Financial and Professional Lines: End of year review

Steering you through the Complexities

January 2021

2020 was a very unusual year. The global pandemic caused major disruption to lives and businesses and resulted in a dramatic economic downturn. This posed many (ongoing) challenges for financial institutions (FIs), directors and officers (D&Os) and professionals and whilst we are not yet seeing many covid-related claims against FIs, D&Os and professionals, we expect such claims to emerge in due course. For now, we look back at key developments plus an overview of the case law impacting financial and professional lines.

A: DEVELOPMENTS

LEGAL PROFESSION

On 25 November 2019, the Solicitors Regulation Authority (SRA) introduced new Standards and Regulations, in place of the previous Handbook, with 7 Principles, 2 Codes of Conduct (one for firms, one for individuals) and numerous new or updated Guidance notes. The key changes introduced include:

Shorter and less prescriptive rules, with an emphasis on personal responsibility and professional judgment;

Shorter Accounts Rules;

Enabling solicitors to carry out ‘non-reserved’ legal work from within a business not regulated by a legal services regulator;

Allowing solicitors to provide reserved legal services on a freelance basis; and

Changes to the disciplinary rules.

Also on 25 November 2019, the Solicitors Disciplinary Tribunal (SDT) adopted a new standard of proof for professional misconduct cases, lowering it from the criminal standard ("beyond reasonable doubt") to the civil standard ("balance of probabilities"). This brought solicitors into line with barristers, licensed conveyancers and legal executives, to whom the civil standard already applied, as it does to most other regulated professionals.

It is too soon to comment on prosecutions of breaches under the new rules as most of the cases we are seeing come through are still governed by the old rules. However, over the past year or so we have observed the following general themes:

- Heightened intervention/enforcement activity (COVID-19 notwithstanding – see below), with the SRA more engaged, more likely to see cases through to a conclusion and active in identifying issues from the press;
- A willingness to pursue non-lawyers too, for example in the recent SDT prosecution of a large firm's HR director for his conduct of the firm's internal investigation into allegations of sexual misconduct against a Partner;
- Increased scrutiny of personal as well as professional conduct – see for example our briefing here which discusses the regulator's sanction of communications made by lawyers in a personal as well as professional context. The successful appeal in late November of the SDT's findings against a magic circle partner in relation to drunken sexual activity with a junior potentially marks a turning of this tide and a reassertion of the right to a private life outside the regulator's remit. That said, while the SRA confirmed in late December that it is not appealing that judgment, it gave a rather defiant public statement inter alia asserting that the case was properly brought, noting that the events in question took place before the introduction of the new Standards and Regulations and emphasising that the judgment confirmed that the principles of acting with integrity and upholding public confidence "are entitled to reach into a solicitor's personal life";

- Many cases continue to concern #MeToo issues of sexual harassment and bullying. The SRA statement mentioned above reaffirmed, notwithstanding the outcome of that particular case, that the SRA took allegations of sexual misconduct and sexual harassment very seriously and will continue to act upon them;
- The emerging prominence of diversity and discrimination issues, which would chime with global cultural shifts and also the new SRA Principle 6, requiring solicitors to act in a way that encourages equality, diversity and inclusion;
- Financial misconduct and money-laundering remains a source of many breaches and a key area of regulatory concern, as underscored by the SRA Business Plan 2020-2021 published on 29 September 2020;
- A willingness to prosecute junior solicitors and impose strong sanctions against them particularly where there is any element of dishonesty, even if there is evidence of them having mental health difficulties or operating within a toxic firm culture. One example here is the highly publicised strike off in April 2020 of a junior solicitor who left client documents on a train, experienced great anxiety and then lied to cover up her mistake (though currently subject to appeal); and
- A continued focus on the inappropriate use of non-disclosure agreements.

These observations are borne out in the SRA's "Upholding Professional Standards 2018/19" report, published on 14 December 2020, which provides a summary of enforcement action for the period.

This year, the SRA declared that it would be "pragmatic" and take a "proportionate approach" to regulating the profession during the coronavirus outbreak, and would focus on serious misconduct, clearly distinguishing, as per its Enforcement Strategy, between people who were trying to do the right thing, and those who were not.

However it stated that it still expected solicitors and firms to do everything they reasonably could to comply with their rules and follow their Principles. And in our experience the SRA operated very much on a "business as usual" basis following the March 2020 lockdown, in continuing to progress existing investigations and open new ones, issue production notices for documents and conduct 'virtual' forensic inspections. The SDT also continued to conduct hearings remotely.

We discussed the approach of the SRA/SDT in more detail and key areas of regulatory risk in the changed circumstances - including regarding client confidentiality and supervision - in our briefing here.

Whilst Covid-19 is a medical rather than a financial crisis, it is clear that the economic impact of the pandemic will be marked, whatever form any recession takes. What we do know from past experience is that recessions result in an uptick in claims against professionals, whether by financial institutions trying to cap their exposures to a falling or collapsing housing market or clients looking more closely at the outcome of transactions where money supply becomes squeezed. Professionals (and their insurers) become a fairly predictable target. With record low base rates and a suspension of certain stamp duties, the housing market is extremely active. Does fee earners working predominantly from home render mistakes more likely? It is hard to say, but concerns must remain particularly when conveyancers are under pressure from clients anxious to complete before the stamp duty holiday ends. Query also whether other disciplines are likely to be susceptible to error through home working. Supervision of junior fee earners, for example, will never be as easy when it is conducted remotely. This briefing examines the potential claims that may be brought against solicitors in light of the pandemic whether arising out of current and past work or related to any downturn in the economy.

ACCOUNTANTS AND AUDITORS

Audit reform

Audit reform has been on the agenda for a number of years, following the high-profile collapses of BHS, Carillion, and Thomas Cook, to name but a few, which brought the role of the auditors into the limelight.

The call for reform culminated in three reviews, which together set the path for changes to audit in the UK. These three reviews are:

The Kingman Review of the Financial Reporting Council, published 19 December 2018 - includes 83 recommendations and, in particular, recommends the replacement of the Financial Reporting Council (FRC) with a new independent regulator (the Audit, Reporting and Governance Authority (ARGA)), which would be accountable to Parliament. For more information see this briefing note.

The Competition and Markets Authority (CMA) review on the statutory audit market, the final report of which was published on 18 April 2019 – recommended oversight of audit committees to increase accountability, joint audits to increase choice of auditor and drive up quality, and an operational split between the Big Four's audit and non-audit businesses, to ensure maximum focus on audit quality.

The Brydon Review on the quality and effectiveness of audit, published 18 December 2019 – contained 64 recommendations, aimed primarily at the audit of Public Interest Entities (PIEs), for wide-ranging reforms to audit. For more information, see this briefing note.

Since publication of these reports, the Business, Energy and Industrial Strategy (BEIS) Select Committee on delivering audit reform, together with the FRC, has been pushing forward with reforms, subject to some delay due to the pandemic. On 6 July 2020, the FRC announced its principles for operational separation of the audit practices of the Big Four firms and, on 27 October 2020, the FRC submitted written evidence to the BEIS Select Committee, welcoming the broad conclusions of the three independent reviews and the "vast majority" of the recommendations. The FRC "strongly supports" Kingman's recommendation that the FRC be replaced with ARGA, with clear statutory objectives, and powers in law to deliver them; the written evidence sets out the progress made so far. The timetable remains unclear as a number of the changes require primary legislation.

The reforms could lead to increased enforcement activity against auditors but also against directors given that the ARGA is expected to have powers to sanction all directors, not just those that are also accountants.

Enforcement

On 31 July 2020, the FRC released its Annual Enforcement Review, providing a summary of the FRC's enforcement work over the past tax year. The FRC has identified those points on which audit firms most frequently fall short, and the underlying causes for such shortcomings. While there are a number of these, the report's preface by Executive Counsel Elizabeth Barrett singles out the failure to exercise professional scepticism (ISA 200) as an ongoing issue that continues to feature frequently. Auditors being too close to management (with the concomitant risk to objectivity that this creates) and insufficient escalation to and involvement of the audit partner (as a result of which the significance of issues in the context of the audit as a whole may be overlooked) are highlighted by the Report as two of the main causes for this. Another recurring theme that has featured frequently in FRC investigations is failure to obtain sufficient appropriate audit evidence (ISA 500).

