation of any rule of law consistent with the provisions of this Part, in particular, any rule of law as to—
*(a) **matters which are not capable of settlement by arbitration;***
(b) the effect of an oral arbitration agreement; or
(c) the refusal of recognition or enforcement of an arbitral award on grounds of public policy.

Arbitrability – company and insolvency cases:

14. The starting point for this area of law was the 1987 case of *Fulham Football Club (1987) Ltd v Richards* [2011] EWCA Civ 855 [2012] Ch 333. This was a case involving a shareholders' unfair prejudice petition. However, the relief sought was simply injunctive (both mandatory and prohibitory) – so relief which the arbitral tribunal could have granted. Despite this, it give one of the earliest analyses of arbitrability, quoting from both Mustill & Boyd (2nd edition) Commercial Arbitration and Born (3rd edition) International Commercial Arbitration detailing known examples of non-arbitrability. Born in particular stated:

"The types of disputes which are non-arbitrable none the less almost always arise from a common set of considerations. The non-arbitrability doctrine rests on the notion that some matters so pervasively involve public rights, or interests of third parties, which are the subjects of uniquely governmental authority, that agreements to resolve such disputes by 'private' arbitration should not be given effect."

15. The Court of Appeal then said this:

40. This extract is interesting because it attempts to identify some common criteria applicable in the cases in which the matter in dispute has been held to be non-arbitrable. But it also, I think, indicates that the limitation which the contractual basis of arbitration necessarily imposes on the power of the arbitrator to make orders affecting non-parties is not necessarily determinative of whether the subject matter of the dispute is itself arbitrable. As Mustill & Boyd point out, it does not follow from the inability of an arbitrator to make a winding up order affecting third parties that it should be impossible for the members of a company, for example, to agree to submit disputes inter se as shareholders to a process of arbitration. It is necessary to

consider in relation to the matters in dispute in each case whether they engage third party rights or represent an attempt to delegate to the arbitrators what is a matter of public interest which cannot be determined within the limitations of a private contractual process.
41. Not surprisingly, the source of such restrictions cannot be found in the 1996 Act or what might be termed the law of arbitration itself. The statements of principle set out in the textbooks referred to above are simply recognitions that the scope of even the most widely drafted arbitration agreement will have to yield to restrictions derived from other areas of the law…

16. In the end the Court of Appeal concluded that unfair prejudice petitions were essentially arbitrable because, although in theory a winding-up order could be made by the courts, they are essentially private matters between the parties – and that doing so did not engage any public policy objective of protecting the public where a company continues to trade despite being insolvent. However, the Court of Appeal did recognise that winding-up would be a remedy which was outside the remit of the arbitrators. And finally, Patten LJ made an *obiter* suggestion (at paragraph 83) that an arbitrator could, in appropriate circumstances, make a ruling on whether it would be appropriate for a complainant to initiate winding up proceedings or be limited to some other remedy.

17. That conclusion leads to the next area of jurisprudence on non-arbitrable disputes – insolvency disputes. For a decade the leading English authority on the issue was Salford Estates (No.2) Ltd v Altomart Ltd [2014] EWCA Civ 1575 [2015] Ch 589. That was a highly contentious decision of the Court of Appeal which held that

    a. A winding up petition is not a "*claim*" for payment of the debt, so does not fall under Arbitration Act 1996 s.9(1)(4).

    b. However, the discretionary power of the Court in relation to winding-up companies under the Insolvency Act 1986 s.122 should be exercised to either dismiss or stay the winding-up petition whilst the underlying dispute as to the debts it was based on were determined by the arbitration proceedings – **irrespective of whether that dispute was a *bona fide* or genuine one**.

    c. At that stage the petitioner could, if appropriate, come back to the Courts for a winding-up order.

18. That requirement for any dispute as to the underlying debt – however hopeless and plainly non-genuine – to be resolved by arbitration before going to the Court for a winding-up order was heavily criticised. Ultimately the decision has very recently (19 June 2024) been overturned by the Privy Council in the case of *Sian Participation Corp v Halimeda International Ltd* [2024] UKPC 16. That decision held that where there is no genuine dispute as to the underlying debt the Court can simply proceed to winding-up, although if there is a dispute then the proper place for it to be adjudicated will be the arbitral proceedings. Again, once the status of the debt was resolved the parties could return to the Courts for a winding-up order, if still required.

