SAFEWAY STORES LTD v TWIGGER: THE BUCK STOPS HERE

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INTRODUCTION

Follow-on claims by victims of illegal cartels are now a settled feature of the UK competition landscape, but what of a follow-on claim by the cartelist itself? A novel attempt at such a claim was considered by the Court of Appeal in the recent case of *Safeway Stores Ltd v Twigger*.[2] Safeway, the supermarket chain, had admitted its own participation in a cartel, and now wanted to recover the £10.7 million fine imposed on it by the Office of Fair Trading (OFT) from 11 of its former directors and employees who were alleged to have been responsible for getting it into the cartel in the first place. The Court of Appeal unanimously dismissed the claim, holding that it was barred by the principle of public policy encapsulated by the Latin maxim, *ex turpi causa non oritur actio*. Although this is a general principle of English civil law, the three judgments in the Court of Appeal are notable for their focus on the architecture of the Competition Act 1998 (the 1998 Act) and competition policy more generally. This is a case which deserves careful attention from competition practitioners, not only for the outcome itself, but also for its wider implications.

BACKGROUND

The case arose out of the OFT's investigation into exchanges of pricing information among supermarkets and dairies regarding the prices of milk, butter and cheese in 2002–2003. Public sentiment at the time was pressing for the large supermarket chains to leave a larger share of the profits to farmers. This resulted in a number of supermarkets raising the retail price of milk and cheese by a few pence, with the apparent intention that the dairies would each raise the price of the milk they bought from farmers by the same amount.

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2 [2010] EWCA Civ 1472, [2010] All ER (D) 245 (Dec).

In 2007, the OFT issued a statement of objections to a number of supermarkets and dairies, in which it alleged that these exchanges breached Chapter I of the 1998 Act and proposed to impose fines on the companies involved. Several parties to the investigation, including Safeway (which had been taken over by Morrisons in 2004), entered into 'early resolution agreements' (ERAs) with the OFT, a form of settlement under which they admitted liability and agreed to pay a reduced penalty. The ERA between Safeway and the OFT provided for Safeway to pay a fine of £16.5 million, to be reduced by 35% to £10.7 million provided Safeway continued to co-operate with the OFT's investigation.

In September 2008, Safeway brought proceedings in the Commercial Court against 11 of its former directors and employees to recover the amount of the fine and the costs it had incurred during the course of the OFT's investigation. Safeway alleged that the directors and employees, in causing Safeway to breach the 1998 Act, had acted in breach of their employment contracts and/or fiduciary duties, and/or had been negligent.

The defendants applied for the claim to be struck out or summarily dismissed, relying on the public policy defence of *ex turpi causa non oritur actio*. At first instance, the defendants also argued that, as a matter of public policy more generally, fines imposed under the 1998 Act for infringement of the Chapter I prohibition should not be able to be passed on to directors and employees (or rather, to their insurers). The application was dismissed at first instance by Flaux J,[3] but unanimously allowed by the Court of Appeal (Pill, Longmore and Lloyd LJJ).

THE EX TURPI CAUSA DEFENCE

The defence of *ex turpi causa* is a rule that prevents a claimant from using the courts to obtain compensation for loss which he has suffered as a result of his own illegal or immoral act.

The case-law draws a distinction between the 'narrow' and the 'wider' form of the rule. As Lord Hoffmann explained in *Gray v Thames Trains Ltd*:[4]

> 'In its wider form, it is that you cannot recover compensation for loss which you have suffered *in consequence of* your own criminal act. In its narrower and more specific form, it is that you cannot recover for *damage which flows from loss of liberty, a fine or other punishment* lawfully imposed upon you in consequence of your own unlawful act. In such a case it is the law which, as a matter of penal policy, causes the damage and it would be inconsistent for the law to require you to be compensated for that damage.' (emphasis added)

3 *Safeway Stores Ltd v Twigger* [2010] EWHC 11 (Comm), [2010] 3 All ER 577.
4 [2009] UKHL 33, [2009] 3 WLR 167.

The *Safeway* case invoked both forms of the rule. Safeway was seeking to recover both the fine itself (thus engaging the narrow form of the rule) and costs and expenses associated with the OFT investigation (which, as they went beyond the fine itself, were arguably within the scope of the wider form of the rule).

DOES THE DEFENCE APPLY TO COMPETITION INFRINGEMENTS?