The Review highlights the FRC's focus on these two areas by remarking that "Work in other areas cannot compensate for failings in these areas and it is rightly an expectation of the public that, at the very least, these two aspects of audit are achieved." In light of this very clear statement, it is to be expected that professional scepticism and sufficient audit evidence will be areas on which future FRC investigations will continue to focus. For more detail, please see our full article here.

Revising fraud standard

On 20 October 2020, the FRC launched a consultation, 'The Auditor's responsibilities Relating to Fraud in an Audit of Financial Statements', on the proposed revision of its UK auditing standard ISA (UK) 240. The consultation proposes revising the standard in order to lay down requirements which would provide clarification on the obligations of auditors when it comes to fraud including clarification that the auditor should obtain reasonable assurance that the financial statements are free from material misstatement due to fraud and a new requirement for an explanation in the auditors' report setting out the extent to which the audit was able to detect fraud. The consultation is open until 29 January 2021.

An economic downturn increases the risk of fraudulent accounting practice, especially if the company is in financial difficulties. Given the significant impact the pandemic has had on many businesses, that risk is particularly great. In addition, it is often when a company runs into financial difficulties that insolvency practitioners unearth irregularities. Greater obligations on auditors may lead to increased scrutiny of auditors and enforcement action.

Climate reporting

On 10 November 2020, the FRC published the findings of its Thematic Review of climate-related considerations by boards, companies, auditors, professional bodies and investors, together with a statement urging businesses to improve corporate reporting standards on climate change. The Thematic Review referred to investor support of TCFD-aligned disclosures, the further improvement needed, and increasing investor expectation that auditors challenge and test management assumptions.

CONSTRUCTION PI

RICS Minimum Terms

Due to unprecedented market conditions, revised RICS Minimum Terms came into effect on 1 May 2020, with the following key changes:

Fire Safety Exclusions: prescribed fire safety exclusions have been removed from the minimum policy terms; insurers can now apply their own fire safety exclusions.

EWS1 Form: RICS launched, in December 2019, a new External Wall Fire Review (EWS) process to be used by valuers, lenders, building owners and fire safety experts in the valuation of high-rise properties, with actual or potential combustible materials. The minimum terms change relates to the exclusion relating to contractual liabilities, which has now been extended to exclude cover for any liability incurred where the insured has relied upon the EWS1 form and the valuation report does not exclude liability to the lender or any person deriving title to the mortgage for any losses or potential losses arising directly and solely from the valuation being provided in reliance upon the EWS1 form. This exclusion only applies to valuations undertaken on or after 1 May 2020. Surveyors completing the form need to provide full information to their brokers/insurers about the process they are following and the measures they are taking to reduce the risk of claims. For surveyors relying on completed EWS1 forms as part of their valuation, they should make clear in their terms of engagement that they accept no liability in relation to the errors in the EWS1 that may impact the valuation.

Other key changes: The excess may now apply to defence costs, introduced to give insurers greater flexibility to write terms, meaning that surveyors may need to fund some of the claim against them. In addition, limits now apply on an aggregate basis with round the clock reinstatements.

FINANCIAL INSTITUTIONS AND D&O

FCA enforcement

Later than usual due to the pandemic, the FCA published its Annual Report and Accounts for the year ended 31 March 2020, along with its Enforcement Data for 2019/20, on 10 September 2020. In line with previous years, the number of open cases remains high, with levels flat with last year (though the number of cases opened during the period decreased by 46%), demonstrating that the FCA is continuing to pursue breaches and fulfil its approach to intervene at an early stage and use investigations as a diagnostic tool. In addition, whilst there has not been much change in terms of the total value of fines imposed (£224.4m in 2019/20 compared to £227.3m in 2018/19), the single largest fine amounted to £102.2m (against Standard Chartered Bank for AML breaches), a significant increase on the largest fines in the last two years (£76m and £34.5m), potentially highlighting that the FCA is willing to show its teeth. However, the distribution of those fines has changed, with the majority of the 15 financial penalties levied being against firms rather than individuals (in 2018/19, there was an even split). Of concern to firms, their D&Os and their insurers, the data shows that cases are taking longer to resolve (an average of 23.9 months, which is a 37% rise on 2018/19) and are costing more (an average of £229,000, up 121% on 2018/19).

The top five areas of enforcement activity remain the same as last year: unauthorised business (142 cases); retail conduct (134 cases); insider dealing (88 cases); financial crime (71 cases); and advice in relation to pensions (61 cases).

Activities carried on by unauthorised firms have come into sharp focus following financial scandals, such as the £236m collapse of mini-bond issuer London Capital & Finance (indeed, the FCA notes that there is an ongoing independent review into its supervision of LCF in this regard). During 2019/20, 20,326 reports were made about unauthorised business, which is the highest number received by the FCA in a single year and an 11% increase from 2018/19. The reports resulted in a number of outcomes, including the opening of criminal and civil investigations. An example of this is the case of *The Financial Conduct Authority v Skinner and ors* [2020] EWHC 1097 (Ch) where Our Price Records was found to have marketed its shares through false and misleading financial promotions that had not been approved by an authorised firm, and they were ordered to pay the amount back in restitution. In terms of outcomes generally, variation/cancellation of permissions or withdrawal of approvals remain the most common outcomes. For more information, see our briefing here.

Tackling money laundering and market abuse continues to be a key priority for the FCA, with the large Standard Chartered Bank fine demonstrating the FCA's commitment to tackling AML breaches. Of note, the Report highlights that the sharing of intelligence with the Government and other relevant agencies is key to this and this is borne out by the FCA's comment "*We play a key role in worldwide efforts to tackle financial services misconduct*" and confirmation that in 2019/20 the FCA received over 1,000 requests for assistance and disclosures from international counterparts. This is a trend that is only set to continue amongst all regulators, both in the UK and globally, and could mean that entities and their directors could face parallel and/or multi-jurisdictional actions against them.

At the heart of tackling market abuse and misconduct, is the drive to improve firm culture and the FCA noted in its Business Plan for 2020/21 and in the Report that it continues to focus on the 4 key culture drivers in firms – purpose, leadership, approach to rewarding and managing people, and governance – and their effectiveness in reducing the potential harm from firms' business models and strategies. Whistle-blowing reports are an important tool for improving firm culture and in the last period, the FCA received 1,153 separate whistleblowing reports, consisting of 2,983 separate allegations. Of the 1,153 reports, 218 resulted in the FCA taking action (8 cases described as "significant action" taken). The rest helped inform the FCA's work, were dismissed or are yet to be dealt with.

Individual accountability is a key part to improving culture and whilst the fines against individuals have decreased this year, this is not to suggest that individual accountability has fallen down the FCA's agenda. With the extension of the Senior Managers and Certification Regime (SM&CR) to all FCA-authorised firms (which occurred on 9 December 2019), the FCA notes *"This extension gives us a universal conduct tool to hold firms and individuals to account if they fail to meet these standards, while embedding personal responsibility within firms."*

Other points to note from the report are the FCA's continued focus on consumer protection, its work to oversee innovation products, such as AI, crypto assets and Fin Tech, in addition to the FCA's commitment to ensure that its regulatory framework allows everyone in financial markets, and those who use them, to respond to the growing risks from climate change and to support the necessary transition to a greener economy, including by improving climate-related disclosures and ensuring firms consider material climate-related financial risks and opportunities. This took a step closer to coming to fruition as on 9 November 2020, the Chancellor announced that HM Treasury intends to make it mandatory by 2025 for large UK companies and financial institutions to make climate-related disclosures in line with those recommended by the Taskforce on Climate-related Financial Disclosures ("TCFD") in 2017. For UK listed companies, the FCA launched a consultation in March 2020 outlining proposals for TCFD-aligned disclosure for premium listed commercial companies on a "comply or explain" basis. While the outcome of that consultation has not yet been published, the Interim Report states that the FCA plans to: (i) implement the new TCFD-aligned disclosure rule with effect from 1 January 2021; (ii) consult in the first half of 2021 on proposed new rules for a wider scope of issuers to be subject to this rule (coordinating as appropriate with BEIS, as discussed in relation to private companies below); and (iii) consider consulting on making the disclosures mandatory.

