

Crime Doesn't Always Pay – A review of recent professional indemnity cases in the context of fraud

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In January of this year, the National Fraud Authority published its Second Annual Fraud Indicator which estimates that fraud is costing the UK over £38 billion a year. Of that figure, £2.1 billion is estimated to result from insurance fraud, with mortgage fraud standing at £1 billion. Claims by lenders against solicitors and surveyors are on the rise again. Its not surprising then that fraud remains high on the agendas of those in the professional indemnity market.

Although claims are on the increase, fewer cases appear to be reaching the courts and there have not been many reported decisions. However, today I am going to talk about a number of cases that have been reported in the last year in which claims against professionals arising from fraud have been defended and which may serve to throw up points of interest for you.

1. The Exclusion for Dishonesty

First, a case that was reported about 18 months ago now, the case of ***Goldsmith Williams v Travelers Insurance Company Ltd 2010] All ER (D) 171*** in which the court considered the important question of effective insurance cover for innocent partners in circumstances in which insurers have repudiated liability for a dishonest or fraudulent partner and provided clarification as to the width of the exclusion for fraud and dishonesty provided for in the SRA Minimum Terms and Conditions.

The Facts

At the time of the events in question, Mr Atikpakpa (“A”) and Ms Usman (“U”), both practising solicitors, were directors of Joshua & Usman Legal Services Ltd (“JULS”). At the time, A was married to U’s sister. A was involved in a series of

fraudulent mortgage applications in which he made false statements and misappropriated mortgage funds. Two of these transactions involved the claimant firm of solicitors, Goldsmith Williams (“GW”). I should note that GW were innocent of any fraudulent involvement in the events in question.

In the first transaction, A sought to borrow approx £540,000, purportedly to purchase a property in Poplar, E14 with a view to letting it. He submitted a mortgage application to Mortgages Plc in which he falsely exaggerated his equity stake in JULS and stated that he was providing a proportion of the purchase price from his own savings. GW was instructed to act for the lender. JULS acted for A.

U witnessed A’s signature to certain documents that were submitted to the lender and certified a copy of A’s passport.

In due course, GW transferred to JULS the mortgage advance of £508,000 in anticipation of the completion of A’s purchase of the property. However, A did not purchase the property. Instead, he stole the mortgage advance.

In the second transaction, A’s wife sought to borrow money from the same lender purportedly to purchase a property in Tulse Hill owned by A and she successfully applied for a mortgage. JULS acted for A in his capacity as vendor. Once again, GW acted for the lender.

Upon the lender releasing funds to GW, they were passed to A’s solicitors and then on to JULS. Again, the transaction never completed and A stole the money which had been transferred to JULS.

The court found that U did nothing to facilitate the purchase of the property in Tulse Hill.

Eventually, GW referred JULS to the Office for the Supervision of Solicitors. The Law Society instituted disciplinary

proceedings against A, U and JULS. A left the UK for Nigeria and U went to Egypt. JULS was struck off.

Meanwhile, the lender brought claims against GW for the total sum advanced to GW, c £672,000. These claims were settled on a full liability basis, with GW taking an assignment of the lender's claims against A. GW commenced proceedings against JULS as assignee, obtained judgement and subsequently commenced proceedings against Travelers, the professional indemnity insurer of JULS, under s1 of the Third Parties (Rights Against Insurers) Act 1930. It was common ground that if Travelers was bound to indemnify JULS in respect of the claim brought by GW, it was also liable to GW.

The court considered the dishonesty exclusion in JULS' professional indemnity policy which provided as follows:

“The Company shall not be liable under the Policy in respect of ... any claim... against any insured arising from dishonesty or a fraudulent act or omission committed or condoned by such insured except that

- a. this policy shall cover each other insured; and*
- b. no such dishonesty, act or omission will be imputed to a body corporate unless it was committed or condoned by, in the case of a company, all directors of that body corporate or in the case of a limited liability partnership, all members of that limited liability partnership.”*

In reliance upon the dishonesty exclusion, insurers argued that they had no liability to indemnify JULS and, therefore, were not liable to GW. Whilst there was no dispute as to A's dishonesty or, therefore, insurers' entitlement to avoid liability to indemnify him on that basis, insurers argued that they were also entitled to repudiate liability in respect of U as the claims arose from her dishonest or fraudulent acts, alternatively that she had condoned the dishonest acts of A.