The threshold question in any case where the *ex turpi causa* defence is invoked is whether the claimant's conduct is sufficiently serious to engage the defence at all. The paradigm case where the *ex turpi causa* rule applies is one where the claimant is relying on his own criminal conduct. But the scope of the rule is not limited to criminal conduct. Is an infringement of the Chapter I prohibition sufficiently serious?

At first instance, Flaux J held that it was – and this finding was not challenged by Safeway on appeal. He said that anti-competitive acts in breach of the Chapter I prohibition involved the necessary element of 'moral reprehensibility or turpitude' and were sufficiently serious to engage the *ex turpi causa* rule in principle. There were essentially three reasons which pointed to this conclusion. First, it was well established that an agreement made in breach of the Chapter I prohibition or Art 101 TFEU is an illegal agreement and that a party to such an agreement cannot claim damages for loss caused by being a party to the illegal agreement: see, for example, *Courage Ltd v Crehan*.[5] Secondly, although proceedings brought by the OFT in respect of competition infringements are not criminal, this is partly to ensure that domestic law is in line with the approach of the European Commission (the Commission), whose penalties are regarded as 'administrative' in order to avoid the legal and political arguments relating to sovereignty that might arise if the Commission had power to impose criminal sanctions. OFT infringement proceedings had nevertheless been regarded as 'quasi-criminal' in nature: *R (Crest Nicholson plc) v Office of Fair Trading*.[6] Thirdly, the penalty which the OFT may impose for an infringement has many of the characteristics of a fine imposed for commission of a criminal offence: the purpose of the penalty, as with a criminal fine, is stated to be punishment and deterrence rather than compensation; further, as with criminal fines, any penalty is paid into the consolidated fund.

Safeway is therefore authority for the proposition that infringement of the Chapter I prohibition is sufficiently serious to engage the *ex turpi causa* maxim.

The case does not address the status of a breach of the Chapter II prohibition or Art 102 TFEU, ie abuse of a dominant position. However, Flaux J's reasoning can readily be extended

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5 (Case C-453/99) [2001] ECR I-6297.

6 [2009] EWHC 1875 (Admin), [2009] UKCLR 895.

to that situation: there is ample authority for the proposition that a finding of abuse is a serious matter (eg *Chester City Council v Arriva plc*);[7] and fines for abuse of a dominant position have the same quasi-criminal character.

ATTRIBUTION OF COMPETITION INFRINGEMENTS TO UNDERTAKINGS

So the *ex turpi causa* doctrine was in principle engaged. But the heart of the dispute on appeal was whether the doctrine applied in circumstances where an undertaking was rendered liable to a competition fine by virtue of the actions of its directors and employees. Was Safeway itself 'personally responsible' for the infringement (with the result that its claim was barred) or was it merely responsible 'vicariously or under the law of agency' (so that the claim was not barred)?

This distinction was derived from a recent decision of the House of Lords, *Stone & Rolls Ltd (in liquidation) v Moore Stephens (a firm)*.[8] *Stone & Rolls* concerned the application of the *ex turpi causa* defence in the case of a claim by a one-man company which had been created and used by its sole shareholder as a vehicle for fraud. The defendant auditors conceded that the claim would not be barred unless the company was 'personally' liable for the fraud perpetrated at the instance of its owner, as distinct from being conduct for which it was 'vicariously liable or which is otherwise attributed to [it] under the principles of the law of agency'.[9]

A majority of the House of Lords held (by 3 to 2) that the company in *Stone & Rolls*, which was solely owned, controlled and managed by the fraudster, was indeed personally responsible for the fraud, such that its claim was barred by the public policy defence. The issue in *Safeway* was how this analysis should be applied in the more usual case of an undertaking with a plurality of employees, directors and shareholders.

It is an axiomatic principle of English law that a company can only act through human agency. In order to hold companies and undertakings liable for the actions of human beings, it is necessary to develop rules of attribution. In *Meridian Global Funds Management Asia Ltd v Securities Commission*,[10] Lord Hoffmann referred to a company's 'primary' rules of attribution as those found in its constitution, typically the articles of association. These usually confer authority on the board of directors, or the shareholders in general meeting, to make decisions which bind the company.

However, the primary rules of attribution are not enough to enable a company to go out into the world and do business. The company therefore builds upon the primary rules of attribution by using general rules of attribution which are equally available to natural persons, namely, the

[7] [2007] EWHC 1373 (Ch), [2007] All ER (D) 146 (Jun).
[8] [2009] UKHL 39, [2009] 3 WLR 455.
[9] Ibid, para [8], per Lord Phillips of Worth Matravers.
[10] [1995] 2 AC 500, at pp 506–507.

principles of agency. It will appoint servants and agents whose acts, by a combination of the general principles of agency and the company's primary rules of attribution, count as the acts of the company.

