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Topics

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Determining
Duty of Care

David Berkley QC

Review by CA in ***CGL Ltd & others-v-Royal Bank of Scotland & ots*** **[2017] EWCA 1073** of the different approaches to determining whether or not a duty of care is owed

On the 24 July 2017, the Court of Appeal handed down its awaited judgment in these three conjoined appeals, which relate to one aspect of the ongoing saga of interest rate hedging products miselling claims.

The decision will be a bitter disappointment to those claimants, whose complaints relate to products sold to them in 2006 and 2007; whose claims were already statute barred when issued; and who had participated unsuccessfully in the Past Business Review scheme agreed between the major banks and the Financial Conduct Authority.

Having delayed issuing their claim forms within the limitation period, sometimes in expectation that they would be able to recover redress within the Review, such claimants inventively raised another untested cause of action against the banks. They sued the banks for their alleged failure to conduct the Review in accordance with the terms agreed between those banks and the FCA.

Although there was no obvious privity of contract between themselves and the banks in respect of the conduct of the Review, the appellants nevertheless maintained that in conducting the Review, the banks owed a duty of care to their customers to conduct the Review with reasonable care and skill. How did such duty arise? The appellants unsuccessfully argued it arose because of a voluntary assumption of responsibility.

More broadly, in the field of tort, when determining whether or not, in any particular circumstances, a duty of care arose in respect of economic loss, judges have developed three formulations: (1) answering the simple question, whether there has been an assumption of responsibility; (2) the well-known three-fold test in *Caparo Industries plc v Dickman* [1990] 2 AC 605; and (3) the incremental approach derived from the Australian case law.

In his leading judgment, with which Lord Justice Lewison and Lord Justice McFarlane agreed, Lord Justice Beatson made plain his reluctance to follow any one of the three traditional tests in isolation and instead preferred "*a broad and relatively open-textured framework within which to assess the detailed factual circumstances and context of the particular case*" (at paragraph 61). The judgment was therefore structured in a manner that identified each of the three tests, in turn.

Significantly, and of wider interest, was Lord Justice Beatson's rejection of an unvarnished voluntary assumption of responsibility test. It appears from the judgment that he considered that the assumption of responsibility test had been overstated or perhaps oversimplified by the appellants. He was able to identify several factors which led him to the conclusion that the letters and communications relied upon by the appellants did not (at least upon an objective analysis) suggest any voluntary assumption of responsibility by the bank to the customer.

The Court also rejected the analogy which had been made with the disappointed beneficiaries cases, such as *White v Jones [1995] 2 AC 207, and* considered (at paragraph 96) that, unlike those exceptional cases, the banks' customers who were disappointed by the Review were not without remedy. Accordingly, there was no need for the common law to step up in order to fill the gap. Personally, I find this part of the judgment less convincing. Having regard to the restriction of some customers' rights of action for breaches of relevant regulations and the reluctance of the judges to make the common-law duties co-extensive with such regulations (cf. *Green & Rowley v Royal Bank of Scotland* [2013] EWCA 1197) a lacuna does arguably exist and certain classes of customers are indeed left without remedy.

Even outside the current interest in banking litigation, the *CGL* decision will be of interest to those lawyers who are engaged in professional negligence litigation, where economic loss has been suffered outside of those relationships or circumstances which traditionally give rise to duties of care.

The range of the inquiry is now likely to be more wide-ranging and the traditional tests are going to be used cumulatively and not in isolation, to produce, perhaps more nuanced answers to the questions of assumption or responsibility and proximity. In turn, practitioners will have to ensure that the information-gathering and disclosure and presentation of arguments are sensitive to this developing jurisprudence. At the time of writing, no decision had yet been made on the appellants' applications for permission to appeal to the Supreme Court.

DAVID BERKLEY QC

Unfair Prejudice Petitions

-Recent Cases

James Davies

Section 994 of the Companies Act:

"(1) A member of a company may apply to the court by petition for an order under this Part on the ground—

(a) that the company's affairs are being or have been conducted in a manner that is unfairly prejudicial to the interests of members generally or of some part of its members (including at least himself), or

(b) that an actual or proposed act or omission of the company (including an act or omission on its behalf) is or would be so prejudicial."

