CLIFFORD
CHANCE

Newsletter June 2014

# Contentious Commentary

*Contract*

## Collateral benefits

**Whether benefits gained by the innocent party following a breach of contract reduce damages is a complicated area.**

A charterer repudiates a charterparty by redelivering the vessel two years early. There is no market for that kind of vessel, so the owner sells it for $23.8m. The owner claims from the charterer the lost income for the two year period (giving credit for the lack of need to service the vessel). A pretty straightforward claim. But at the end of the two year period, the vessel would only have been worth $7m because of the effect of the financial crash. Does the owner have to give credit against the damages for the fortuitous "profit" made on the early sale of the vessel?

In *Fulton Shipping Inc v Globalia Business Travel SAU* [2014] EWHC 1547 (Comm), Popplewell J toured around numerous cases relevant to the issue before concluding that the "search for a single general rule which determines when a wrongdoer obtains credit for a benefit received following his breach of contract or duty is elusive". Some judges have treated the issue as one of causation, others as the cost of steps taken in mitigation, and others still as public policy. All very difficult for a first instance judge to reconcile.

Nevertheless, Popplewell J decided that the outcome shouldn't be affected by whether the issue was analysed as one of causation or of mitigation. There must be a causal link between the benefit and the breach, which, as ever, is to be derived from taking into account all the circumstances. The causal link will not be there if the breach merely provided the occasion for the innocent party to obtain the benefit, even if it flowed from a reasonable decision made after breach (eg it was a benefit that the innocent party could have obtained even if the breach had not occurred). The benefit does not, however, have to be of the same kind as the loss suffered (here, income or capital), though the fact that it is not of the same kind might indicate that it is not causally connected to the breach.

Applying this, the judge decided that the benefit from the early sale did not have to be brought into account in calculating damages. The breach of contract was the occasion or context for the sale of the vessel, but the owner could have sold the vessel at any time. There was insufficient causal link between the breach and the sale, nor was the sale in mitigation of damages (except insofar as it removed the cost of operating or laying up the vessel). In general, however, it is all very fact specific.

## To speak or not to speak

**There can be a duty to point out areas of dispute.**

If a contractual party puts to the other its view as to a certain matter arising under the contract, is the recipient bound to disclose that it might wish to dispute that view? If it doesn't, will it be estopped from subsequently challenging the view? *ING Bank NV v Ros Roca SA* [2012] 1 WLR 472 might have suggested that there is a duty to speak, but in *Starbev GP Ltd v Interbrew Central European Holdings BV* [2014] EWHC 1311 (Comm) Blair J restored a bit more order, confining *Ros Roca* to a contract where the parties were engaged in a joint project as business partners (though that may come close to another heresy, the "relational" contract as a separate category of contracts).

Blair J said that it must be unconscionable for a party to resile from a convention established between that party and the other in order to create an estoppel. Irresponsible behaviour is not enough on its own to render silence unconscionable. It requires some sort of impropriety on the part of the person alleged to have a duty to speak, but impropriety may come from the act of staying silent if a reasonable person would expect someone, acting honestly and responsibly, to bring the true facts to

## Contents

the attention of the other. A trifle circular?

Blair J also concluded that an estoppel could arise not only regarding a fact, but also when there is simply a potential dispute. The bottom line, however, is that if someone asserts a position on which it might act, it is potentially dangerous to allow that person to proceed on that basis without at least flagging a potential disagreement or error, no matter how inconvenient it might be to do so. A cautiously worded reservation will generally be a good idea. But also the bigger the persons involved, and the more serious their advisers, the less likely there is to be an estoppel.

*Tort*

## Saving face

**Someone who supplies information prepared by another can be liable for errors in that information.**

It is common for one person (D) to hand to another person (C) information prepared by a third person (X). In *Webster v Liddington* [2014] EWCA Civ 560, the Court of Appeal explored the liability that D might have for the information, concluding that there are four basic positions:

- D warrants that the information is correct, thereby assuming contractual liability for its accuracy
- D adopts the information as its own, taking on such responsibility as D would have had if it had prepared the information itself
- D represents that it believes, on reasonable grounds, that the information is correct
- D passes on the information to C as material coming from X about which D has no knowledge or belief (and no liability)

There could be intermediate positions, but the test to decide liability in any particular case is what the reasonable person would have understood the position to be in the relevant context. The Court of Appeal cited *IFE Fund SA v Goldman Sachs International* [2007] EWCA Civ 811 as a case in the last category because D had expressly disclaimed any responsibility for the contents.