Impact of COVID-19 on financial regulation

Following the pandemic, which saw an increase in the number of staff working from home, overnight shifts to new systems and working practices and a widespread increase in cyber-crime, operational resilience is considered of vital importance. The FCA's annual report highlights the need for firms to have considered and adopted measures to maintain operational resilience, and that these measures and plans will be closely assessed.

In the US, regulatory and governmental investigations have been brought against companies and their directors and officers relating to COVID-19. Although fines and penalties are typically excluded from coverage, regulatory and criminal actions can result in substantial exposure to D&O policies from defence costs as well as increased liability in parallel litigation brought by shareholders, bankruptcy trustees and other parties. Regulators have focused on the potential for insider trading in the volatile markets, and there have been a number of high profile examples of regulators taking action against insiders. In addition, regulators have taken action against companies for market manipulation, hoarding, price gouging and other unfair business practices during the pandemic, and are focusing on COVID-19 related fraud, including fraud for fake COVID-19 treatments, consumers and lending programs.

We expect similar from the UK, set against an already high regulatory risk for D&Os. And it is not just the FCA, there are a number of regulators/prosecutors that could bring an action against D&Os for COVID-19 failures – which regulators are relevant to a particular director depends on the sector the business the director serves is in and the nature of the failure. It's also worth noting that directors may also find themselves subject to actions by multiple regulators in relation to one underlying issue. With the rise in international cooperation (the FCA notes in its annual report that it fielded over 1000 international requests), directors may also find themselves subject to foreign regulatory actions.

Moving away from enforcement, the pandemic has impacted the FCA's schedule, with many items on their agenda delayed or postponed.

Corporate criminal liability

This past year has seen the SFO enter into four approved deferred prosecution agreements (with Güralp Systems Ltd, Airbus SE, G4S Care & Justice Services (UK) Ltd and Airline Services Ltd), taking the total to nine. Shortly after announcing the latest DPA, the SFO released revised guidance (on 23 October 2020). In essence, the new guidance highlights the relevant factors in considering whether a DPA, as opposed to prosecution, is in the public interest, with the continued focus on cooperation, which has been shown in the DPAs to date to be key to securing one. The guidance also covers the appropriate factors to be taken into account where a DPA is under consideration and there is a parallel investigation by an overseas or other UK agency. For more information, please see our full article here.

DPAs fall within a general push for corporate criminal liability, which in recent years has seen the introduction of the Criminal Finances Act 2017, which makes companies and partnerships criminally liable if they fail to prevent tax evasion by an associated person, further to the Bribery Act 2010 which introduced the 'failure to prevent' model. In a Freedom of Information Request response dated 21 October 2020, HMRC confirmed that, as at 13 October 2020, it currently has 13 live corporate criminal offences investigations plus a further 18 live opportunities currently under review. No charging decisions have yet been made. These investigations and opportunities span 10 different business sectors, including financial services (which has the most investigations), oils, construction, labour provision and software development.

Ms Osofsky, the director of the SFO, is an advocate for more failure to prevent offences to be introduced and has been keen to reform the identification principle in corporate criminal liability. This is where, in order for the company to be held liable, a prosecutor must prove that the individuals involved in the crime represent the “directing mind and will” of that company i.e. the individuals' actions are to be considered those of the company. This is very difficult to establish and has led to a low number of convictions. This was seen in February 2020 when the SFO released judgments (originally handed down in 2018 but delayed until the executives themselves were acquitted) showing that charges against Barclays were dismissed as the court found that the senior executives were not the directing mind and will of the bank in the circumstances, despite being the CEO and CFO.

On 3 November 2020, the government published its response to the 2017 call for evidence on corporate liability for economic crime, which showed that none of the suggested reforms (which included introducing legislation to replace common law rules, a new vicarious liability offence in relation to economic crime and regulatory reforms) gained the support of more than half of the respondents. However, many agreed that the identification principle inhibits holding companies to account for economic crimes

On the same day, the Law Commission announced a project to investigate the law concerning corporate criminal liability, with the intention of publishing an Options Paper in late 2021.

The conversation is moving and we can only expect there to be more scrutiny and investigations into companies that fail to prevent crime within their organisations, presenting a greater risk to FIs and their D&Os.

B: CASE LAW

GENERAL

Vicarious liability

Vicarious liability is the legal principle by which one person or organisation is held liable for harms caused by another. There are two elements to the test:

There must be a **relationship** between the parties which makes it fair, just and reasonable for the law to make one pay for the wrongs committed by another ("1st stage").

There must also be a **close connection** between that relationship, and the tortfeasor's wrongdoing ("2nd stage").

In recent years there have been a number of decisions which have stretched the boundaries of this principle. Earlier this year the Supreme Court gave judgment in two decisions which each considered a different element of the test.

In *Barclays Bank plc v Various Claimants* [2020] UKSC 13, the Court considered the first stage of the test and the nature of the relationship between the wrongdoer and the entity allegedly liable for him, providing clarity on the test to be applied. Our briefing note is available here.

Although in a professional firm context, it is of course clearly established that firms will be vicariously liable for the actions of their employees and Partners, this judgment is helpful in confirming that the key distinction is between relationships "akin to employment" and mere independent contractors. This is because:

it confirms that a firm will not have vicarious liability for the acts of other parties it has involved in a matter – for example, barristers or overseas agents - if it can demonstrate those other parties were engaged as independent contractors; and

conversely, that other professional firms and companies can be held vicariously liable, for contribution purposes, for the acts of other individuals with whom they have a relationship "akin to employment".

In *WM Morrison Supermarkets plc v Various Claimants* [2020] UKSC 12, the court was concerned with the 2nd stage of the vicarious liability test, and the "close connection" necessary between the 1st stage relationship and the tortfeasor's wrongdoing in circumstances where the tortfeasor had gone outside the strict confines of his employment. The Supreme Court confirmed that the test to be applied is that set out in the case of *Dubai Aluminium v Salaam* [2002] UKHL 48, i.e. whether the wrongful act was so closely connected with the acts the tortfeasor was authorised to do that, for the purpose of the liability of the employer to third parties, the wrongful conduct may fairly and properly be regarded as done by the tortfeasor while acting in the ordinary course of the employer's business or his employment. Our briefing note is available here.

Illegality

It is a well-established principle that claimants are barred from recovering where their claim is marked by illegality. The illegality defence has come back into focus over recent years after the Supreme Court's decision in *Patel v Mirza* [2016] UKSC 42, in which the court identified a number of factors that may be relevant to the assessment of whether the defence should operate to prevent a claim being brought:

The underlying purpose of the prohibition which has been transgressed and whether the purpose would be enhanced by denying the claim;

Any other relevant public policy on which the denial of the claim may have an impact; and

Whether denial of the claim would be a proportionate response to the illegality.

In doing this, the Supreme Court allowed the Courts to take a discretionary approach based on individual factors and policy considerations in each case.

Three recent decisions allow us to see how the Courts are interpreting the Supreme Court's guidance for the illegality defence and particularly highlight how fact specific, and on occasion narrow, the illegality defence is.

On 3 November 2020, the Supreme Court in *Stoffel & Co v Grondona* [2020] UKSC 42 applied the test in *Patel* and declined to bar a claim against a law firm for negligence in the context of a mortgage fraud. In doing so, the court upheld the decisions made in the lower courts (though only the Court of Appeal decision had applied *Patel)* and considered the degree of connection between the illegal conduct and the retainer needed for the doctrine to apply. However, the decision does not establish any principle that claims against professionals tainted by illegality can proceed; rather that the policy considerations at play on the facts did not produce the necessary incoherence in the law required. Our full article on the case is here and the briefing by our accountants' team is here.

Earlier this year, the Supreme Court, applying *Patel*, also declined to find that the illegality test barred a company's claim against a bank for breach of its Quincecare duty, choosing instead to apply a reduction for contributory negligence. Further details of the decision in *Singularis* are below, together with a link to our briefing note.