The unfair prejudice petition procedure continues to produce a number of reported decisions, both appellate and first instance. This seminar focuses on three recent decisions:

- *Ferster v Ferster* [2016] EWCA Civ 717
- *Re C & MB Holdings Ltd* [2017] 1 BCLC 269
- *In the matter of C F Booth Limited* [2017] EWHC 457 (Ch)

***Ferster v Ferster* [2016] EWCA Civ 717**

This was an appeal from a decision of Mrs Justice Rose to permit the amendment of a Section 994 petition to refer to the contents of an email.

The email had been sent in the context of a mediation and would normally have attracted mediation/ without prejudice privilege:

"*Dear Catherine,*

> *Thank you for returning the call. I am setting out below the 11 points of communication that I have discussed with you following written and telephone communications with DAC. The messages from the claimant are as follows:*

*1. We withdraw our existing offer to sell the shares of Warren and Stuart for the sum of [**redacted**].*

*2. We make a revised offer to sell the shares of Warren and Stuart to Jonathan for the aggregate sum of [**redacted**]. The revised offer is made subject to contract and without prejudice as part of a global compromise incorporating all the parties to the proceedings and the petition. The sale price is to be settled on completion in cash and also by the transfer to Warren and Stuart by Jonathan at market value of his share in any assets which the three brothers on jointly. Any settlements will contain amongst other provisions, confidentiality provisions.*

3. We have increased our offer because we have become aware of further wrongdoings by Jonathan. Jonathan knows the extent of his wrongdoings and our client believes that Jonathan is in very serious trouble which will also have serious implications for Jonathan's partner (Jonathan Seeds) by reason of Jonathan's actions.

4. It is for Jonathan to assess the reasonableness of the offer we are making. Jonathan ought to realise that the offer is beneficial to him and Jonathan Seeds and HSF should take is instructions.

5. The claimant has information that Jonathan does not only hold bank accounts in England (as per his affirmation) and various additional offshore accounts are held by him or on his behalf (and/or now Jonathan Seeds).

6. It is clearly in everyone's (and particularly Jonathan's) interest to wrap this up speedily and quietly. If it is not settled within 48 hours there is a real risk that such a settlement may no longer be possible – the concern being that others will become aware of it.

7. Mr Watts is expected to take his client's instructions as a matter of urgency as a settlement will obviate the need of further steps such as committal proceedings being issued.

8. If this offer is not accepted the company also proposes to accept third party funding. The amount of the company's claim will be amended and the amount required by Warren and

*Stuart for the purchase of their shares will be considerably higher than [**redacted]** (by at least another £3m) in light of the third party funder's share of sums recovered. Jonathan will also face the repercussions detailed below.*

9. If Jonathan has misled HSF and sworn false evidence Alan Watts will be aware that Jonathan will face charges of perjury, perverting the course of justice and contempt of court and is likely to be imprisoned. If Jonathan Seeds is implicated he will likewise be investigated and/or charged.

10. In the above circumstances, Jonathan's credibility and reputation will be destroyed barring him out of the online gaming business in the future. He will also have no prospect of succeeding in this case.

11. Furthermore and hypothetically, if a substantial judgment is entered against Jonathan and it is not satisfied by assets in Jonathan's own name, we will pursue third parties, such as Jonathan Seeds, as regards claims against them where Jonathan has sought to put assets out of the reach of his creditors.

If you wish me to convey any message back once you have talked to Alan and taken your client's instructions I am happy to assist. I do however have a very busy 48 hours coming up so we do have limited time."

The proposed amendment alleged that by that email the respondents had sought to extort a ransom price by making improper and unwarranted threats.

Mrs Justice Rose allowed the application to amend and the respondents on the petition appealed to the Court of Appeal. Lord Justice Floyd, delivering the judgment of the court, dismissed the appeal:

In *Unilever plc v The Procter & Gamble Co.* [2000] 1 WLR 2436 the issue before the court was whether it was open to a party to rely on allegedly unjustified threats of patent infringement proceedings made in the context of a without prejudice meeting. In the course of his judgment, Walker LJ at page 2444 identified a number of discrete exceptions to the without prejudice rule. One was:

"… One party may be allowed to give evidence of what the other said or wrote in without prejudice negotiations if the exclusion of the evidence would act as a cloak for perjury, blackmail or other "unambiguous impropriety" (the expression used by Hoffman LJ in Forster v Friedland (unreported) 10 November 1992… But this court has, in Forster v Friedland and Fazil-Alizadeh v Nikbin (unreported), 25 February 1993… warned that the exception should be applied only in the clearest cases of abuse of a privileged occasion."

The critical question was whether the privileged occasion is itself abused. The test remains unambiguous impropriety, it may be easier to show where there has been an improper threat rather than where there is simply an unambiguous admission of the truth.