19. One point to note in relation to *Sian Participation* is that the PC specifically limited the decision to generally worded arbitration clauses. As it said, "*Different considerations would arise if the agreement or clause was framed in terms which applied to a creditor's winding up petition*". Perhaps most interestingly of all, the Privy Council made what is called a *Willers v Joyce* direction, which provides that although this was a Privy Council decision on a BVI appeal, it applies to the law of England and Wales and therefore Salford Estates is now overturned both in the BVI and in England and Wales.

20. More generally in relation to arbitrability though is the only slightly less recent decision of the Privy Council in *FamilyMart China Holding Co v Ting Chuan (Cayman Islands) Holding Corporation* [2023] UKPC 33. That case was a 'just and equitable winding up' claim, where the shareholders agreement contained an arbitration clause.

21. In a decision which is well worth reading in full if you are interested in this area of law, the Privy Council distinguished between

    a. Subject matter non-arbitrability (e.g. the whole dispute is excluded due to public policy) and

    b. Remedial non-arbitrability (e.g. the award of certain remedies is beyond the jurisdiction the parties can confer).

22. In the latter case the PC emphasised that whilst some remedies may be unavailable, the underlying disputes (e.g. whether a party has breached a shareholders' agreement) may well be 'matters' which can be subject to arbitration (and the PC tended to follow up on the recent trend of authorities which takes a broad view of what constitutes such a 'matter').

23. However, the PC went on to hold that not only was winding-up not an arbitrable remedy, but also that Patten LJ's *obiter* suggestion in *Fulham Football Club* (i.e. that arbitrators could rule on whether seeking a winding up order was appropriate) was wrong, and that any ruling as to whether winding up was just and equitable would be "*ineffective*".

24. Overall I think that *Sian Participation* and *FamilyMart* follow the tendency in recent years of the courts to take a practical approach to arbitration. Rather like the recent broad brush approach to what is 'a matter' to be arbitrated (contrary to the earlier 'granular' approach) they have shown a clear preference for a real world / spirit of the law approach to controlling the court's processes – whilst at the same time emphasising the courts' supremacy over issues which are truly non-arbitrable, and to be retained in the public sphere.

Arbitrability – Trusts disputes:

25. *Grosskopf v Grosskopf* is the first English case which expressly considers this issue of arbitrability of trust disputes. It was argued in November 2023 and decided in February 2024, so after *FamilyMart* but before *Sian Participation*.

26. The case itself was factually a little unusual. It concerned a private trust of an orthodox Jewish family. Essentially the late father had settled a family trust, with his seven children being income and discretionary beneficiaries, and grandchildren and later descendants being discretionary beneficiaries. By the date of the dispute arising the father had died, two out of the seven children (the Defendants) were the trustees and at least one of the remaining children (the Claimant) was unhappy with how the Defendants were and had administered the trust, alongside how they had administered the father's estate. This was, of course, in the context of wider disputes within the family relating to, inter alia, various business dealings in both the UK and Israel. So far, so reasonably ordinary. What makes it odd is how the Claimant and Defendants sought to resolve their disputes (namely arbitration), and the arbitration process thereafter.

27. Because they are orthodox Jews the parties did not want, at least initially, to go to the secular courts. Instead in 2017 they brought their dispute before a Jewish rabbinical court, called a *Beth Din*, consisting of (at least in this case) three rabbis. As is standard with such matters the Beth Din required the parties to enter into an arbitration agreement, fixing the Beth Din as the arbitral tribunal. NB: Although this is absolutely standard procedure before Batei Din (the plural of Beth Din), the

precise wording of the arbitration agreement varies from tribunal to tribunal. Some are more comprehensive than others. In this case the original agreement recited that "*a dispute or difference has arisen … in regards to a claim about full disclosure of the estate / assets of the late R'Myer Grosskopf*" and that the parties agreed that "*any and all disputes and differences between them regarding the above issue*" were referred to the Beth Din "*according to principles of halachah* [Jewish rabinnical law] *and/or general principles of equity customarily employed in arbitration by the Beth Din and/or English law where applicable as decided by the Beth Din*". Accordingly, there was an arbitration agreement in place between the Claimant (one of the beneficiaries) and the Defendants (trustees, who were also beneficiaries) – at least in relation to some sort of dispute about "*full disclosure*".

28. The Beth Din proceedings then suffered from what might be called 'issue creep'. Effectively the issues covered by the arbitration agreement expanded, possibly by agreement, until by 2018 (by which time there had been three interim awards) when the Claimant sought to issue proceedings alleging breach of trust and seeking accounts and enquiries, the High Court held that that claim was subject to the arbitration agreement, and accordingly stayed the 2018 proceedings[1]. The Beth Din arbitral proceedings then continued, with a fourth interim award being granted.