Finally, in *Day v Womble Bond Dickinson* [2020] EWCA Civ 447*,* the Court of Appeal applied *Patel v Mirza* where a claimant alleged that the defendant law firm had acted negligently in defending him in criminal proceedings, and, in particular, had not raised an abuse of process defence. The court barred the claim on the basis that it would be an abuse of process under the civil procedure rules to allow a collateral attack on the subsisting conviction; the proper approach being for an aggrieved defendant is to pursue an appeal through the Criminal Appeal Courts. Applying *Patel v Mirza*, the court concluded that this was a fair and proportionate result as it avoided an abusive collateral attack on the appellant's conviction and avoids inconsistency and incoherence. There was no public policy considerations which strongly suggested a different outcome. In this case (in contrast to *Stoffel)*, the claim was inextricably linked to the criminal conduct and the claim could not succeed without the Court undermining a criminal conviction.

However, the Court of Appeal did accept that Mr Day could, at least theoretically, claim for the increased legal costs incurred as a result of the fact that his costs were higher than they would have been if the case had proceeded in the Magistrates Court, on the basis that this was not part of the punishment handed down by the criminal court and was not necessarily caused by the illegal conduct.

Dishonesty

In July, the Court of Appeal confirmed in *R v Barton* [2020] EWCA Crim 575 that the test for dishonesty in criminal proceedings is that set out (*obiter*) by the Supreme Court in *Ivey v Genting Casinos UK Ltd* [2017] UKSC 67 and not that set out in *R v Ghosh* [1982] Q.B. 1053, thus ending the uncertainty over the correct test that had existed since *Ivey* was decided. *Barton* confirms that the correct test is, firstly, the Defendant's actual state of knowledge or belief as to the facts and, secondly, whether the Defendant's conduct was dishonest by the standards of ordinary decent people. Crucially, it is no longer necessary for the defendant to have realised that his conduct was dishonest by those standards. Our briefing note is available here.

LEGAL PROFESSIONALS

SAAMCo

The case of *LIV Bridging Finance Ltd v EAD Solicitors LLP* [2020] EWHC 1590 (Ch) concerned four loans paid over a 10 month period as part of short term bridging facilities for use in the development of land. LIV, the lender, contended that it suffered loss as a result of the solicitors paying away the loan monies in breach of trust without ensuring that they were first secured by a first legal charge over specific properties, contrary to their instructions. Therefore, when the borrowers defaulted, LIV sustained significant losses and sued the solicitors for breach of trust, seeking recovery of the full amounts lost. The High Court confirmed that the SAAMCo principle (as elucidated in the 2018 case of *Hughes-Holland v BPE Solicitors*), limiting recovery of damages in certain circumstances, applies to cases of breach of trust by solicitors.

This is helpful to the profession; it reinforces the application of the principle that solicitors are only responsible for losses within the scope of their duty. The critical distinction remains whether a solicitor is advising on a course of action (which exposes greater losses) or merely providing information for the client to be able to do so (which makes those losses more capable of challenge). Importantly, this extends to breach of trust - an argument often made when client funds are involved.

Read the full article here.

Conflict of interest

Claims can often involve an allegation of conflict of interest; for example continuing to act when the firm may have been negligent. However disputes can also arise in relation to the holding of confidential information.

In *Glencairn IP Holdings Ltd v Product Specialities Inc (t/a Final Touch)* [2020] EWCA Civ 609, the Court of Appeal has provided helpful guidance on the circumstances in which a law firm can be restrained from acting for a defendant where, in earlier similar litigation, the same firm has acted for another defendant against the same claimant and that earlier litigation was settled.

The somewhat unusual application was made on the basis that the law firm, Virtuoso Legal, had obtained information confidential to Glencairn IP Holdings Ltd following its settlement of the earlier litigation, and that there was a risk this information would be passed to Virtuoso's client, Product Specialities Inc (t/a Final Touch).

This judgment provides helpful clarification on the scope of application of the *Bolkiah* test. A "true fiduciary relationship", such as that between solicitor and client, justifies the imposition of the strict approach in *Bolkiah*, but a more limited relationship - such as a duty of confidence - does not. In the latter case, the burden of demonstrating a risk of misuse of confidential information will remain with the applicant, and the onus will not be on the law firm to show that there is no risk of prejudice.

Read the full article here.

Loss of chance

What might be seen as a decision which need concern only personal injury lawyers bears some examination given the possible ramifications on actions against professionals. The Court of Appeal recently handed down judgment in *Swift v Carpenter* [2020] EWCA Civ 1295, addressing what has long been viewed as an unsatisfactory approach to the calculation of awards for accommodation needs in personal injury and clinical negligence litigation.

Ms Swift was aged 39 at the time of the accident, and suffered serious injuries to her lower limbs. Unfortunately her injuries meant that she had to undergo a below-knee amputation to her left leg, and needed a metal plate inserting in her right foot. She was been left with significant ongoing symptoms, including incurable phantom limb pain where her left lower leg was amputated, and pain and stiffness in her right foot.

The Judge at first instance made an award for general and special damages in the sum of £4,098,051.

Due to the extent of her injuries and ongoing limitations, Ms Swift required a more expensive property which would be suited to her specific needs. The Judge found that Ms Swift's accommodation needs would be met by a property valued at £2,350,000, the purchase of which would require additional capital investment of £900,000 in excess of the value of the Claimant's current home of £1,450,000. However, the Judge held that she was bound by the longstanding approach to accommodation claims as laid down in Roberts v Johnston, and awarded nothing for the additional capital cost of Ms Swift's property.

The Court of Appeal's approach to solving the problem of overcompensation was to award a sum which was equivalent to income which would have been achieved had the capital used to purchase the property instead been invested in risk free-investments. Since 2001, this has seen the Courts calculate accommodation awards using the prevailing discount rate, at that time 2.5%. Of course, in 2017 a negative discount rate of -0.75% was announced. Although this meant that the value of Claimants' future loss claims increased overnight, one (perhaps unintended) consequence was that accommodation claims went the other way; potential awards were suddenly wiped out due to the impact of a hypothetical negative return on risk-free investments. This remained the case when the discount rate was changed to -0.25% in 2019.

It was held that Mrs Swift that she should be awarded the additional capital cost of the new property less the value of the reversionary interest. The Court concluded that the value of the reversionary interest is to be calculated by reference to a "market valuation" adopting an investment return of 5% per annum across the claimant’s expected lifetime (applying the appropriate life multiplier).

The upshot of this was that the decision at first instance with regard to Ms Swift's claim for accommodation costs was overturned and she was awarded £801,913.

The means that Claimants with specific accommodation needs can now expect the overall value of their injury claim to increase, and in many cases this will be by a very considerable margin. It should be noted that the Court of Appeal stated that in some instances, such as cases with short life expectancy, a different approach may be justified.

Read the full article here.

Conflict of interest

Claims can often involve an allegation of conflict of interest; for example continuing to act when the firm may have been negligent. However disputes can also arise in relation to the holding of confidential information.

In *Glencairn IP Holdings Ltd v Product Specialities Inc (t/a Final Touch)* [2020] EWCA Civ 609, the Court of Appeal has provided helpful guidance on the circumstances in which a law firm can be restrained from acting for a defendant where, in earlier similar litigation, the same firm has acted for another defendant against the same claimant and that earlier litigation was settled.

The somewhat unusual application was made on the basis that the law firm, Virtuoso Legal, had obtained information confidential to Glencairn IP Holdings Ltd following its settlement of the earlier litigation, and that there was a risk this information would be passed to Virtuoso's client, Product Specialities Inc (t/a Final Touch).

This judgment provides helpful clarification on the scope of application of the *Bolkiah* test. A "true fiduciary relationship", such as that between solicitor and client, justifies the imposition of the strict approach in *Bolkiah*, but a more limited relationship - such as a duty of confidence - does not. In the latter case, the burden of demonstrating a risk of misuse of confidential information will remain with the applicant, and the onus will not be on the law firm to show that there is no risk of prejudice.

Read the full article here.

Loss of chance

What might be seen as a decision which need concern only personal injury lawyers bears some examination given the possible ramifications on actions against professionals. The Court of Appeal recently handed down judgment in *Swift v Carpenter* [2020] EWCA Civ 1295, addressing what has long been viewed as an unsatisfactory approach to the calculation of awards for accommodation needs in personal injury and clinical negligence litigation.