The threat here was not concerned with what would happen if the increased offer was accepted but what would happen if it was not accepted.

They did not make an offer on the basis of the company's increased value. A fair reading of the email was that they wanted more for their shares because they had learned of their ability to cause the company to take the steps identified. *"To put it bluntly, Stuart and Warren believed that they had alighted on a way of frightening Jonathan into paying more their shares."*

What was involved was an evaluation of whether the threats unambiguously exceed what was permissible in settlement of hard fought commercial litigation (*Boreh v Republic of Djibouti* [2015] EWHC 769 (Comm) at [132]). The Court of Appeal held that Mrs Justice Rose was right to conclude as she did.

Allegations of serious misconduct are not uncommon in Section 994 proceedings. Whilst the principles discussed in this case are of wider application to civil litigation, in the context of Section 994 how such allegations are put in without prejudice discussions requires careful consideration.

***Re C & MB Holdings Ltd* [2017] 1 BCLC 269**

The petition in this case was presented by the trustee in bankruptcy of Mr Brown. Mr and Mrs Brown had operated the company together, and Mr Brown had continued to involved in its management notwithstanding his bankruptcy. On the trustee being appointed Mr Brown's 50% shareholding in the company vested in him. However, the trustee was not as a shareholder for a further ten months.

The trustees presented a petition for unfair prejudice or in the alternative for winding up under Section 124(2)b) of the Insolvency Act (the just and equitable ground). A dispute as to the trustees' standing arose in relation to the winding-up petition as they had not been registered as shareholders for at six months of the previous eighteen months.

Issues also arose in relation to the distinction between matters which were prejudicial to the trustees in their capacity as trustees and in their capacity as shareholders. The court was also required to consider in principle to what extent conduct pre-dating the ownership of the shares was relevant.

On the issue of standing the Registrar relied on the wording in Section 250 of the Insolvency Act that a member was to be read as including anyone to whom shares had devolved by operation of the law notwithstanding that their name had not been recorded in the register of members. The same concept also applies to petitions under Section 994 alone.

The shares had devolved to the trustees on their appointment as part of the vesting of the bankrupt's estate. The trustees had accordingly held the shares for the minimum ownership period and had standing to present a petition.

In order to obtain the 'protection' of s 994(1)(a) of the 2006 Act against unfair prejudice, a petitioner had to prove on the balance of probability (i) acts or omissions by the company or which involved conduct of the company's affairs, (ii) which caused prejudice to the petitioner's interests as a member, and (iii) which were unfair. As a matter of law, establishing financial loss to the petitioner was not a prerequisite to showing prejudice, as prejudice could cover many situations other than economic loss, but it could be difficult to establish prejudice without it.

The prejudice suffered by the trustees as a member had to be distinguished from any prejudice that actions in regard to the company might have had on them in their capacity as trustees in bankruptcy.

In addition, although the petitioners could rely on matters occurring before Mr Brown's bankruptcy which amounted to unfair conduct they could not do so if it was authorised, approved or ratified by the directors or if the unfairness had been remedied, unless it was likely to re-occur. Since the evidence showed that Mr Brown acted as a director after he was made bankrupt and that Mrs Brown permitted him to do so, the petitioners had established both that it would be unfair and prejudicial to

their interests as shareholders if they were required to remain locked into a company which continued to be managed by a disqualified director and that those circumstances made it just and equitable to wind up the company subject to determining the adjourned issues.

***In the matter of C F Booth Limited* [2017] EWHC 457 (Ch)**

There were a number of features of this trial to raise the interest of a shareholder disputes practitioner:

1) Allegations of excessive remuneration;
2) Allegations of an unfair dividend policy;
3) Considerable passage of time since the dividend policy was instigated;
4) A provision for a shareholder's shares to be bought under the articles, leading to a defence that the petition was an abuse of process.

Remuneration

The judge applied the test set out by Blackburne J in *Irvine v Irvine* [2007] 1 BCLC 349 the court considered whether applying objective commercial criteria the remuneration which was taken was within the bracket that executives carrying the responsibility and discharging the sort of duties that the respondent was could expect to achieve.

The court also drew attention to the fact that fair remuneration can impact on the price a purchaser is willing to pay for the purposes of valuation of shares under Section 994. On the facts of this case, and assisted by expert evidence, the court concluded that the remuneration paid exceeded the amount that reasonable directors acting in the best interests of the company could have sought.