29. Not deterred the Claimant came back in 2022 with a fresh claim. This time the Claimant sought removal of the trustees and appointment of a substitute judicial trustee. The Defendants applied to have the 2022 proceedings stayed under the Arbitration Act 1996 s.9.

30. The Claimant's argument was (essentially) that the relief sought was one which the arbitral tribunal could not grant, and as such was non-arbitrable, could not be subject to an arbitration and the proceedings could not be stayed under the Arbitration Act. As Lewin on Trusts (20th edition) puts it:

    "An arbitrator will lack the powers conferred on the court by statute, such as the power to remove a trustee or to appoint a new one and similarly lacks the court's jurisdiction to give directions to trustees… Nonetheless, an arbitrator will frequently be able to make orders having a comparable effect; an arbitrator could give effect to a claim for removal, for example, by ordering the trustee to resign, to appoint a new trustee and to convey the trust property to that person. If arbitration requires the consent of the beneficiaries, it is only if all those concerned in the question to be determined are of full age and capacity that there can be an effective decision. In other cases there can generally be no effective decision in view of the lack of contractual capacity of some of the beneficiaries."

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[1] Unreported, but at (2018) EWHC 3272.

31. With that background, in *Grosskopf* the Claimant argued that the claim was non-arbitrable. At most, he said, the underlying facts relating to the Court's decision on whether to remove trustees and appoint judicial trustees in their place could be subject to arbitration (and in *Grosskopf* had in the majority of cases **already** been determined by the Beth Din under the fourth interim award), but the claim itself could not – by analogy to the insolvency jurisdiction. (Possibly with some more power, had *Sian Participation* been decided in time – if the facts are obvious, just get on with the application for removal / appointment?)

32. Master Clark held otherwise. Essentially she held:

    a. At paragraph 65 that the arbitral tribunal could make orders which were **similar** in effect to replacement of trustees: "*it could direct the defendants to stand down; and to seek the appointment of new trustees by Malka; and, if she failed to do so, an application to the court under s.41(1) of the Trustee Act 1925, or indeed for a judicial trustee, could be made.*"
    b. And then, at paragraph 72:

       "*The fact that the claim seeks relief which the Tribunal cannot grant does not, in my judgment, make the dispute inarbitrable since:*
       "*(1) the grounds on which the appointment is sought are clearly suitable for resolution by arbitration; and*
       "*(2) in such an arbitration, the Tribunal would have the power to make a direction as to the defendants' position which could, if necessary, be enforced outside the arbitration.*"

33. That decision is not being appealed. The current status of this decision is therefore that it is effective as between the parties, but is only by a decision by a Master – which in turn leads to the (probable[2]) conclusion that it is persuasive but not binding authority, at least at High Court level.

Conclusion

34. The trend of the courts in England and across the common law world has been to favour the arbitrability of factual and legal disputes even where there are limits on the remedies which can be ordered by the arbitral tribunal.

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[2] See Michael Ashdown's article on this issue at https://www.wilberforce.co.uk/article/precedent-value-of-chancery-masters-decisions-3.

35. For example, while the remedy of winding-up is only available from a court, the underlying question grounding the relief – such as whether there has been unfairly prejudicial conduct by a majority shareholder (*Fulham Football Club (1987) Ltd v Richards* [2011] EWCA Civ 855) or whether it would be "just and equitable" to wind up a company (*FamilyMart China Holding Co Ltd v Ting Chuan (Cayman Islands) Holding Corporation* [2023] UKPC 33) – can perfectly properly be decided by an arbitrator. On the other hand, with the decision in *Sian Participation Corp* v *Halimeda International Ltd* [2024] UKPC 16 there is now an emphasis on preserving the courts' jurisdiction to decide the ultimate non-arbitrable matter.

36. *Grosskopf v Grosskopf* continues that trend by again focusing on what the arbitrator can properly decide (even if I think the court got the answer to that question wrong), and in that case thereby avoiding the issue of whether there are any remaining "gaps" to be filled by subsequent – and much more limited – court proceedings. In the absence of statutory intervention, practitioners in this space can no doubt expect to see more reported English cases on the boundaries of arbitrability in the trusts context. But whether any such decisions are actually enforceable, at least around the world, is still open to debate – and is a question for another paper.