*Webster* itself was a case where private clinics passed on laboratory brochures concerning treatments supposed to rejuvenate skin. Given the consumer relationship, the imbalance in knowledge between the parties and the fact that the procedure was entirely elective, the Court of Appeal decided that the case fell within the second category, ie the clinics were adopting the contents of the brochures as if they were their own and, accordingly, were liable for misrepresentations in the brochures. If the clinics had wanted to move to the third or fourth categories, they should have issued a disclaimer.

## Liability limited

**A parent company does not owe its subsidiary's employees a duty of care.**

In *Chandler v Cape plc* [2012] 1 WLR 3111, the Court of Appeal decided that a parent company owed a duty of care to its subsidiary's employees regarding the safety of the employees when handling asbestos. The decision arose largely from an understandable sympathy for those employees suffering from health issues caused by the asbestos and who would not otherwise have had a remedy because of the demise of the subsidiary.

The factors the Court of Appeal pointed to in imposing liability on the parent in *Chandler* were that the parent and subsidiary carried on the same business, that the parent had superior knowledge of health and safety, that the subsidiary's work system was unsafe as the parent knew or ought to have known, and that the parent ought to have foreseen that the subsidiary's employees would rely on the parent using its superior knowledge. As legal reasoning goes, this is thin. On the scanty historical facts available, it really amounts to little more than an assertion that the parent should be, and therefore would be held to be, liable.

In *Thompson v The Renwick Group plc* [2014] EWCA Civ 635, the Court of Appeal declined to push this approach further, despite the case also involving asbestos. All that could really be shown in *Thompson* was that one company was the parent of another and that the parent had appointed the person who ran the subsidiary. This was insufficient to impose liability.

The use by a parent of its voting power as shareholder to appoint a director of a subsidiary does not make the parent liable for the subsidiary's obligations. If it did, separate corporate personality and limited liability would be no more. Absent special factors, a parent is not liable to its subsidiary's employees, and in *Thompson* there was no evidence of any special factors. In truth, there was little evidence at all, not least because the relevant events were some 40 years ago and no records remained.

Tough on the employees, but legally inevitable absent legislative change.

*Courts*

## Hard Prest

**The assets of a wholly-owned company are not caught by a freezing injunction.**

In *Lakatamia Shipping Co Ltd v Nobu Su* [2013] EWHC 1814 (Comm), the judge defied more than a century of legal orthodoxy. Burton J held that if D was subject to a freezing injunction, the assets of a company wholly owned by D were also subject to that freezing injunction. This was impossible to reconcile with the separate corporate personality of the company, only recently reasserted by the Supreme Court in *Prest v Petrodel Resources Ltd* [2013] UKSC 34 (and, indeed, on the same day that Burton J frolicked, upheld by Hildyard J in a case identical to *Lakatamia*: *Group Seven Limited v Allied Investment Corporation Ltd* [2013] EWHC 1509 (Ch)). In *Lakatamia Shipping Co Ltd v Nobu Su* [2014] EWCA Civ 636, the Court of Appeal (featuring two-thirds of the panel from *Thompson v The Renwick Group Ltd*, above) rejected Burton J's first instance conclusion, recognising that, since at least *Salomon v A Salomon and Co Ltd* [1897] AC 22, the assets of a company are just that and, in particular, are not the assets of the company's shareholders, even its sole shareholder.

But although the Court of Appeal condemned Burton J's reasoning, they did not overturn his decision. The assets of the company in question might not be assets of D, but D's shares in the company were his assets and were therefore subject to the freezing injunction. Any conduct by D that diminished the value of his shares would infringe the freezing injunction. If the company carried on business in the ordinary course, that would not cause a problem because the company would be seeking to make a profit and thereby to increase the value of its shares. But if, as was the case, the company was suspected of transactions outside the ordinary course that would reduce the value of the shares, any involvement by D in those transactions would be contempt of court. And since the company was wholly owned by D, it was difficult to conceive that the company would have reduced its value without D's involvement.