Dividend Policy

The directors of the company controlled the dividend because the no higher dividend could be declared by the company than the directors recommended. No dividend had been declared since 1987.

Directors are not under a positive duty to consider whether profits should be distributed by way of dividend. The question is whether by not recommending the payment of a dividend the directors could be said to be abusing their fiduciary powers (*Irvine v Irvine* at [274]).

The directors' decision not to pay a dividend would only by impugned if they were in breach of their duties as directors which include:

i. To exercise the power to recommend or not recommend a dividend for the purposes for which the power was conferred;
ii. To reach the conclusion that they consider in good faith would be most likely to promote the success of the company as a whole;
iii. To exercise independent judgment.

The Judge concluded that the directors had long ago closed their mind to any possibility that the company would pay a dividend again. The justification that cash was key to the business did not work in the light of the findings about excessive remuneration. The directors were obliged to consider whether their own remuneration was in reality a distribution of profit discriminating against non-director shareholders. The directors had closed their minds to the concept of sharing profits with, and ignored the interests of, the non-director members.

Abuse of Process

The respondents relied upon the provisions in the articles provided for fair value sale to an existing member of the company. Fair value was to be determined by the company's auditors. If a member wished to purchase the shares at that fair value then the shares would be sold at that price.

On the basis that there was a mechanism in the articles to enable a members shares to be purchased at fair value the respondents argued that the petition was unnecessary or at least premature. This was not accepted. The auditors might well have reflected the no-dividend and remuneration policies which featured in accounts which they themselves had certified. There was no prospect of appeal under the procedure set out in the articles.

In respect of the delay argument it was acknowledged that the court's will not allow stale claims. In addition, if the company had sought to recover excessive remuneration from the directors it would have been limited to a period of six years. Any remedy was to reflect that period.

However, there had been no acquiescence in the no-dividend policy. It had been made clear in 1991 that the petitioner viewed the dividend policy as unfair. The failure to act did not mean that it would

be inequitable for them to complain about the failure to declare dividends during the six years leading to the issue of the petition.

Although a first instance decision the case provides a useful analysis of the issues which can arise in the second and third generation family companies where a division has arisen between those who hold shares, but are no longer involved on a day to day basis and those who remain active director/ shareholders.

Conclusions

The Section 994 route continues to provide an attractive route to shareholders who believed they have been prejudiced unfairly. There is no concept of "no fault divorce" under Section 994 and the cases demonstrate that it is not just current conduct which is relevant. Historic conduct can also be brought into account, but the considerations in such cases may differ.

JAMES DAVIES

What a relief -
A stage-by-stage approach to
relief from sanctions

Charles Irvine

Most practitioners will have come across relief from sanction applications in the post-*Denton*[1] world and the number of reported cases dealing with relief from sanction applications seem to be falling after the initial flurry of cases after *Mitchell*[2] and *Denton*. This guide deals with how the Court deals with relief from sanction applications during various stages of litigation.

The basics

CPR r. 3.8(1) provides: *"where a party has failed to comply with a rule, practice direction or court order, any sanction for failure to comply imposed by the rule, practice direction or court order has effect unless the party in default applies for and obtains relief from the sanction"*. CPR r. 3.8(4) provides an exception, whereby, unless the court orders otherwise, the time for compliance may be extended by a maximum of 28 days by prior written agreement of the parties provided no hearing date is put at risk.

The Court of Appeal's guidance in *Denton* provides a three-stage test to be applied by the Court where an application for relief from sanctions is made:

(1) Assess the seriousness and significance of the failure to comply with a rule, PD or court order. If the failure is not serious or significant, relief will generally be granted.
(2) Why the default occurred? If there is a good reason for the failure to comply, relief will generally be granted.
(3) If the breach is serious and significant and there is no good reason for the breach, the Court must look at all of the circumstances of the case to deal with cases justly, including the factors set out in CPR r. 3.9(1)(a) and (b). Those factors are for the litigation to be conducted efficiently and at proportionate cost and to enforce compliance with rules, practice direction and court orders.