GW, whilst it did not dispute that the claim against JULS arose from the dishonesty and/or fraudulent acts of A, submitted that the evidence failed to demonstrate that the claim arose from dishonesty or fraud on the part of U or that she condoned the dishonest or fraudulent activity of A.

U's involvement in the first transaction had been to witness A's signature on certain documents and to certify a number of documents on A's behalf which U knew to contain false statements. It was generally accepted that U's conduct helped A to obtain the first loan. There was no evidence that U took any part in facilitating the transaction relating to the Tulse Hill property or that she even knew of it.

However, insurers adduced evidence of other allegedly fraudulent activities on the part of A as well as evidence that U had engaged in mortgage fraud in her own right, albeit that none of these activities had been causative of loss to GW.

The trial judge found that A had a wide ranging history of dishonest conduct, not limited to making false statements in mortgage applications and stealing the proceeds; and that U knew A was engaged in mortgage fraud prior to the transactions that were the subject of the claim. Further, the court was satisfied that in relation to the first transaction, because U had knowingly certified and witnessed fraudulent documents, she was found to have "*knowingly facilitated the mortgage fraud perpetrated by A*".

In relation to the second transaction, there were different considerations for the court – A had not perpetrated a mortgage fraud as he did not apply for the loan of the money which he stole. His dishonesty was to steal the money intended to be used by his wife to purchase the property. Notably, there was no evidence before the court that U was aware of A's theft of the mortgage monies advanced, or of any prior history of such conduct by A.

It was argued on behalf of GW that the claim arose from the theft of the money and not from the dishonest and fraudulent

mortgage application and that there must be a direct causative link between the dishonesty and the loss. The court relied upon the 2006 case of **Zurich Professional Ltd v Karim and others [2006] EWHC 3355 (QB)** in rejecting this interpretation as being too narrow and in finding that the phrase “*arising from*” in the exclusion clause was apt to embrace both aspects of A’s dishonesty.

In relation to the second transaction, even though there was no finding that U was involved in it, or even aware of it, the judge found that, by the time A stole the second advance, U knew he was engaging in mortgage fraud and that he had previously made false representations and “*that was a course of conduct which she condoned*”. Had she not condoned such conduct, A would have been in no position to steal the money borrowed by his wife in order to purchase the second property. U’s condoning of A’s fraudulent mortgage applications permitted a state of affairs to arise whereby he was left free to steal.

Thus, if an insured condones a course of conduct which is dishonest or fraudulent and that course of conduct leads to or permits the specific acts or omissions upon which the claim is founded, the insurer is entitled to repudiate liability. On that basis, insurers were entitled to rely on the exclusion in repudiating liability to indemnify both A and U.

Was a total denial of cover just? In my view, yes. The purpose of the exclusion clause is to impose liability on an insured who has condoned dishonesty. To allow an insured to escape liability because the losses caused by breach of the insured’s duty not to condone dishonesty increased beyond what was foreseen would avoid this purpose. Dishonest parties are commonly held liable for all the consequences of their dishonesty or fraud and questions of foreseeability and remoteness do not arise.

2. Breach of fiduciary duty

Barely a handful of us here today will recall the heady days of the late '80s/early '90s when a wave of lender claims followed the property recession. At that time, there was a degree of success in defending such claims on behalf of professionals by reliance on the principles of contributory negligence, causation and remoteness.