*Restitution*

## Tracer bullets

**The route of tracing need not be clearly established.**

The ability to trace property does not in itself provide a claim. Tracing identifies what has happened to property through a series of substitutions. Once the final destination of the property is known, it is then necessary to assert a claim against the holder of the property (for example, liability as a knowing receipt constructive trustee). Tracing commonly involves bank accounts. *Relfo Limited v Varsani* [2014] EWCA Civ 360 shows that the courts will not necessarily demand strict evidence of all the stages of the tracing or even that substitution takes place in chronological order. It always helps, of course, if the movement of money is clearly fraudulent.

*Relfo* involved a payment made from C's bank account to an account in Latvia in the name of M. On the same day, an equivalent sum, less bank charges and a 1.3% "money laundering charge" (according to Floyd LJ), was paid to D from T's account at a different bank, this time in Lithuania. The link between the money in the Latvian and Lithuanian accounts was not, it seems, established; the money in T's Lithuanian account at the time of payment to D did not include the monies paid to M's account. Was this enough to establish that C's money had reached D?

The Court of Appeal considered that the links between M, T and D were sufficient to allow it to conclude that D had received C's money and, as a result, that C could recover that money under a knowing receipt constructive trust. The intention of the person behind a fraudulent scheme is not on its own enough to establish tracing, but it is relevant when filling evidential gaps. Nor was the fact that C's money can only have reached T after T had paid D enough to prevent tracing; reimbursement suffices as long as the payment is made in reliance on subsequent payment. So the Court of Appeal concluded that D must have received C's money since the whole scheme was concocted for that purpose.

C would also have won in unjust enrichment even if it had not been possible to trace C's money into D's hands. The principal issue was whether unjust enrichment is only available if D is enriched directly at C's expense or whether D's being enriched indirectly at C's expense is sufficient. The Court of Appeal accepted that the general rule requires that D receive a benefit directly from C rather than via a third party, but it is a rule with a significant number of ad hoc exceptions. The Court of Appeal declined to lay down any general principle, or even any general exception, but, following *Menelaou v Bank of Cyprus UK Ltd* [2013] EWCA Civ 1960, decided that one exception is where the "economic reality" is that the benefit conferred on D has come from C. Echoing its conclusions on tracing, the Court of Appeal decided that the causal connections between the various payments allowed the conclusion that D had been enriched at C's expense. Again, fraud helps.

The standard freezing injunction states that defendants must not "dispose of, deal with or diminish the value of any of their assets". The Court of Appeal's conclusion is that a director subject to a freezing injunction can, as director, dispose of or deal with the company's assets with impunity, but if the director is involved in conduct that diminishes the value of the shares of the company, the director will be in contempt of court. Though orthodox, this will often be a fine distinction to navigate.

The alternative recognized by the Court of Appeal is to try to subject the company's assets to the freezing injunction under the so-called *Chabra* jurisdiction even though there is no cause of action against the company. But that is anything but easy.

## Undertakers' duties

**Damages awarded on the undertaking in damages are contractual in nature.**

In order to obtain an interim injunction, it is necessary to give an undertaking in damages, that is to undertake to comply with any order the court may make "if the court later finds that this order has caused loss to the Respondent and decides the said Respondent should be compensated for that loss." The undertaking is given to the court, not to the subject of the injunction, and the court has a discretion whether or not to make an order. If the court makes an order, it is contempt of court not to pay the sum in question.

The starting point is invariably that the interim injunction should not have been granted, demonstrated by its having been overturned at the interim stage or the claimant ultimately failing in the action. In those circumstances, the injunctee can generally expect the court to order an enquiry as to the losses it has suffered which the claimant should meet. But how are those losses to be assessed?