[1] *Denton v TH White Ltd* [2014] EWCA Civ 906
[2] *Mitchell v News Group Newspapers Ltd* [2013] EWCA Civ 1537

1. Pleadings

Claim Form/Particulars of Claim: If a claim form has been served in its unsealed format or by second class post (rather than first class post), these are issues of substance and not form.[3] Provided these issues have been remedied, the Court will be willing to find that the first limb of *Denton* is made out in that the breach is not serious or significant and relief has been granted. However, if there has been a deliberate breach or the breach has not been remedied by the time of the application, relief will generally not be granted.[4]

Acknowledgement of Service/Defence: Generally the Court will look at the factors set out in CPR r. 13.3; however, the Court still need to consider the factors set out in *Denton*. If the breach is deliberate, the Court will generally not grant relief.[5]

Amended Pleadings: If the breach is ongoing at the time of the application or the amendment was ordered due to a lack of particularity in the first instance, the Court will generally refuse the application. However, if the amendment will not generally prejudice proceedings, relief will be granted.[6]

Cost Budgeting: If the budget is late but does not materially impact on the efficiency of litigation (even if there are chasers from the other side), relief will generally be granted.[7] However, if there is no budget at all, relief will generally be refused.[8]

Disclosure: If the disclosure order arises from a specific disclosure order or unless order, the Court will generally refuse relief from sanctions.[9] However, if there is no sanction attached to the disclosure order, the Court is likely to make an unless order in the first instance if an application is made promptly.[10]

[3] *Cant v Hertz Corpn [2015] EWHC 2617 (Ch) and Viridor Waste Management v Veolia ES Ltd [2015].*
[4] *North Midland Construction plc v Geo Networks Ltd* [2015] EWHC 2384
[5] *Talos Capital Ltd v JCS Investment Holding XIV Ltd* [2014] EWHC 3977
[6] *Simon Cockell t/a Cockell Building Services) v Holton* [2015] EWHC 1117
[7] *Murray v BAE Systems Plc*
[8] *Jamadar v Bradford Teaching Hospitals NHS Trust* [2016] EWCA Civ 1001
[9] *Matthew Chadwick (Phelps v Button* [2016] EWHC 3185
[10] *Ardilla Investments N.V. v ENRC N.V.* [2015] EWHC. As to promptness: *Egglesham v MOD* [2016] EWHC 3011

Evidence of Fact: If there is sufficient time for a party to investigate the allegations contained in the new witness evidence in good time before trial, relief will generally be refused.[11] By contrast, if there is sufficient time, relief will generally be granted.[12]

Evidence of Expert: Relief will generally be granted (subject to the usual rules on expert evidence).[13]

Other matters: These largely depend on whether the case has merits, what the breach is and whether the breach has been deliberate. For example, if hearing fees are paid albeit it late, relief will generally be granted.[14] By contrast, relief is generally not granted for breaches of unless orders or where a case is weak and the breach has

CHARLES IRVINE

[11] *Warwick Buswell v Symes & MIB* [2015] EWHC 2262*; Moore v Plymouth Hospitals Trust*
[12] *Sloutsker v Romanova* [2015] EWHC 545
[13] *Marchment v Fredrick Wise* [2015] EWHC
[14] *Abdulle v Commissioner of Police* [2014] EWHC 4052

Exclusions and limitations of liability
– interpretation and enforceability

Nicole Bollard

THE DECISION

Revie of Royal Devon and Exeter NHS Foundation Trust v Atos IT Services UK Ltd

Royal Devon and Exeter NHS Foundation Trust ("the Trust") entered into a with Atos IT Services UK Ltd ("Atos") for the provision of IT services ("the Contract"). Under the Contract Atos was required to provide a system for the provision of health record scanning, electronic document management and IT services ("the System"). The Contract price was just under £5 million. The Trust had various issues with the System when it was first introduced in 2012 and throughout the term of the Contract. Atos provided various modifications to the System but the problems persisted. The Trust terminated the Contract and brought a claim for breach of contract claiming damages of approximately £7.9 million.

The matter before O'Farrell J was the determination of two preliminary issues concerning the interpretation of two clauses in the Contract which sought to limit or exclude liability. The first issue was whether the Trust's claim for damages for wasted expenditure was excluded under a clause which sought to exclude liability for loss of profits, business, revenue, goodwill or anticipated savings. The second preliminary issue was whether clauses limiting Atos' liability was, as the Trust sought to argue, not capable of being construed and should therefore be declared as unenforceable. The relevant clauses were drafted in such a way that their intended meaning was not clear.