Ms Swift was aged 39 at the time of the accident, and suffered serious injuries to her lower limbs. Unfortunately her injuries meant that she had to undergo a below-knee amputation to her left leg, and needed a metal plate inserting in her right foot. She was been left with significant ongoing symptoms, including incurable phantom limb pain where her left lower leg was amputated, and pain and stiffness in her right foot.

The Judge at first instance made an award for general and special damages in the sum of £4,098,051.

Due to the extent of her injuries and ongoing limitations, Ms Swift required a more expensive property which would be suited to her specific needs. The Judge found that Ms Swift's accommodation needs would be met by a property valued at £2,350,000, the purchase of which would require additional capital investment of £900,000 in excess of the value of the Claimant's current home of £1,450,000. However, the Judge held that she was bound by the longstanding approach to accommodation claims as laid down in Roberts v Johnston, and awarded nothing for the additional capital cost of Ms Swift's property.

The Court of Appeal's approach to solving the problem of overcompensation was to award a sum which was equivalent to income which would have been achieved had the capital used to purchase the property instead been invested in risk free-investments. Since 2001, this has seen the Courts calculate accommodation awards using the prevailing discount rate, at that time 2.5%. Of course, in 2017 a negative discount rate of -0.75% was announced. Although this meant that the value of Claimants' future loss claims increased overnight, one (perhaps unintended) consequence was that accommodation claims went the other way; potential awards were suddenly wiped out due to the impact of a hypothetical negative return on risk-free investments. This remained the case when the discount rate was changed to -0.25% in 2019.

It was held that Mrs Swift that she should be awarded the additional capital cost of the new property less the value of the reversionary interest. The Court concluded that the value of the reversionary interest is to be calculated by reference to a "market valuation" adopting an investment return of 5% per annum across the claimant’s expected lifetime (applying the appropriate life multiplier).

The upshot of this was that the decision at first instance with regard to Ms Swift's claim for accommodation costs was overturned and she was awarded £801,913.

The means that Claimants with specific accommodation needs can now expect the overall value of their injury claim to increase, and in many cases this will be by a very considerable margin

It should be noted that the Court of Appeal stated that in some instances, such as cases with short life expectancy, a different approach may be justified.

In this context, we would expect to see claims against legal professionals alleging the loss of a chance to obtain a higher settlement, whether that be:

against practitioners who fail to take into account (or challenge where appropriate) the new guidance when settling Schedules of Loss and negotiating settlements following the handing down of the Swift judgment; or

against practitioners who ought to have known that the Swift claim was to go before the Court of Appeal as a test case addressing the methodology of calculating accommodation claim, and who failed to advise their Claimant clients to delay settling their claims until the outcome of the Appeal was known.

Liability for rogue partners

The judgment in *Baines and others v Dixon Coles and Gill (A Firm)* EWHC 2809 (Ch) provides helpful guidance on the key issues to consider when there are claims against innocent partners arising from the fraudulent acts of a dishonest partner. The Court followed the House of Lords decision in *Dubai Aluminium Co Limited v Salaam* [2003] 2 AC 366 in finding that it is necessary for claimants to demonstrate that the dishonest acts were carried out in the ordinary course of the firm's business and so the innocent partners should be liable for them pursuant to the Partnership Act 1890.

The case is also an important decision in relation to aggregation under the SRA's minimum terms and conditions, discussed in more detail in the Insurance section below.

AUDITORS

SAAMCo

The Court of Appeal decision in *Assetco plc v Grant Thornton UK LLP* was handed down on 28 August 2020 ([2020] EWCA Civ 1151), largely dismissing an appeal by auditors against an order awarding Assetco damages for the negligent audit of its accounts, though it did reduce damages because it found that the judge had erred in disallowing credit for one of AssetCo's share capital raisings.

The Court confirmed that the SAAMCo principle applies to negligent audit cases and it could be used by the Court to determine which losses resulted from the incorrect information as opposed to any loss flowing from entering into the transaction at all. However it was not a "rigid rule of law" but a tool of analysis and if the facts of the case are such that the application of SAAMCo was incapable of reaching such a determination, it would not be used.

Application of the principle to this case did not assist the auditor because the damages would not have been suffered if the audit opinion had been true. In relation to the loss of chance arguments, where the loss claimed depends on the hypothetical actions of a third party, the claimant must prove on the balance of probabilities what it would have done but need only show that there was a real or substantial chance of any necessary action by the third party. The court then evaluates the lost chance as part of the assessment of damages. The Court of Appeal held that there was no basis on which to interfere with the Judge's findings at first instance, noting its reluctance to do so given the extensive evidence the Judge had read and heard.

Another case looking at SAAMCo, *Manchester Building Society v Grant Thornton UK LLP* [2019] EWCA Civ 40, in which the Court concluded that an auditor which had given incorrect information concerning the accounting treatment of long-term interest rate swaps was not liable for the losses suffered on closing the swaps early (as the losses would have occurred even if the information had been correct), is currently under appeal. The hearing was heard on 14-15 October 2020 and judgment is awaited. The specific issue under appeal is whether the Court of Appeal was right to hold that the break costs claimed by MBS fell outside the scope of the auditor's duty of care as professional accountants.

Pre-action disclosure

In June 2020, the judgment in *Carillion Plc (in liquidation) v KPMG LLP & Anor* [2020] EWHC 1416 (Comm) provided welcome confirmation of the position that pre-action disclosure orders are not the norm in the Commercial Court and pre-action disclosure applications should only succeed if there are grounds for distinguishing a case from the "usual run".

Read our full briefing here.

Costs – "Arkin cap"

The Court of Appeal handed down its judgment in February 2020 in *ChapelGate Credit Opportunity Master Fund Ltd -v- Money & others*. The Court of Appeal has upheld the decision of the High Court not to limit a commercial funder's liability for payment of the costs of the successful BDO administrators to the extent of the funding provided. Our view is that the decision helpfully clarifies that the Arkin cap is only guidance and not a rigid rule.

Whilst the Court of Appeal has said that the cap might still be appropriate on the facts of some cases, it is nevertheless clear that the Court considered that the litigation funding market had moved on from the early days when Arkin itself was decided, such that there was a less obvious case for protecting successful funders by means of a special cap not otherwise available in litigation.

Read our full briefing here.

CONSTRUCTION PI

Design life

We have written previously about the Supreme Court decision in *MT Højgaard A/S v E.ON Climate & Renewables UK Robin Rigg East Ltd and others* [2017] UKSC 59 (see this briefing). In June 2020, the TCC handed down its decision in *Blackpool Borough Council v Volkerfitzpatrick*, which considered *MT Højgaard* and which provides useful guidance on the meaning of 'design life', an important term deployed in typical construction contracts. For the full briefing, see here.

Assumption of responsibility

Surprising as it may seem, claims are not always brought against the professional by former clients. Professionals can be at risk of assuming duties to others.

In another case on assumption of responsibility, *Valley Brook Investments Ltd and another v Huam Ltd* [2020] EWHC (Ch) 1715, the High Court has held that a professional can owe a duty of care towards a third party (an SPV) who reasonably relies on the professional's work, even where the third party did not exist when the professional supplied its work. In this case, the architect had supplied drawings to the client and later engaged in informal discussions with a potential buyer of the development (the soon to be owner of the SPV) in which it was alleged that the architect stated the development could accommodate 16 units. The architect later supplied drawings to this effect to the buyer. The SPV was incorporated thereafter for the purpose of buying the development and it transpired that the development could not accommodate 16 units. On the evidence, the judge decided in this case that the number of flats which could be created had been discussed with the buyer, and this, taken together with the architect having directly supplied a copy of the drawings to the buyer, led to the conclusion that the architect had assumed responsibility towards the buyer and that there was a reasonable expectation of reliance.

Of note, the professional's contemporaneous documentation was sparse and of little assistance to the judge, emphasising the importance of professionals keeping clear, contemporaneous notes of their dealings, even those that appear informal.

This underlines the need for caution. Is it likely a yet to be incorporated entity will claim reliance on the advice of a solicitor and should the retainer letter be crafted to deal with that possibility?