Lord Hoffmann left open the possibility that the 'primary' and 'agency' bases of attribution might not always be sufficient to enable one to determine a company's rights and obligations. For example, a rule of law might expressly or by implication exclude attribution on those bases, for example, a requirement that the defendant 'himself' have a particular state of mind. How is such a rule to be applied to a company? Lord Hoffmann's answer was as follows:

> 'One possibility is that the court may come to the conclusion that the rule was not intended to apply to companies at all; for example, a law which created an offence for which the only penalty was community service. Another possibility is that the court might interpret the law as meaning that it could apply to a company only on the basis of its primary rules of attribution, i.e. if the act giving rise to liability was specifically authorised by a resolution of the board or a unanimous agreement of the shareholders. But there will be many cases in which neither of these solutions is satisfactory; in which the court considers that the law was intended to apply to companies and that, although it excluded ordinary vicarious liability, insistence on the primary rules of attribution would in practice defeat that intention. In such a case, the court must fashion a special rule of attribution for the particular substantive rule. This is always a matter of interpretation: given that it was intended to apply to a company, how was it intended to apply? Whose act (or knowledge, or state of mind) was for this purpose intended to count as the act etc of the company? One finds the answer to this question by applying the usual canons of interpretation, taking into account the language of the rule (if it is a statute) and its content and policy.'

These principles have previously been applied in a competition context, but in relation to earlier (now defunct) legislation.[11] The *Safeway* case offered the first opportunity for the courts to examine their application to the provisions of the 1998 Act in any detail.

At first instance,[12] Flaux J held that the basis of Safeway's liability was that the wrongful acts had been committed in its name by the defendants, who as directors and employees were acting in the course of their employment. Accordingly, those acts were to be attributed to Safeway by virtue of the general law of agency, with the consequence that the *ex turpi causa* defence did not bar the claim. Flaux J gave little weight to the submission that the 1998 Act itself made clear that the liability of Safeway, qua undertaking, was personal.

The Court of Appeal took a very different approach, with the central focus being on the architecture of the 1998 Act itself. The starting point, in the judgment of Longmore LJ, was

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11 *Director General of Fair Trading v Pioneer Concrete (UK) Ltd and Another* [1995] 1 AC 456.

12 See n 3, above.

that Safeway's liability under the 1998 Act was not vicarious. This was because s 36 of the 1998 Act imposed liability *only* on the undertaking which infringed the Chapter I prohibition and only if the infringement was committed intentionally or negligently by the undertaking.[13] No one was liable for the penalty imposed by the 1998 Act except the relevant undertaking. Lloyd LJ regarded this as the 'central and decisive point'.[14]

It followed that the undertaking's liability was inherently a 'personal' one. As Longmore LJ stated (at para [23]):

> 'If a penalty is imposed, it will only be because the undertaking itself has intentionally or negligently committed the infringement. In those circumstances it is the undertaking which is personally at fault (there can be no one else who is) and, once the [*ex turpi* causa] maxim is engaged, the undertaking cannot say that it was not personally at fault in order to defeat the application of the maxim. The whole hypothesis of the undertaking's liability is that it is personally at fault.'

Lloyd LJ placed weight on the fact that only the undertaking on which the fine is imposed can bring an appeal against the imposition of a penalty, or its amount, under s 46(3)(i) of the 1998 Act. Section 47(1) of the 1998 Act is clear that third parties cannot appeal against decisions as to the imposition or amount of a penalty.

SAFEWAY WAS NOT A VICTIM OF THE DEFENDANTS' ACTS FOR ATTRIBUTION PURPOSES

Safeway's fallback argument was that the infringing acts of the defendants could not properly be attributed to it for the purposes of the *ex turpi causa* rule, since the defendants were acting against Safeway's interests. This was an attempt to rely on the common law rule named after the case of *Re Hampshire Land Co*,[15] whereby acts of an agent are not to be regarded as attributable to his principal if the acts of the agent were deliberately intended to be in fraud of and cause loss to the principal or, arguably, where the acts were in breach of the agent's duty to the principal.

The Court of Appeal rejected this argument as well. Once it was appreciated that Safeway was personally (not vicariously) liable to pay the penalty under the 1998 Act, Safeway could not invoke the *Hampshire Land* principle. The 1998 Act attributed responsibility for the infringement to Safeway, and the court held that it would be inconsistent with this for Safeway to be able to recover those penalties from the defendants.