However, the lenders fought back, and incorporated into their claims against solicitors, claims for breach of trust or breach of fiduciary duty, relying on the uncontroversial premise that solicitors act as agents for their lender clients and that, pending completion, those solicitors hold the mortgage advance on trust for the lender. The lenders advanced claims that any breach of trust or fiduciary duty by the solicitor entitled the lender to recover the whole of the mortgage advance, without any reduction for contributory negligence such as imprudent lending practices and with issues of causation and remoteness being of no relevance.

However, in the late '90s a number of significant decisions limited the lenders ability to establish breach of fiduciary duty and thus to recover damages unlimited by considerations of causation, remoteness of contributory negligence.

In the 1995 case of ***Target Holdings v Redfern [1995] 3 All ER 785***, the House of Lords held that the remedy for breach of trust was not necessarily automatic restoration of the trust fund (that is, the mortgage advance) and that causation was, indeed a relevant consideration – if the solicitors breach of trust had caused no loss, then no compensation would be payable.

In 1996, there was the case of ***Bristol & West v Mothew (t/a Stapley & Co) [1996] 4 All ER 698***, in which the Court of Appeal held that an oversight by a solicitor caused by a failure to exercise reasonable skill and care could not amount to a breach of the solicitor's fiduciary duty of good faith. Liability

for breach of trust required the trustee to have acted in bad faith or to have breached the conflict rule.

However, in the recent case of ***Lloyds TSB Bank v Markandan & Uddin [2010] EWHC 2517 (Ch)*** a claim by a lender for breach of trust against a firm of solicitors arising out of a residential conveyance was successful, even where there was no negligence on the part of the solicitors who unknowingly assisted a fraud.

Facts

In June 2007, a Mr Victor Davies successfully applied to Cheltenham & Gloucester plc (“C&G”) (the predecessor in title to the Claimant) for a mortgage to purchase a property in Barnet, London. Mr Davies instructed the defendant firm of solicitors (“M&U”) to act for him. M&U were also instructed to act for C&G on the transaction in accordance with the Council of Mortgage Lenders’ Handbook for England and Wales (“CMLH”.) which required them to hold the funds on trust for C&G “*until completion*”.

On 24 August, M&U were contacted by the Holland Park office of Deen’s solicitors, a firm with a head office in Luton, who said they were acting for the Vendors of the Property, a Mr and Mrs Green. Mr Markandan, a partner in M&U, checked the Register of Solicitors and found that the Luton branch of Deen’s appeared, but not the Holland Park Branch. He contacted the Holland Park branch and spoke to someone purporting to be a member of the firm, Mr Duphar, who brought round to Mr Markandan’s offices a copy of a letter from the SRA acknowledging receipt from Mr Duphar of an application to register a new branch of Deens at the Holland Park address. Mr Duphar was the name of a solicitor on the Law Society records as practising from the Luton office of Deen.

On 29 August, Mr Markandan completed the Certificate of Title, stating the completion date to be 31 August.

On 31 August, C&G remitted to M&U the mortgage advance of £742,500. However, completion of the purchase of the Property did not occur that day.

On 4 September, having received Replies to Requisitions on title from Deen, M&U sent the net mortgage advance to an account nominated by Deen. However, no signed contract, or transfer, effecting transfer of title to the Property from the vendors to the purchaser was received from Deen.

M&U did not request those documents until a week later. They did not receive them.

On 25th September, Deen returned the funds to M&U, having deducted £5,000, with a request that M&U should re-send the money to a different account.

Somewhat extraordinarily, and despite the fact the M&U had still not received the transfer documentation, it did so.

Deen then disappeared, as did the money. The owners of the Property denied all knowledge of the transaction. It transpired that the transaction was a fraud, and there was evidence to suggest that Mr Davies had been involved in other, similar frauds. There was no allegation that M&U were involved in the fraud and the trial judge specifically noted that there was no evidence before the court of M&U's involvement in that fraud.

In due course, C&G issued a claim against M&U, alleging breach of trust, contending that the advance had been given to M&U in accordance with the provisions of clause 10.3.4 CMLH which provides:

“You must hold the loan on trust for us until completion. If completion is delayed, you must return it to us when and how we tell you.”