FINANCIAL INSTITUTIONS AND D&O

Reflective loss

In July 2020, the Supreme Court handed down its landmark judgment in *Sevilleja v Marex Financial Ltd* [2020] UKSC 31, confirming that the rule in *Prudential* still stands (i.e. that where a shareholder has suffered loss in the form of a reduction in the value of its shares or a reduction in distributions, the shareholder is precluded from bringing a claim against a defendant where the company has also suffered loss and has a parallel claim against that defendant) but it does not preclude a creditor, or a shareholder claiming to have suffered losses separate and distinct from those of the company, from pursuing the wrongdoer independently from the company. As such, there was a narrowing by the Supreme Court of the application of the so-called rule against the recovery of "reflective" losses, overruling a number of cases which had applied *Prudential* more widely.

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In the first judgment to consider *Marex*, the High Court in *Broadcasting Investment Group Ltd v Adam Smith* [2020] EWHC 2501 (Ch), applied the principles laid down in *Marex*, finding that the shareholder's claims were reflective of the company's losses and, thus, were to be struck out. However, the claim by the individual, who was a second - or further - degree shareholder, was not struck out as *Marex* had made it clear that the rule only bars claims by shareholders in the loss-suffering company itself.

This case clearly impacts financial institutions. Whether it troubles legal professionals remains to be seen; but it does expose professionals to a potentially wider group of aspirant claimants.

For more information on these two cases, please see our full briefings: *Broadcasting Investment Group Ltd v Adam Smith* and *Sevilleja v Marex*.

In October 2020 there was another case which considered *Marex*: *Naibu Global International Co Plc (2) Naibu (HK) International Investment Ltd v (1) Daniel Stewart & Co Plc (2) Pinsent Masons LLP* [2020] EWHC 2719 (Ch). There was a Chinese sportswear company. Its parent company (C2) and the holding company (C1) of the parent held shares in the Chinese company. The assets in the Chinese company had been dissipated, leaving the shares valueless. Following this, C1 was delisted from AIM and C1 and C2 subsequently brought proceedings against their lawyers alleging they were negligent in their due diligence when they prepared the holding company for flotation on AIM.

The lawyers sought to strike out the holding company's claim on a few bases. One of these was that its loss was almost entirely reflective of the losses claimed by C2 and was therefore irrecoverable under the rule against recovery of reflective losses. The court agreed, finding that the loss was entirely composed of the diminution in the value of its shareholding in C2. Mrs Justice Bacon described the case as a "*paradigm*" example of a claim barred by the reflective loss principle as confirmed in *Marex* and confirmed that it was essential to look at the nature of the shareholder's loss.

SIPPs

In the long-awaited judgment in *Adams v Carey Pensions* [2020] EWHC 1229 (Ch), handed down on 18 May 2020, Mr Justice Dight held that the claim failed on each of the three heads and therefore dismissed the claim against Carey Pensions (the Defendant).

The judgment brings much needed guidance as to (1) what a Self-Invested Personal Pension (SIPP) provider is responsible for when acting on an execution-only basis (2) the boundary of Rule 2.1.1 of the Conduct of Business Sourcebook Rules (COBS) and (3) the application of section 27 Financial Services and Markets Act 2000 (FSMA). Given the number of complaints and claims outstanding against SIPP providers, which are similar to the *Carey* claim, this judgment will give cause for optimism to SIPP providers although the precise facts in each case will still need to be carefully considered. Note that the hearing of the appeal in the Court of Appeal is to commence on 2 March 2021. Read the full article here.

Quincecare duty

Having not been considered in the space of 25 years since it was originally coined in the 1992 case of *Barclays Bank Plc v Quincecare Ltd*, recent years have witnessed a number of cases citing a breach of the so-called "Quincecare duty", starting with the case of *Singularis v Daiwa*. The duty is defined as a duty for the financial institution to protect its customer from itself where circumstances are such so as to put the bank on inquiry that there may be fraud on the account.

On 30 October 2019, the Supreme Court handed down its judgment in *Singularis* ([2019] UKSC 50), unanimously dismissing Daiwa's appeal. It upheld the High Court judgment that Daiwa (the bank) owed the Quincecare duty to Singularis (the customer company) not to execute an order if it had been put on inquiry that it was an attempt to misappropriate funds of the customer, and that the bank had breached this duty.

The full article on the case can be found within our Financial Institutions and D&O International Review – November 2019.

The duty was also considered in another case in 2019, *Federal Republic of Nigeria v JP Morgan Chase Bank* [2019] EWHC 347 (Comm), in which the Claimant claimed that the bank had made transfers from its depository account, which it would not have done had it been exercising reasonable care. Nigeria's case was that the bank had breached its Quincecare duty of care. The issue to be decided was whether the duty applied to depository accounts as well as current accounts and the court found that it did and, in doing so, refused the defendant's application for summary judgment. This finding was upheld on appeal (*JP Morgan Chase Bank NA v Federal Republic of Nigeria* [2019] EWCA Civ 1641).

2020 continued the stream of cases. In *Stanford International Bank Ltd (in liquidation) v HSBC Bank plc* [2020] All ER (D) 169 (Jul), the defendant bank sought the striking out of, or summary judgment of, Stanford's claim (brought by liquidators). The liquidators claimed that Stanford had been operated as a Ponzi scheme and that HSBC had acted as correspondent bank for Stanford and had failed, in breach of its Quincecare duty, to take sufficient care to see that the monies that were being paid out from accounts under its control were being properly paid out and not misappropriated.

The defendant denied breach and also asserted that on a net asset basis, Stanford was in an equal position and had not suffered any loss. The application was dismissed and the claim could proceed. In relation to the Quincecare duty, noting that the duty is owed to the company and not to the creditors, the Judge considered that the correct question should be whether the company was worse off by having £118m (the amount paid out in the period in question) wrongfully extracted from its bank accounts and he found that it was, as if the liquidators had that money it could more easily pursue claims. The Judge commented that the loss position was different where the claimant company was insolvent, which may provide further scope in relation to Quincecare duty arguments in future cases. The appeal in this case is due to be heard in November 2021.

The Quincecare duty is also being defined broadly. Despite its origins in deposit taking financial institutions, in *Singularis* it was applied to an investment bank and in the 2020 case of *Hamblin and another v World First Ltd and another* [2020] EWHC 2383 (Comm), the court held that it may also apply to a payment service provider (PSP) who took instructions from a company that was controlled by fraudsters. The court dismissed the application for summary judgment and strikeout, on the grounds that the case had a reasonable chance of success.

Directors' duties

In *Hunt (as Liquidator of System Building Services Group Ltd) v Michie & Ors [*2020] EWHC 54 (Ch), the High Court confirmed that directors continue to owe fiduciary duties post insolvency. This confirmation brings clarity to what is expected from a director of an insolvent company. Directors should therefore not consider themselves “off the hook” once an administration or CVL has been entered into. Directors' roles in pre-pack deals in particular are likely to continue to be an area for scrutiny. Read our full briefing on this case.

CLASS ACTIONS

Following on from the judgment in the Lloyds group action at the end of 2019, there have been some further developments in 2020. The Tesco case settled and the £14bn MasterCard claim has just received the go ahead to be reconsidered for a CPO. In the Tesco case, claims for £100 million were brought against Tesco on behalf of more than 125 institutional funds in relation to Tesco's £263 million over-statements of profits in October 2014, which allegedly resulted in a significant fall in its share price. The claims were advanced under s90A FSMA which makes issuers liable for misleading statements or dishonest omissions in published information relating to securities.

The trial was due to take place in October 2020 and was to be the first judicial consideration of s.90A but shortly before the trial date, a consent order was filed with the court confirming the case had settled (the details of which are not public).