Accessory liability following *Lifestyle Equities CV v Ahmed* [2024] UKSC 17

Thomas Lowe KC and Tara Taylor

What did the Supreme Court Decide?

1. In *Lifestyle Equities CV v Ahmed* [2024] UKSC 17, the Supreme Court was faced with the following question: when are directors of a company liable as accessories for causing the company to commit a tort of strict liability? In particular, is such liability also strict or does it depend on knowledge, or some other mental element. Further, if the directors are strictly liable, should they be ordered to account for profits made by either (i) the company or (ii) the directors themselves, in the latter case even if there is no finding of unconscionability or bad faith?

2. The facts of the case, in brief summary, were as follows. Lifestyle Equities brought proceedings against sixteen defendants claiming remedies for, inter alia, infringement of registered trademarks under ss.10(2) and 10(3) of the Trade Marks Act 1994 (infringement based on likelihood of confusion or reputation-based respectively). Liability under both those provisions is strict.

3. Those sued included two family-owned companies, Continental Shelf 128 Ltd and Hornby Street Ltd, both trading under the name "Juice Corporation". The defendants also included Mr Kashif Ahmed and his sister, Ms Bushra Ahmed. Mr Ahmed was the sole director of Continental Shelf and both were directors of Hornby Street at all relevant times. Lifestyle Equities complained that the Juice Corporation companies had been selling various items infringing trademarks registered by them. The Ahmeds were sued on the basis that they had authorised or procured the companies to do the acts complained of or had engaged in a common design with each other or the companies to cause them so to act. The case put against them was on the basis of strict liability only.

4. At first instance Hornby Street was found liable for infringing Lifestyle Equity's registered trademarks. Mr Ahmed was found jointly and severally liable with the Juice Corporation companies for the acts of infringement and Ms Ahmed was found jointly and severally liable with Hornby Street, notwithstanding the absence of any finding of bad faith in respect of either of them.

5. As to Lifestyle Equity's claim for account of profits, while the Court rejected the suggestion that the Ahmeds were liable to account for the profits made by their companies from the sale of the infringing goods, it held that they were liable to account for the profits they had personally made from the infringements by way of apportionment of their salaries during the relevant period. The Court also found that a loan made by Hornby Street to Mr Ahmed was profit derived from the infringements

for which Mr Ahmed was liable to account. Both parties appealed to the Court of Appeal, who dismissed the appeals save in relation to the Ahmeds' appeal in respect of the loan. Both parties appealed to the Supreme Court.

6. The main issues before the Supreme Court fell into two categories: (i) the liability issue, namely whether the lower Courts were wrong in law to hold that the Ahmeds were jointly liable with Hornby Street in the absence of any finding that they knew or ought to have known that the company's use of certain signs infringed Lifestyle Equity's trademarks; and (ii) the account of profits issue, in particular was it appropriate to award this remedy where there was no finding of unconscionability or bad faith. If it was, should the Ahmeds have been ordered to account to Lifestyle Equity for profits which the company had made from its infringing trade?

7. With respect to the liability issue, the Supreme Court had to begin by examining the nature of a directors' liability for procuring the company to commit a tort with strict liability. They went on to hold that there were no exceptions to exclude a director from such liability. The blow was softened because knowledge was an essential feature of the tort to justify imposing joint liability on someone who has not committed the tort; this is so even where, as in the case of infringement of IP rights, the tort does not itself require such knowledge.

8. In the present case, although the Ahmeds had procured acts attributable to the company which amounted to infringements, neither of them was found to have had the knowledge required to make them jointly liable on either principle of accessory liability and the lower Courts were therefore wrong to hold that they were jointly liable with Hornby Street.

9. As to the accounts of profits issue, the Supreme Court confirmed that although it is an equitable, discretionary remedy, it is to be expected that the Court will exercise that discretion in accordance with clear principles. These include that where accessory liability is established, liability will only attach to profits that were made personally from the infringements by the tortfeasor. In this case clearly the loan was not a profit, nor was the proportion of the Ahmeds' salaries upheld by the Court of Appeal; although payments made ostensibly as remuneration may in reality be a way of extracting profits from a company, there was no allegation or finding in this case that the salaries were anything but ordinary remuneration for services.

10. Accordingly, the Supreme Court dismissed Lifestyle Equity's appeal and allowed the Ahmeds' appeal.

The Tangle of Accessory Liability

11. Procuring a tort is not a separate tort but a species of accessory liability which gives rise to joint liability with the primary tortfeasor. That liability does not depend on the accessory satisfying all the elements of the tort. Instead, that accessory liability turns on the form of procurement by the accessory and the accessory's knowledge or intention. *Lifestyle Equites* establishes three important propositions concerning joint liability.