Analysis

In relation to the first issue, the Court considered previous authorities in which damages for wasted expenditure had been awarded. Atos argued that the sums claimed, in particular the internal staff costs, should be classed as lost revenue and relied upon a number of cases including *Aerospace Publishing Ltd v Thames Water Utilities Ltd* [2007] EWCA Civ 3. The Court held that the court was entitled to recover damages to compensate for the loss of a functioning System – being the non-pecuniary benefit of the Contract - and there was a rebuttable presumption that the value of this benefit was at least equal to the Trust's expenditure. The Court distinguished the authorities relied

upon by Atos, on the basis that in those case the internal costs related to staff expenditure diverted because of the breach rather than staff expenditure incurred in the performance of the contract.

On the second issue, the Court accepted the Trust's submission that the relevant clauses were poorly drafted. However, O'Farrell J directed herself to the courts' general aim to give effect to all contractual clauses where possible and proceeded to rescue the clauses by applying a sensible interpretation. The Court concluded that it was clear that the parties had intended to limit their liability and therefore sought to give effect to the parties' intention. O'Farrell J concluded that the language used in one particular clause was "not helpful" but it was possible to ascertain the parties' intentions when construing the Contract as a whole. Accordingly, O'Farrell J concluded that damages relating to a breach in the first twelve months of the contract would be limited to the total contract price, and if there was no default in the first twelve months damages would be limited to the charges paid in the twelve months prior to the first default.

IMPACT OF THE DECISION

This case restates a number of important points when it comes to both the drafting and interpretation of contractual clauses seeking to exclude or limit liability. Ultimately both issues before the court related to questions of interpretation and therefore the findings are specific to the facts in question. However, a number of more general points can be taken from the judgment.

On the first issue, O'Farrell J considered a number of previous authorities where damages for wasted expenditure had been awarded and concluded that, on the facts before the Court, these could not be categorised as lost profits, revenues or saving and were not caught by the exclusion clause. Parties who wish to exclude wasted expenditure will need to specifically provide for this in exclusion clauses.

There is nothing new here in relation to the second issue and the interpretation of clauses generally or the interpretation of limitation clauses. However, the case provides a useful example of the court saving a poorly drafted limitation clause, to avoid it being held unenforceable. How far a court will go to rescue poor drafting remains uncertain and it is therefore a potentially risky argument. As always, parties drafting contracts need to ensure that clauses (in particular important ones such as those seeking to limit liability) are clearly drafted.

NICOLE BOLLARD

Privilege

In Bankruptcy

Susan Jones

Introduction

Re Lemos; Leeds and another (in their capacity as the joint trustees in bankruptcy of the estate of Lemos) v Lemos and others

1. Sitting as a Judge of the High Court Judge Hodge QC considered:
    a. Whether the principle formulated by Mr Justice Goff in *Crescent Farm (Sidcup) Sports Limited v Sterling Offices Limited* [1972] Chancery 553 *"the Crescent Farm* Principle*"* applies in bankruptcy and
    b. Whether the second ground for the decision of Mr Justice Peter Gibson in *Re Konigsberg* [1989] 1WLR 1257 is still good law.
2. These questions required the Judge to consider the true meaning and effect of the first instance decision of Mr Justice Arnold in *Shlosberg v Avonwick Holdings Limited* [2016] EWHC 101(Chancery) and the Court of Appeal decision *Avonwich Holdings Limited v Shlosberg* [2017] 2 WLR 1075.

Factual Background

3. Mr Lemos petitioned for his own bankruptcy and on 1st April 2015 Joint Trustees were appointed. On 12th March 2017 Mr Lemos secured his discharge from Bankruptcy. Although Mr Lemos had significant debts there were very limited recoveries.
4. During the course of their investigations, the Trustees became aware that Withers had acted for Mr Lemos and obtained copies of Wither's files. Some of those documents may be subject to legal profession privilege belonging to either Mr Lemos or Mr Lemos jointly with his wife. Mrs Lemos also asserted that some documents might be subject to her sole privilege.
5. The Trustees believed a number of documents were likely to be useful for proceedings under section 423 of the Insolvency Act 1986 relating to transactions defrauding creditors. Those proceedings would be to set aside certain transactions entered into by Mr Lemos many years prior to his bankruptcy and related to offshore trustees owning property in which he and Mrs

Lemos resided. If those proceedings succeeded they would result in recovery of an asset valued in the order of £16.5 million, for the benefit of creditors.