C&G contended that completion had never occurred and thus it was entitled to the return of the money, irrespective of any

negligence on M&U's part, and that there could be no issue of contributory negligence.

In its Defence, M&U admitted that it held the mortgage advance on a bare trust for C&G with C&G's authority to pay it away in connection with Mr Davies' purchase of the property.

At case management stage, given M&U's admission, the Master ordered a trial of the following preliminary issues:

- (i) Had there been a breach of trust by M&U?;
- (ii) If so, was M&U entitled to relief under s61 Trustee Act 1925;
- (iii) Could M&U rely in principle on the defence that any loss or damage was caused or contributed to by C&G's own fault?

In relation to the first preliminary issue, M&U contended that the trust upon which they held the mortgage advance was more limited than that contended by C&G.

M&U argued that the mortgage had been completed as Mr Davies had signed the mortgage deed. C&G, on the other hand, contended that completion did not take place until the transaction was registered with the Land Registry.

The court did not agree with either view, instead finding that C&G's authority entitled M&U to pay away the mortgage advance on receipt of documents necessary to register title, or upon receipt of a solicitor's undertaking to provide such documents.

The court stated that it was important to distinguish between the terms of the trust and the contractual terms between M&U and C&G. The first preliminary issue was concerned only with the breach of trust and not with any breach of contract/negligence. The issue of whether Mr Markandan made sufficient checks as to the identity of the solicitors

purportedly acting for the vendors was one of negligence and not one of breach of trust.

The court found that in paying away the money without receiving the requisite documents and without receiving a solicitor's undertaking to provide such documents, irrespective of whether they had acted in breach of contract and/or negligently, M&U had acted in breach of trust.

S61 of the Trustee Act, upon which M&U sought to rely, provides that where a trustee is personally liable for a breach of trust but has acted honestly and reasonably and ought fairly to be excused for the breach, the court may relieve him from personal liability.

Whilst there was no suggestion that M&U had acted dishonestly, C&G contended that their actions had been unreasonable. The court agreed with the submission that in paying the money to Deen without receipt of the transfer documentation, in re-paying the money to Deen once it had been returned and in failing to establish, as specifically required by the CMLH, that Deen did not have an office in Holland Park, M&U had acted unreasonably and were not entitled to relief under s61.

The third preliminary issue to be decided was whether, in order to reduce liability for breach of trust, M&U could rely on a defence of contributory negligence. The court confirmed that the limited categories where a defence of contributory negligence could be relied upon in contractual claims did not extend to cases of breach of trust.

The decision may, at first glance, appear to be at odds with the decision in ***Bristol & West Building Society v Mothew***, where the Court of Appeal held that a defendant solicitor was not guilty of breach of trust in paying away mortgage funds in circumstances in which he had unwittingly misrepresented circumstances to the lender due to an inadvertent failure and not because of disloyalty or infidelity. However, in *Mothew*, the lender's standard instructions did not make clear that the

solicitor's authority to complete the mortgage transaction was conditional upon having complied with his instructions. That was not the case in the present case, in which the only real issue to be determined by the court was the extent of M&U's authority and, in the circumstances, the court was satisfied that that was clear.

So, on the basis of this decision, an honest but negligent solicitor if found to have acted in breach of trust will be unable to rely on causation, remoteness or contributory negligence and will be liable to re-pay the entire mortgage advance to the lender.

3. **Doctrine of illegality**

An increase in claims founded in fraud inevitably leads to an increase of instances in which professionals and their insurers may be able to rely upon the defence of illegality.

This doctrine is often referred to by its Latin maxim "*ex turpi causa non oritur action*" – literally "*from a dishonourable cause an action does not arise*".

The doctrine of illegality is a doctrine of public policy which is potentially of very wide application and which may operate to prevent a claimant from obtaining a remedy to which he would otherwise be entitled.