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[13] See n 2, above, at para [20].
[14] Ibid, para [36].
[15] [1896] 2 Ch 743.

POLICY CONSIDERATIONS

There is a revealing contrast between the judgments at first instance and on appeal regarding the impact of competition policy on the outcome of the case.

Flaux J adopted a more restrictive approach, taking as his starting point the assumption that, in the absence of clear words, it should be assumed that the 1998 Act was not intended to limit the normal principles of common law governing the *ex turpi causa* doctrine. Flaux J was also unimpressed with the submission that the 1998 Act applies to undertakings and not individuals: in his view, the same could be said of any legislation aimed at regulating companies. Dealing with the argument that it would be contrary to the policy of the 1998 Act for undertakings to be able to pass on the fines imposed on them to their directors and employees, Flaux J said that he regarded it as a 'peculiarly unattractive argument to be run by the very directors and employees whose breaches of duty will have led to the penalty being imposed.' He also dismissed as 'completely illogical' the argument that undertakings would be deterred from breaching the 1998 Act only if they were prevented from suing the individuals who caused the breach.[16]

By contrast, all three judgments in the Court of Appeal indicate a greater focus on the policy of the 1998 Act in the competition sphere, with a particularly strong emphasis on policy in the reasoning of Pill LJ. In his view, the policy of the 1998 Act was to attribute liability to the undertaking and to place the impetus on the undertaking to take preventative measures. The provisions of the 1998 Act were to be contrasted with those in Part 6 of the Enterprise Act 2002, which created a criminal offence of dishonesty on the part of individuals in agreeing to make identified anti-competitive agreements. He stated (at para [44]):

> 'The policy of the 1998 Act is to protect the public and to do so by imposing obligations on the undertaking specifically. The policy of the statute would be undermined if undertakings were able to pass on the liability to their employees, or the employees' D & O insurers. Only if the undertaking itself bears the responsibilities, and meets the consequences of their non-observance, are the public protected. A deterrent effect is contemplated and the obligation to provide effective preventative measures is upon the undertaking itself.'

The reference to the employees' directors and officers (D&O) insurers is significant. It was common ground that Safeway would not have been able to insure itself against the risk of being subject to an OFT fine. However, unless its claim was barred by the *ex turpi causa* doctrine, Safeway would in principle have been able to recover the fine from its former directors and employees, who were all beneficiaries of D&O insurance policies. The claim thus potentially offered a means of accessing insurance cover indirectly, in circumstances where Safeway could never have obtained cover in its own right for the penalties.

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[16] See n 3, above, at para [130].

A further, wider policy consideration is mentioned in the judgment of Longmore LJ who noted that, in Safeway's case, the *ex turpi causa* maxim would have virtually no application in corporate (and thus competition) cases, because it would apply only where the undertaking's board of directors (or its shareholders in general meeting) specifically authorised the infringement. In his view, this would not be a desirable legal development.[17]

CONCLUSION

Safeway decides that an undertaking which has been fined by the OFT for breach of the Chapter I prohibition cannot seek to recover that fine from its directors or employees. As such, the financial consequences of infringing the Chapter I infringement (or, by parity of reasoning, Chapter II) will fall squarely on the undertaking found to be in breach – and no one else.

The Court of Appeal's approach is clearly in line with the policy of the 1998 Act, which is to punish undertakings for breaches of the Chapter I and II prohibitions, and to deter other undertakings from infringing. Penalties can be imposed on individuals only under the provisions of the Enterprise Act 2002 – which requires, among other things, proof of dishonesty. Individuals who are directors of a company that commits a breach of competition law may also be disqualified.

More broadly, however, the outcome is likely to ensure a more effective enforcement regime, particularly in the sphere of leniency programmes. Individual employees will surely be more willing to report (or confess to) a suspected infringement if they are not at risk of being sued by their employer for the amount of any fine ultimately imposed – even if it is paid out by an insurer. In other, related, areas the OFT has acknowledged the importance of reassuring individuals as to their personal liability in order to ensure the effective functioning of its leniency policy: it guarantees, for example, immunity from prosecution under the cartel offence to individuals named within the scope of an immunity application.

By contrast, had the decision gone the other way, this could have had a chilling effect on the OFT's leniency programme in circumstances where individuals are reluctant to speak out, sources of information dry up and companies' ability to blow the whistle on a suspected infringement is hampered.[18]

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17 See n 2, above, at para [26].

18 Safeway has applied to the Supreme Court for permission to appeal the Court of Appeal's judgment.