In *Hone v Abbey Forwarding Limited* [2014] EWCA Civ 711, the Court of Appeal was clear that the approach to assessment is, by analogy, contractual, in line with *Hadley v Baxendale* (1854) 9 Ex 341. The Court of Appeal rejected a number of recent first instance judicial doubts about whether this approach was satisfactory. Losses recoverable on the undertaking in damages are those that the claimant should have foreseen at the time the order was made or which arise from special circumstances known to the claimant. But the court may be a bit more generous at the without notice stage, and the injunctee's position may also be improved if it asks for permission to carry out certain transactions whilst the injunction is in force. Refusal by a claimant could increase any damages.

The Court of Appeal even decided that the injunctee can recover general damages, without proof of actual loss. These will be pretty low, but recognise that (in *Hone*) the grant of a freezing injunction is a severe invasion upon the liberty of the individual to deal with assets as he or she sees fit, and that it is bound to have a profound effect on daily life. In this, the Court of Appeal was highly critical of C's solicitors' correspondence - "wrong in principle", "seriously misplaced", imprudently and intemperately worded", "over-aggressively expressed" and "objectionable and misconceived". Any correspondence that might be put before a court needs to be the very soul of moderation; any intemperate rejection of requests risks increasing damages if the case fails.

## Collateral damage

**The court should only allow the use for other purposes of documents disclosed in proceedings if there are cogent and persuasive reasons.**

Documents disclosed in proceedings may only be used for the purposes of those proceedings unless the document has been referred to at a public hearing, the party who disclosed the document and the person to whom the document belongs consent, or the court gives permission (CPR 31.22). In *Tchenguiz v Director of the Serious Fraud Office* [2014] EWHC 1315 (Comm), Eder J decided that seeking advice from a criminal lawyer as to whether disclosed documents revealed criminal conduct was using the documents for a purpose outside the proceedings. Permission was therefore required.

Eder J recognised that, logically, this meant that if the lawyers acting on the case considered whether the documents revealed criminal activity, that too could infringe CPR 31.22; such consideration has nothing to do with the proceedings themselves. Despite logic, Eder J felt that a line could be drawn between the two; going to outside criminal counsel was somehow different from the lawyers already on the case considering the impact of the documents on extraneous matters. But there could be something to argue about in future, though in practice, consideration by the lawyers on the case will seldom be discovered unless they actually do something extraneous with the documents, for which permission will unquestionably be required.

Having decided that permission was required to send the papers to criminal counsel, Eder J then granted permission. He accepted that the burden of proof lies on the person

seeking permission and that this person must show cogent and persuasive reasons, amounting to special circumstances, why any document should be released. But here the proposed course of conduct was limited: seeking advice from a lawyer rather than actually deploying the documents in criminal proceedings. Further, parties should not generally be hampered from obtaining legal advice, and the advice sought related to potentially serious criminal offences.

*Tchenguiz* is the latest of numerous decisions in C's campaign against the Serious Fraud Office following C's arrest for Icelandic-related offences. The arrest warrant, which was later set aside, was based on information provided to the SFO by accountants. C will be taking criminal advice on whether the accountants made false and misleading statements to the SFO when providing information pursuant to section 2 of the Criminal Justice Act 1987 which could amount to a criminal offence under section 2(14), whether the accountants made false allegations of criminal fraud to the SFO that could amount to perverting the course of justice, whether the SFO's providing information to the accountants in exchange for information from the accountants constituted offences under the Bribery Act 2010, and whether the SFO committed perjury. The SFO argued that this was all merely intended to put the frighteners on the SFO's witnesses before the trial, due in the Autumn, but Eder J did not consider that sufficient reason to refuse permission.

## Just in time

**An application for an extension of time made before expiry of the period is not an application for relief from sanctions.**

In *Hallam Estates Ltd v Baker* [2014] EWCA Civ 661, the Court of Appeal declined to extend the rigour of *Mitchell v News Group Newspapers Ltd* [2013] EWCA Civ 1537 to an application for an extension of time filed before expiry of the period, even if the application is heard after. The Court of Appeal said that the overriding objective, with its new stress on "enforcing compliance with rules, practice directions and orders" (CPR 1.1(2)(f)) does not require "the courts to refuse reasonable extensions of time, which neither imperil hearing dates nor otherwise disrupt the proceedings". Indeed, the court would rather that the parties dealt with such matters themselves without bothering the judiciary.