6. The Trustees wrote to Mr and Mrs Lemos seeking confirmation that they did not object to the deployment of certain of the Withers documents for the purposes of proceedings relating to the property. Richard Slade & Co, acting for Mr Lemos, objected on the basis that the documents were privileged and privilege was not waived. Mrs Lemos' solicitors wrote in similar terms.
7. That matter came before Judge Hodge QC when Mr Lemo's Trustees applied for:
    a. Directions in relation to the use that could be made of privileged documents obtained by them from the bankrupt's former solicitors, Withers.
    b. An order pursuant to section 366(1) of the Insolvency Act 1986 requiring Withers to deliver up any further documents in their possession relating to the bankrupt's affairs or a witness statement containing an account of such affairs.

Legal Background

Avonwick v Shlosberg

8. Mr Shlosberg applied for an injunction to restrain a Dechert from continuing to act both for major creditors (Avonwick) in his bankruptcy and his trustees in bankruptcy. Avonwick were continuing with proceedings against Mr Shlosberg alleging conspiracy. Mr Shlosberg argued that Dechert had been provided with a large quantity of documents by his former solicitors and solicitors acting for a party in litigation against him should not have access to privileged documents.

9. At first instance the application of the *Crescent Farm* principles to cases where a trustee in bankruptcy acquires assets (as opposed to liabilities) was conceded by counsel for Mr Shlosberg. In those circumstances Mr Justice Arnold accepted that privilege in documents relating to assets of the bankrupt vested in the trustee. This point was not considered on appeal.

10. Mr Justice Arnold, at first instance held privilege remained with the bankrupt in respect of documents relating to liabilities, as this was not property that vested in the Trustees. This position was upheld on appeal with the Court of Appeal confirming privilege is a fundamental right that does not constitute property within the Insolvency Act 1986.

11. In *Lemos* there was a fundamental dispute between the trustees and respondents as to what the recent Court of Appeal decision of *Avonwick* decided. Determination of this required examination of the First Instance decision and the Court of Appeal Judgment and discussions on *Morgan Grenfell, Crescent Farm* and *Re Konigsberg.*

12. At first instance Mr Justice Arnold did not consider the principles stated by the House of Lords in *R (Morgan Grenfell & Co Ltd) v Special Commissioner of Income Tax* [2002] UKHL 21, [2003] 1 AC 563 were directly applicable to this case. This approach was not endorsed by the Court of Appeal. Sir Terence Etherton, Master of the Rolls, considered the question was whether or not the effect of the statutory bankruptcy codes was that Mr Shlosberg had been involuntarily deprived of his fundamental right to assert privilege. The Master of the Rolls could see no reason why the principles in *R v Derby Magistrates' Court ex p. B* [1996] 1 AC 487, *R v Secretary of State for the Home Department, Ex p Simms* [2000] 2 AC 115 and *Morgan Grenfell* should not apply.

13. Mr Justice Arnold considered *Crescent Farm (Sidcup) Sports Ltd v Sterling Office Ltd* [1967 C. No. 4181] and set out Mr Justice Goff's statement of the applicable principle:

> *"…it is clearly established that legal professional privilege of a predecessor in title does enure for the benefit of his successor…"* ("*the Crescent Farm* principle").

14. *Crescent Farm* involved the sale of land by the First Defendant to the Second Defendant and voluntary disclosure by the former to the latter of privileged legal advice. *Crescent Farm* decided that the Second Defendant as successor in title was able to maintain privilege in the advice as against a third party. The application of the *Crescent Farm* principle was conceded by counsel for Mr Shlosberg at first instances and was not considered on appeal. The Court of Appeal, however, distinguished *Crescent Farm* on the basis that it was not an insolvency case and turned on its own facts.

15. Mr Justice Arnold also referred to the decision of Mr Peter Gibson in *Re Konigsberg*, a decision which was applied in the context of bankruptcy, and was based on the *Crescent Farm* principle. Mr Justice Arnold stated: *"In this jurisdiction the trustee will often be able to rely upon the Crescent Farm principle".* The Master of the Rolls noted that Mr Justice Peter Gibson's decision in *Re Konigsberg* was based on a concession from counsel and predated *Derby Magistrates' Court, Simms* and *Morgan Grenfell* which set out the proper approach. The privileged information in issue in *Re Konigsberg* related to information liabilities and

assets. The Master of the Rolls stated the Judge in *Re Cook* [1989] BPIR 881 wrongly relied on *Re Konigsberg* in concluding that:

> *"....the power and the right to waive privilege in relation to the estate and affairs of a bankrupt pass to his or her trustees in the same way that his or her assets and the rights of possession of the books, papers and other records of the bankrupt relating to his or her estate and affairs pass t their trustee under section 311".*

The Decision

16. The Court of Appeal in *Avonwick* were not concerned with documents relating to assets, Judge Hodge therefore did not regard the Court of Appeal decision as directly authoritative on that point. Judge Hodge QC was of the view that on a true reading of the Master of the Rolls judgment, particularly because of reference to the trilogy of House of Lords cases, the Court of Appeal was intending to convey that merely because privilege is held by the bankrupt, the trustee does not automatically step into his shoes. HHJ Hodge QC was satisfied this extended to documents concerning liabilities and assets of the bankrupt.