    11.1. No special rule applies to directors who procure a tort by their company. The reasoning that suggested a director should not be liable if doing no more than carrying out his constitutional role (see Chadwick LJ in *MCA v Charley Records* [2003] 1 BCLC 93) is no longer good law.

    11.2. Moreover, there is a greater potential for the joint tortious liability for directors and shareholders based on furthering a common design. Lord Leggatt emphasised (see [122] and [135]-[136]) the two quite separate, albeit occasionally overlapping principles of accessory liability in tort: (a) procuring the commission of a tort (without necessarily having any common or shared intention with the principal tortfeasor) and (b) more than minimal participation in a common design to commit a tort (without necessarily having the causal effect of procuring the tort).[3] Knowingly assisting the commission of a tort does not fall within (a) or (b) and does not give rise to joint liability (see [132]). A director who joins in a decision at a board meeting or a shareholder who votes at an EGM and contributes to the company's decision to take tortious action is not acting as agent for the company in committing the tort. Nevertheless, each of these may well be jointly liable with the company for having "participated" in a common design. The director who carries the vote into effect and commits the tort on the company's behalf is also jointly liable for procuring the tort.

    11.3. Thirdly, Lord Leggatt adopted a new explicit requirement for knowledge. He observed that "it seems unjust that anyone whose act causes another person to commit a tort should he held jointly liable for the tort as an accessory if the individual was acting in good faith and without knowledge of all of the essential facts which made the act of the other person tortious" (see [85] and [134]. It is not

[3] S The Supreme Court disapproved of statements which confused the two forms of liability such as in successive editions of Clerk & Lindsell "*Persons are said to be joint tortfeasors when their respective shares in the commission of the tort are done in furtherance of a common design*" (approved in *The Koursk* [1924] P 140 p151 and very recently confirmed by Lord Toulson in *Fish & Fish Ltd v Sea Shepherd UK* (see [2015] AC 1229 at [22]

surprising that this knowledge is required when liability is based on a common intention but the requirement exists whatever form of joint liability is under consideration (i.e. also for procurement). Moreover, knowledge is required for accessory liability even if the liability of the primary tortfeasor was strict without any mental elements, such as is the case in trade-mark infringement (see [134]). There is no logical requirement that the knowledge required for accessory liability must mirror that required for primary liability. "Good faith", whatever that might have meant, seemed to have been dropped by the time Lord Leggatt summarised the principles.

12. If joint liability can be established by a person acting in furtherance of a common design, where does the tort of unlawful means conspiracy fit in? Unlawful means can obviously include tortious conduct. However, an intention to injure the claimant is a necessary ingredient of unlawful means conspiracy but does not appear to be required when basis of liability of a joint tortfeasor is the furtherance of a common design.

13. Lifestyle Equities also re-defines the boundaries of the related tort of procuring a breach of contract:

    13.1. Although the liability for procuring a tort and procuring a breach of contract have been said to be different sides of the same coin (see *OBG v Allen* [2008] AC 1), in the corporate context these two forms of liability operate very differently because of the rule in rule in *Said v Butt* [1920] 3 KB 497. In that case McCardie J held (pp505-506) that a servant or agent, who causes a breach of his master's contract with a third person, cannot be held liable for procuring a breach of that contract.[4] Although this principle extends to any agent or servant who procures a breach of contract by his principal, it has particular application to directors. It is also thought to extend to a shareholder who would not be liable for voting in a manner which causes the Company to be in breach of contract.[5]

    13.2. The reason for the rule is not, as previously thought, because the servants' acts are those of his master.[6] The reason why the servant or agent or shareholder has no liability is because the normal understanding in a contractual setting is that if an agent causes the principal to break a contract only the contracting counterparty and not the agent will be liable (see [54]-[57]). The new rationale for

[4] It does not protect the agent for the principal's tortious conduct.