In relation to the MasterCard claim, on 11 December 2020, the Supreme Court handed down its decision on whether the case can proceed under the Consumer Rights Act 2015 opt-out group action procedure (administered by the Competition Appeal Tribunal (CAT)). For background, in 2016, a former Financial Ombudsman, Walter Merricks CBE, sought to bring a £14bn class action on behalf of 46 million customers before the CAT. The collective proceedings were brought on an opt-out basis and sought an aggregate award of damages, representing the loss suffered by the class as a whole, rather than individual damages. In order for the action to proceed, Mr Merricks had to satisfy the CAT that it was suitable for collective proceedings and obtain a Collective Proceedings Order (CPO). He initially failed and the CAT claimed there was no appeal route provided by the legislation. The Court of Appeal itself claimed it did have jurisdiction to hear the appeal and held that the CAT had applied the test incorrectly and that it must reconsider the case’s suitability for a CPO. MasterCard appealed that decision to the Supreme Court, who heard the appeal in May 2020. The Supreme Court agreed with the Court of Appeal that the CAT’s decision is undermined by error of law and has sent Mr Merricks’ application for a CPO back to the CAT. In particular, the Supreme Court found that the CAT made five errors of law:

1. It failed to recognise that in addition to overcharge, the merchant pass-on issue was also a common issue and should have been a powerful factor in favour of certification.

2. The CAT placed great weight on its decision that the case was not suitable for aggregate damages. Whilst this was a relevant factor to consider, it was not a condition.

3. The CAT judged suitability incorrectly. If the forensic difficulties would not have prevented an individual claim from proceedings then it should not be the reason to deny certification for collective proceedings.

4. The CAT was wrong to consider that difficulties with incomplete data and interpreting the data are a good reason to refuse certification. This problem is often faced by courts.

5. The CAT was wrong to require Mr Merricks' proposed method of distributing aggregate damages to take account of the loss suffered by each class member. The Consumer Rights Act expressly modifies the ordinary requirement for the separate assessment of each claimant's loss.

There are also a number of other large claims underway using the procedure (for example, relating to forex fixing), many of which were hinging on the outcome in the MasterCard case so we can expect those claims to proceed in earnest now.

INSURANCE

Braganza duty

It was held in the 2001 case of *Gan Insurance v Tai Ping (Nos 2 and 3)* [2001] Lloyd's Rep IR 667 that an (re)insurer, when exercising its rights under the policy (in that case, under a claims control clause), should not act arbitrarily or take into account irrelevant matters. This "duty of rationality" was later expressed in the 2015 case of *Braganza v BP Shipping Ltd* [2015] UKSC 17 to arise where:

The contract affords a decision-making power to one party;

The exercise of that power affects both parties' rights under the contract; and

The decision-making party has a clear conflict of interest in the making of the decision.

This duty is now known as the "Braganza duty". For the court to assess what is a rational consideration, it will consider the "Wednesbury principles" established in the decision in *Associated Provincial Picture Houses Ltd v Wednesbury Corporation* [1948] 1 KB 223, whereby the court looks at whether the person making the decision asked the right questions and took the right matters into account and avoided a result so outrageous that no reasonable decision-maker could have reached it.

In the 2020 case of *UK Acorn Finance Ltd v Markel (UK) Ltd* [2020] EWHC 922 (Comm), the High Court confirmed that the Braganza duty applies to innocent non-disclosure clauses which require the insurer to exercise discretion. The claimant lender had sought an indemnity, under the Third Parties (Rights Against Insurers) Act 1930, from the defendant professional indemnity insurers in relation to two judgments it had obtained against the now insolvent insured surveyor. The policies contained an unintentional non-disclosure clause (UND clause) which read: *"In the event of non-disclosure or misrepresentation of information to us, we will waive our rights to avoid this Insuring Clause provided that…you are able to establish to our satisfaction that such non-disclosure or misrepresentation was innocent and free from any fraudulent conduct or intent to deceive."*

The court found that the insured had made a false representation in relation to who it undertook work for and the representations were warranties (there had been a basis of contract clause) which entitled the insurers to avoid the policies, subject to the application of the UND clause. Applying the Braganza duty, the court held that the insurers had failed to take into account only relevant matters and exclude irrelevant considerations. In particular, insurers had approached the issue from a position that the insured was dishonest, rather than with a more open mind that the more probable outcome was that the disclosure was innocent or negligent. Further, it was clear that the insurers generally did not trust the insured's systems or the way it did business. Whilst these may have suggested the potential for wrongdoing, they were not evidence of fraud and were taken too greatly into account. As a result, the court held that the decision to avoid was not a proper outcome.

This case is also a rare example of how to interpret a UND clause.

Non-disclosure

Whilst *Niramax Group Ltd v Zurich Insurance plc* [2020] EWHC 535 was decided under the old law (i.e. sections 18-20 Marine Insurance Act 1906), it provides useful commentary on how the court may look at non-disclosure points if an insurer argues that it was not given a fair presentation of the risk under the Insurance Act 2015 and, thus, should be entitled to avoid or seek a proportionate remedy.

Niramax had taken out policies with the insurer to cover its plant and machinery, along with buildings insurance (with another insurer) which required, inter alia, fire suppression measures and the installation of CCTV. These requirements were not met, resulting in special terms coming into effect. Upon renewal of the plant and machinery policy (in December 2014), the company failed to disclose those failures to comply. The next year, new machinery (the Eggersmann plant) was added to the plant and machinery policy and, shortly thereafter, a fire occurred destroying the new machinery. Niramax sought an indemnity of £4.5 million but the insurer sought to avoid the policy, arguing that Niramax had failed to disclose material circumstances, which it claimed, had hey been disclosed, would have resulted in the decision as to whether to provide cover being referred to a senior underwriter, whereupon the risk would have been refused.

Under section 18(2*), "Every circumstance is material which would influence the judgment of a prudent insurer in fixing the premium, or determining whether he will take the risk".* The burden of proof in this regard lies with the insurer. When looking at the matters in question in this case, the Judge stated: *"failure to comply with risk requirements, and the imposition of these special terms, in these circumstances, was material because absent "active engagement" it manifested an attitude to compliance which was relevant to the risk."*

Turning to inducement, the Judge scrutinised the evidence of the witnesses, acknowledging the risk of accepting evidence about what someone would have done in a hypothetical situation. The seniority of the various employees and how they interacted with each other on out of the ordinary risks, meant that the Judge was satisfied that had the matters been disclosed, they would have been referred up to a more senior employee. She was also satisfied that that senior employee, if he had been presented with this information, *"would have reluctantly offered renewal terms in December 2014 [given the longstanding relationship with the insured] but would have refused the extension to cover the Eggersmann plant in September 2015."* This was on the basis of the underwriter's evidence but also upon scrutiny of the insurer's stated risk appetite for waste risks (guidance had been issued in July 2013 against insuring "fixed plants on waste risks") and the, no doubt, increased exposure the insurer faced upon accepting the new machinery on risk (due to its lack of mobility).

As such, the court held that the insurer was entitled to avoid the extension of the policy.

How the Judge approached the issue may be instructive for cases brought under the Insurance Act 2015 where, in the event of challenge, insurers can expect their underwriting processes, published guidance, interaction with colleagues and personalities of each to be closely examined in order to determine what would have happened had there been a fair presentation of the risk.

Contractual interpretation and notification language

Whilst not an insurance case, *Towergate Financial (Group) Ltd & Ors v Hopkinson & Ors* [2020] EWHC 984 (Comm), provides useful commentary on contractual interpretation, confirming, citing the established cases on contractual interpretation, (i) *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50, [2011] 1 WLR 2900; (ii) *Arnold v Britton* [2015] UKSC 36, [2015] AC 1619; and (iii) *Wood v Capita Insurance Services Ltd* [2017] UKSC 24, that the language of the clause should not be divorced from its commercial purpose and its context and, in any event, the clause could easily be interpreted from a simple linguistic reading.

Notice in this case was supposed to be given "as soon as possible". The court refrained from saying when notice should have been given but said that waiting for two years was plainly not "as soon as possible".

Aggregation

Notwithstanding the House of Lords decision in *Lloyds TSB*, which was seen at the time as providing significant clarification, aggregation remains the cause of regular disputes. As the case of *Baines and others v Dixon Coles and Gill (A Firm)* EWHC 2809 (Ch) again demonstrates, each claim will turn upon its facts and the interpretation of the clause can cut both ways – for example, it may be in an insured firm's favour if it means just one retention is payable for multiple claims, but, alternatively, if the claims do not aggregate they may be able to benefit from a limit "per claim" (up to any aggregate limit). In this case, the interpretation favoured the law firm (and the underlying claimants) who now have a per claim limit of £2m. Further, the Court's analysis of the aggregation clause in the MTC is of interest, especially that the thefts were the relevant "acts" and the dishonesty of Mrs Box, and the way she perpetrated the various misappropriations, could not act as the unifying factor to allow the claims to be aggregated. The full article can be read here.