The defence of illegality may defeat a claim against professional advisors where the claimant relies upon their own wrongdoing. It is been described as a very blunt instrument and, if applicable, will defeat a claim in negligence even if the claimant succeeds in establishing duty, breach, causation and loss, even if the result is that the defendant unjustly avoids liability.

In March 2010, the Law Commission published its final report on the illegality defence following its recent consultation into the issue, in which it described this area of the law as

“technical, uncertain and in some cases arbitrary and lacking in transparency”.

It is a notoriously uncertain area of law, which has recently been considered in a number of cases looking at the level of culpability on the part of the claimant that is needed for a claim to be defeated.

Nayyar v Denton Wilde Sapte [2009] EWHC 3218 is a good example of the application of the doctrine in the case of a claim against a firm of solicitors. The claimant travel agents had paid a significant sum in anticipation of their appointment as exclusive agents by Air India. The claimant’s introduction to Air India had been effected by a senior solicitor employed by the defendant who had *“facilitated”* the payment. The travel agents claimed that the solicitor had given them negligent advice and had made negligent misrepresentations. The court held, however, that in acting effectively as a *“deal broker”* it would have been apparent to a reasonable and competent person in the position of the claimant that the solicitor was not performing a solicitorial or legal advisory role, meaning that the defendant firm was not vicariously liable for her conduct. She was not acting within her actual or ostensible authority. The Judge held that the payment was intended to be a bribe and that this was sufficient to engage the doctrine of illegality, as a result of which the claim failed.

In the case of ***Griffin v UHY Hacker Young & Partners [2010] EWHC 146*** the claimant had established a company to market a soft drink but the company had gone into insolvent liquidation. He therefore took advice from a partner in the defendant accountants about the possibility of establishing a new company to trade under a very similar name for the same purpose. He was consequently convicted of a strict liability offence under s.216 of the Insolvency Act 1986 of taking part in the management of a company with an apparent connection with the insolvent company. The claimant alleged negligence against his former accountants and claimed damages for the effect on his businesses and reputation. The accountants sought summary judgment, citing the claimant’s criminal

conviction as a basis for the application of the doctrine of illegality. Their application was, however, dismissed on the basis that the doctrine would apply only if a degree of serious moral culpability was demonstrated and that was an issue which it was impossible to resolve short of a trial.

Safeway Stores Ltd v Twigger & Ors [2010] EWCA Civ 1472 was a Court of Appeal case that arose out of the actions of a number of companies who, colluded in order to raise the price of certain dairy products. This constituted an infringement under the Chapter I prohibition of the Competition Act 1998.

A number of the companies involved, including Safeway, agreed early resolution agreements with the Office of Fair Trading (OFT). In doing so, they admitted liability and agreed to cooperate with the ongoing OFT investigation. Although the OFT has not taken a final decision as to the level of fine to impose on Safeway, it is likely to be in excess of £10m.

Safeway (having been acquired by Morrisons) subsequently brought an action in the High Court seeking an indemnity in respect of the fine to be paid (once imposed), together with the costs of cooperating with the OFT investigation, from its former directors and employees who had allegedly been involved in the anticompetitive conduct. It was argued that those employees and directors had acted negligently and/or breached their employment contracts and/or committed a breach of their fiduciary duties. As a result, Safeway alleged that those individuals should be liable to compensate the corporate group.

The defendants responded by seeking a summary judgment against Safeway. They argued that the doctrine of illegality applied, preventing Safeway's claim from succeeding. They also argued that the basis of the claim was incompatible with the UK competition regime. The defendants failed in their summary judgment application, on the basis that the illegality principle could only be engaged if the claimant could be shown to be "*personally*" at fault. Mr Justice Flaux held that it was at least arguable that the acts of the directors and

employees were not "*personal*" to Safeway. He considered that the question turned on whether the relevant individuals could be said to be the "*controlling mind or will*" of the company, which at that time it was not possible to determine. The principle of *ex turpi causa* was therefore not engaged. Further, the claim did not infringe against UK competition law policy.