This means that if an application for an extension of time is made before the time expires, the court can look at the matter in the round, considering, in particular, whether the extension has any effect on the action. If the application is made after the time has expired, the court must ask whether the breach is trivial; if not, the extension will be refused absent a good explanation for the delay. Whethe this creates a logical or sensible structure is less clear. An application for an extension of time filed one day after expiry of the period in question is subject to *Mitchell*; an identical application filed on the previous day is not subject to *Mitchell* even if the two applications are heard by the same court on the same day.

*Groarke v Fontaine* [2014] EWHC 1676 (QB) is similar to *Hallam Estates*. An application by D to plead contributory negligence formally was made at the start of the trial but refused even though it would not have required an adjournment of the trial (and the trial judge felt able to say that he would have reduced damages by one-third for contributory negligence had he allowed the amendment). The judge hearing the appeal overturned the decision. He paid due homage to the need for efficiency in the conduct of litigation, but focused on the prejudice to C of allowing the late amendment. He could find none. He didn't think efficiency would be enhanced by requiring D to sue his lawyers. The judge did not think that discipline for discipline's sake was a sufficient reason. So, balancing the interests of the parties, he allowed the appeal, just as he would have done in the pre-*Mitchell* days.

In June 2014, the Court of Appeal, led by the Master of the Rolls, is to hear together appeals in three cases concerning relief from sanctions, and has invited the Law Society and the Bar Council to make submissions on the general impact of *Mitchell*. Second thoughts, or sterner still and sterner?

*Immunity*

## Diplomatic language

**Documents published by Wikileaks are admissible.**

In the *Spycatcher* saga of the 1980s, the courts prevented publication in England of Peter Wright's book about spies within, and misdeeds by, MI5 even though the book's content was known throughout the world (the book was even published in Scotland). Then, somewhat belatedly, the courts realised that, while England might have an insular approach to many things, it couldn't be treated as an island in the sea of information. The only effect of banning publication in England of what was already well-known was to make the courts look foolish. The injunction was lifted.

CLIFFORD CHANCE

Similar thoughts may have flickered across judicial brows in *R (on the application of Bancoult) v Secretary of State for Foreign & Commonwealth Affairs* [2014] EWCA Civ 708 when faced with documents published by Wikileaks (through the offices of Bradley Manning). Anyone could look at the documents on the internet, but the Government argued they were inadmissible in the English courts because the documents in question originated from the US embassy in London. Under article 24 of the Vienna Convention on Diplomatic Relations (in force in England by virtue of the Diplomatic Privileges Act 1964), the documents of an embassy are "inviolable", which, according to the Divisional Court, meant inadmissible in the English courts.

The Court of Appeal disagreed. Admitting in evidence what was already known to the world for extraneous reasons did not violate the documents of an embassy. Departing from dicta *in Shearson Lehman Brothers Inc v Maclaine Watson & Co Ltd* [1988] 1 WLR 16, the Court of Appeal concluded that inviolability meant that the receiving state could not seize embassy documents but where, as here, neither C nor the Government had anything to do with the release of the documents, their admission in evidence in the English courts would not itself violate the embassy's sanctity or impede the proper functioning of the mission.

This decision was insufficient to change the substantive outcome of the case, which concerned the validity of the creation of a marine protected area around the Chagos Islands (and, in particular, the US base on Diego Garcia). This was one of David Miliband's final acts as Foreign Secretary, done against the advice of FCO officials. The Court of Appeal decided that even if the Divisional Court had admitted properly the US embassy documents, which recounted discussions between FCO staff and US diplomats and indicated that the reason for the MPA was to prevent the Chagos Islanders returning to their former homes, it would not have resulted in the order setting up the MPA being overturned.

Clifford Chance acts for the Chagos Islanders.

*Contentious Commentary* is a review of legal developments for litigators

## Contacts

**Simon James**
Partner

T: +44 20 7006 8405
E: simon.james
@cliffordchance.com

**Anna Kirkpatrick**
Senior PSL

T: +44 20 7006 2069
E: anna.kirkpatrick
@cliffordchance.com

**Susan Poffley**
Senior PSL

T: +44 20 7006 2758
E: susan.poffley
@cliffordchance.com



35245-5-61-v1.0