PRIVILEGE

Legal Advice Privilege - dominant purpose test

In an important decision in January 2020, *The Civil Aviation Authority v. R (Jet2.com Limited) Authority* [2020] EWCA Civ 35, the Court of Appeal confirmed that the dominant purpose test, long understood to be part of the test for litigation privilege, also applies to legal advice privilege. In order to be protected by legal advice privilege, a communication must have been brought into existence for the *dominant* purpose of giving or getting legal advice.

The Court also provided guidance on the circumstances in which multi-purpose/multi-addressee communications (in practice, usually emails) copied to both lawyers and non-lawyers could attract legal advice privilege, which will depend, in summary, on whether the dominant purpose of the communication (or series of communications of which it forms part) is to obtain legal advice or commercial views.

The Court further held that it was correct to consider emails and attachments separately for the purposes of identifying documents that are protected by legal advice privilege.

The decision also contains helpful guidance on waiver of privilege, and observations on the difficulties that have been created by the narrow definition of the "client" in *Three Rivers (No 5)* [2003] EWCA Civ 474. For our full article see here.

As an aside, the recent case of *The Financial Reporting Council Ltd -v- Frasers Group Plc* (formerly Sports Direct International Plc) [2020] EWHC 2607 (October 2020) applied the dominant purpose test in the context of litigation privilege and underscored the need for a nexus between the purpose of the document over which privilege is claimed and the issues in the litigation reasonably in contemplation at the relevant time, as further discussed in our note here.

Foreign Lawyers

PJSC Tatneft -v- Bogolyubov & Others [2020] EWHC 2437 (Comm), in September 2020, provided welcome clarity as to the scope of English legal advice privilege as it relates to communications between foreign lawyers (including in-house lawyers) and their clients. The Court held that such communications can be privileged if the lawyer is acting *"in the capacity or function of a lawyer"*, irrespective of the particular standards of qualification or regulation which apply to the lawyer under local law (into which the Court will not enquire). Our article on this decision can be found here.

Exceptions to privilege

An important judgment in February 2020 (*Sports Direct International plc v The Financial Reporting Council* [2020] EWCA Civ 177) saw the Court of Appeal confirm that the only exceptions to the absolute nature of legal professional privilege were (i) in cases of fraud/iniquity and (ii) where there was an express or necessarily implied statutory override.

The case concerned an investigation by FRC into Grant Thornton in relation to its audit of the financial statements of Sports Direct. The FRC issued several statutory notices to Sports Direct, seeking material relating to the audit. Sports Direct argued the documents were protected by privilege.

The Court rejected the FRC's arguments that there were additional exceptions which applied where a regulator, such as the SRA or the FRC, requested documents in certain circumstances. It did not accept, as some previous cases had suggested, that there was no infringement of the privilege of clients of the regulated person in those circumstances (the so-called "no infringement exception") or a mere technical infringement, which was regarded as authorised by implying statutory override of the privilege to a lower threshold than usually applied (the so-called "technical infringement exception").

The Court also held that emails and their attachments should be considered separately for privilege purposes. So non-privileged documents attached to privileged emails were disclosable - even if those (non-privileged) documents only fell within the criteria for disclosure because they were attached to (privileged) emails that did so. Sports Direct has applied for permission to appeal this aspect of the Judgment to the Supreme Court and the outcome of that application is awaited. Our briefing on the case can be found here.

Fraud exception to privilege

Legal professional privilege does not attach to communications between a lawyer and a client if the lawyer is instructed for the purpose of furthering crime, fraud or iniquity.

Addlesee v. Dentons Europe LLP [2020] EWHC 238 (Ch) confirmed in March 2020 that the fraud exception applies where the challenging party can establish a strong prima facie case that that was the purpose of the lawyer's instruction and it does not matter if the solicitor is not aware of the wrongful purpose.

Barrowfen Properties v Patel [2020] EWHC 2536 (Ch) held in September 2020 that the fraud exception extended to breaches of a director's statutory duty. Accordingly, a company which satisfied the court that there was a strong prima facie case that its former director had breached his statutory duties was entitled to disclosure and production of privileged documents created by solicitors who had advised the company and the director under a joint retainer.

Loss of Confidentiality and therefore Privilege

We have seen a number of decisions this year in which the Courts rejected challenges to the privileged status of certain documents made on the basis of loss of confidentiality (confidentiality of course being an essential element of both legal advice and litigation privilege).

In *Raiffeisen Bank International AG v Asia Coal Energy Ventures Ltd & Anor* [2020] EWCA Civ 11 (January 2020), the Court of Appeal held that confidentiality and legal advice privilege are not lost in documents containing or evidencing a client's instructions to its solicitor just because the solicitor makes a statement to a third party as to and pursuant to those instructions.

In that case, the Bank sought disclosure of documents containing the instructions that a law firm had received from their client. The Bank asserted that those instructions were not confidential (and therefore not privileged) because the client had authorised the solicitors to give a written confirmation which referred expressly to them. The Court of Appeal disagreed and said that *"a statement by a solicitor to a third party as to the instructions he has from his client does not automatically and without more give rise to a loss of confidentiality in the documents which contain or evidence those instructions".* Further, it *"is by no means uncommon for solicitors to make such statements and it would be surprising if, by their doing so, privilege in their underlying instructions was lost".* Our briefing on the case is here.

In *SL Claimants v Tesco plc; MLB Claimants v Tesco plc* [2019] EWHC 3315 (Ch) (February 2020), the High Court considered the threshold for retaining confidentiality in respect of privileged documents deployed in parallel proceedings.

Here, the Claimants sought disclosure of a privileged attendance note from the Defendant. The Claimants said it was no longer confidential (and not, therefore, privileged) because it had been disclosed to the SFO under limited waiver in related criminal proceedings and referred to/read from to some extent in open court in the course of those proceedings. The Judge held that confidentiality was not lost in this instance as the references to some of the information in the document on these facts did not constitute *"sufficient exposure of the document to the public"*; however, this will be a matter of fact and degree on a case-by-case basis. Further the principle of open justice was also separately capable of extinguishing confidentiality, even where confidentiality was not lost by the extent of the exposure. Our fuller note considering this case and its implications for professionals can be found here.

Waiver of privilege

In a significant decision, *PCP Capital Partners LLP v. Barclays Bank plc* [2020] EWHC 1393 (Comm) (June 2020), the Court refined the test to be applied when determining whether reference to privileged material (there to legal advice in witness statements and opening submissions) amounted to a waiver of privilege. The Court said that the traditional distinction that reference to the *content* of privileged material amounted to a waiver, whereas a reference merely to its *effect* did not, should not be applied mechanistically. Rather, the Court should consider (1) whether there was reliance on the privileged material referred to and (2) the purpose of that reliance (i.e. was it to support or advance the party's case on an issue on which the Court must decide?) and (3) the particular context of the case in question.

The Judgment went on to underscore the risk, in the event of a waiver being found, of the Court finding the collateral waiver of privilege in all other material which forms part of the same "transaction" or issue if fairness requires it (see also *Jet2* above). See our full article on the case here.

Our article above refers also to the judgment, in April 2020, in *TMO Renewables -v- (1) Desmond George Reeves (2) Maxwell Charles Audley* [2020] EWHC 789 (Ch). In that case, no waiver was found because the reference to privileged material was relevant to the merits of the case, but was made in the context of a security for costs application which would not consider the merits. Accordingly, there was no reliance on the privileged material in support of an issue then before the Court. See our full article here.

Disputes where there has been a limited waiver

A v B and FRC [2020] EWHC 1491 (Ch) (June 2020) concerns a dispute which arose in the context of a request by the FRC for documents from auditors belonging to its client. The client considered the documents privileged (and provided them to the auditors on a limited waiver basis) but the auditors disagreed. The Court considered the correct mechanism for resolving such disputes, as discussed in our full article here.