17. Given the relevant principles were those in *Derby Magistrates*, *Simms* and *Morgan Grenfell*, maintaining the focus of privilege as a fundamental right, examining the express terms of section 311 which describes the duty of trustees to take possession of documents, there was nothing in that section about use of documents by the trustees. It followed that trustees were entitled to look at the documents but it was not necessarily implicit that trustees could waive the bankrupt's privilege.

18. Judge Hodge QC considered that whilst Mr Justice Arnold accepted the application of the *Crescent Farm* principle in relation to asset documents, he did so solely because the contrary was not argued, and with some reservation. Judge Hodge QC continued that the Master of the Rolls disapproval of *Re Cook* was because the deputy judge failed to have regard to the overarching fundamental human right implicit, and embodied, in the concept of legal professional privilege. Judge Hodge QC was satisfied that the view that *Re Konigsberg* applied in bankruptcy was inconsistent with the observations and reasoning of the Court of Appeal in *Avonwick*, and should not be followed.

19. As the *Crescent Farm* principle did not apply, the remaining issue was whether Mr Lemos could be ordered under section 333 and 363 of the Insolvency Act, to waive privilege in any documents released to his trustees.

20. On behalf of the Trustee's it was argued that section 333 imposes an obligation upon a bankrupt to cooperate with his Trustees in the fulfilment of their functions to the extent that the Trustees reasonably require and section 363(2) enables the Court with supervisory jurisdiction to compel compliance.

21. Mr Lemo's representatives argued that the reasoning underpinning the Court of Appeal's decision in *Avonwick* applies with equal force to section 333 and 363. The essence of the Court of Appeal's reasoning in *Avonwick* is the bankrupt can only be deprived of legal professional privilege if the Act expressly provides or such deprivation is a necessary implication of the express language of the Act's provisions. Section 333 does not expressly require a bankrupt to waive privilege if requested to do so by the trustees, accordingly the Court must presume the general words of the section were intended to be subject to basic rights, such as privilege.

22. HHJ Hodge QC preferred the submissions made on behalf of Mr and Mrs Lemos, stating:

> *"in my judgment the right to privilege is such a fundamental principle, as recognised by the House of Lords in the trilogy of cases previously cited, and by the Master of the Rolls in Avonwick, that only an express power to waive privilege in s.362(2) itself would confer jurisdiction upon the court to order such a waiver"* [279].

23. In the event that he was wrong, HHJ Hodge QC considered a very strong case would have to be made before the Court should order a bankrupt to waive privilege in relation to documents. The Judge considered it difficult to conceive circumstances in which such an order would be appropriate.

24. Judge Hodge QC refused permission to appeal.

Conclusion

25. The answer to both questions, considered by the Judge was a resounding No. In summary *Crescent Farm* was not a bankruptcy case and application of the principle to involuntary transfer of assets to a trustee would amount to an abrogation of the right of privilege.

Furthermore, *Crescent Farm* concerned assertion not waiver of privilege. *Crescent Farm* therefore is no authority on who has the right to waive privilege. In so far as Mr Justice Peter Gibson held that *Crescent Farm principles* did apply to bankruptcy, *Re Konigsberg* was wrongly decided. Judge Hodge QC was satisfied that the Court of Appeal in *Awonwick* overruled the second ground of the decision in *Re Konigsberg.*

26. This case acts as a reminder that privilege is fundamental and although privilege can be abrogated by statute, this requires express words or necessary implication, in the absence of either the Courts presume general words were intended to be subject to basic rights of the individual. Given the fundamental nature of privilege it is unsurprising that, the public interest in ensuring a trustee in bankruptcy is able to get in, realise and distribute assets, does not justify even a limited exception to the absolute nature of privilege. In short privilege trumps this public interest.

27.

28. In practice this case highlights the need for care for those acting on behalf of trustees and bankrupts, as trustees cannot use privileged documents in any way that may about to waiver of privilege without the bankrupt's consent nor can waiver be compelled, regardless of the potential benefit to creditors.

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