[5] See above for torts *Stocznia Gdanska SA v Latvia Shipping Co* [2001] 1 Ll R 537

[6] the so-called "dis-attribution fallacy": the attribution rule has nothing to do with personal liability of the director

Said v Butt also means that the principle is wider and extends to cases where the defendant causes a breach of certain relationships which are akin to contract or in which there was a voluntary arrangement between the parties. The Supreme Court agreed that where parties come together voluntarily to co-operate with each other on an understanding as to the allocation of risk, the law of tort does not impose obligations for procuring a breach of a contract. Thus, the building owner cannot normally sue the sub-contractor for a defect that causes the main contractor's contractual non-performance (see [57] approving *Simaan General Contracting v Pilkington Class Ltd No 2* [1988] QB 758). By this same token, a director will not be liable for causing a negligent misstatement made by the company because the parties do not proceed on the basis that the director has assumed the personal responsibility which creates the special relationship (see *Williams v Natural Health* [1998] 1 WLR 830 as explained by Lord Leggatt at [59]-[60]). As acknowledged by Lord Leggatt, this reasoning leaves *Henderson* v *Merrett* [1985] 2 AC 145 doubtful House of Lords authority for the liability of agents.

13.3. *Lifestyle Equites* confirms that accessory liability for tort also requires knowledge of all the essential facts, the same degree of knowledge that has always been recognised as necessary to establish the tort of procuring a breach of contract. This nevertheless remains a separate tort. However, the tort has an additional mental element of intention, although Lord Leggatt nowhere appears to recognises, it: the breach of contract had to be an end in itself (see *OBG* [22]-[25]).

Account of profits

14. An account of profits is a discretionary remedy requiring the defendant to account for the profits he has gained from his wrongdoing and disgorge them irrespective of whether his wrongdoing caused the claimant any corresponding loss (*Attorney General v Blake* [2001] 1 AC 268). It is, accordingly, a gains based rather than loss based remedy (by contrast to equitable compensation). The remedy is primarily available for equitable wrongs including breach of fiduciary duty, dishonest assistance, breach of confidence, infringement of IP rights and possibly knowing receipt (*Snell's Equity* 34th Ed. at [20-039ff]).

15. While it is well-established that the liability of a fiduciary who gains unauthorised profits within the scope of his duties to account for those profits to their beneficiary or principal is strict; and that those who dishonestly assist or knowingly receive trust property may also be required to account for the profits they gain directly as a result of their misconduct, until the decision of the Supreme Court in *Lifestyle Equities* there was a lack of clarity as to whether an innocent infringer of IP rights could be held to account.

16. For example, while the Court of Appeal in *GlaxoSmithKline UK Ltd v Wyeth Holding LLC* [2017] EWHC 91 (Pat) confirmed (at [23]) that "*a basic principle of accounts of profits is that there should be some unconscionable or improper conduct by the defendant*",

Birss LJ went on to explain that the remedy is not limited to cases of unconscionability, nor does the need for improper conduct impose any extra hurdle for a successful claimant in circumstances where the acts which render the defendant liable are themselves improper conduct. While it therefore appeared that provided liability is established, there is *no* additional requirement that there should be some unconscionable or improper conduct by the defendant, this was at odds with a number of earlier cases (see [147-149]).

17. The Supreme Court has now clarified that in the case of IP trademark infringement, the remedy is not confined to conscious or deliberate infringement. Its reasoning was based on the analysis that a central purpose of IP rights is to "*encourage and reward creativity and innovation by enabling the owner of the right to enjoy the fruits of its exploitation. That purpose is promoted by allocating profits made from exploiting the right to the owner, including where the right is infringed by commercial use made without the owner's consent. For this purpose it does not matter whether the infringement is deliberate or innocent. The reason for redirecting the profits to the owner of the right is not to punish or deter wrongdoing. It is to achieve the goals which the right exists to further*". The Supreme Court concluded that as "*lack of knowledge is no defence to a claim for damages for infringement of a trade mark, it should not defeat a claim for an account of profits*" ([157]).

18. The Supreme Court has also confirmed that the only profits for which a person should be ordered to account are profits which they have made personally; an order to account for someone else's profits (including the profits received by the dishonestly assisted fiduciary) would constitute a penalty or fine falling properly within the ambit of punitive damages ([158]). In those circumstances, the mere fact that a fiduciary has a substantial interest in a company which knowingly receives trust property will not make the fiduciary personally accountable for the receipt. Instead, a claimant would have to show that the profits (or some benefit representing them) flowed from the company to the defendant personally, for example in the form of a dividend.

19. While the decision in *Lifestyle Equities* has therefore curtailed a defendant's ability to avoid disgorging profits in IP trademark infringement cases where liability is established, it has also narrowed the scope of the profits that can be recouped. Time will tell whether and to what extent this leads to claimants abandoning claims for an account of profit in favour of damages.

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