Accordingly, the judge held that the matter should proceed to trial.

The defendants successfully appealed against this decision. The Court of Appeal held that liability under the Competition Act was directed at the company itself. Safeway was therefore personally liable not simply vicariously liable for the acts of its directors and employee. Consequently, Safeway could not recover for its own wrongdoing - the principle of *ex turpi causa* being engaged. The claim against the former employees and directors therefore failed.

In reaching its conclusions, the Court of Appeal also noted that the UK competition regime was designed to discourage companies from engaging in anticompetitive behavior. If they were allowed to pass on liability to their directors and employees this would undermine the entire regime.

4. **A solicitors' right to assume his client's honesty**

The case ***Frank Houlgate Investment Co Ltd v Biggart Baillie LLP***, is actually a Scottish case, but the Judge relied upon numerous English and Commonwealth authorities and principles of general relevance to both jurisdictions. In this case, the Claimant made investments in a purported business run by a fraudster, who was represented by the Defendant solicitors. The fraudster, John M Cameron, claimed to be the owner of a Scottish estate. The Claimants advanced money to John M Cameron who granted security to them over the property. The solicitors were not aware that John M Cameron was not the title holder until they received contact from solicitors acting for the true owner, a John Bell Cameron. At that point, John M Cameron, the fraudster, confessed to

solicitors that he was not the true owner of the property and that he had acted fraudulently in relation to the transaction of the Claimants. The solicitors did not convey this information to the Claimants, who subsequently advanced further sums to John M Cameron before discovering his fraud. The Claimants claimed that the solicitors had a duty to take reasonable care to confirm John M Cameron's identity and to confirm that he was the registered title holder, or further to advise the Claimants that the solicitors were acting for someone other than the registered title holder. The Claimants further contended that, by continuing to act for John M Cameron once they knew of his fraud, the solicitors impliedly warranted that John M Cameron was the registered title holder and owner of the property.

Perhaps crucially, the claim was not advanced on the basis of fraud on the part of the solicitors.

The claim failed, the Scottish Court holding that this situation did not fall within the exceptions to the general rule that a solicitor in a conveyancing transaction will owe no duty to the other side. Likewise, the Court took a narrow interpretation of the warranty of authority given by the solicitors; it held that that warranty was simply that the firm was acting for John M Cameron, rather than that he was the true owner of the property.

The Scottish Court referred to the English decision in ***Gran Gelato Ltd v Richcliff (Group) Ltd [1992] Ch 560*** as the principal authority relied upon by the Defendant's solicitors. The Claimant entered into negotiations for the acquisition of two underleases. In the course of the negotiations, the Claimant's solicitors asked the sellers' then solicitors whether any rights existed in the head leases which would inhibit the enjoyment of the underleases. The solicitors replied "*not to the lessors' knowledge*". In fact, the head leases of both properties contained break clauses which, if exercised, would terminate the under leases after 5 years. When the matter came to light, the Claimants raised an action against both the seller of the under leases and their solicitors. In relation to the

latter claim, Sir Donald Nichols V-C held that *“in normal conveyancing transactions solicitors who are acting for a seller do not in general owe to the would-be buyer a duty of care when answering the enquiries before contract or the like”*. Three reasons were given for this conclusion. First, the context in which such representations are made; namely that there is a contract for the sale of an interest in land, and that the answers given by the seller’s solicitor are given on behalf of the seller. Secondly, the law provides the buyer with a remedy against the seller in respect of any misrepresentation in the answers given on his behalf. The seller himself owes a duty of care to the buyer, and the seller will be as much liable for any carelessness of his solicitor as he would be for his own personal carelessness. This is because the solicitor has implied authority from the seller to answer the questions on his behalf. Thirdly, caution should be exercised before the law takes the step of concluding, in the field of negligent misrepresentation, that an agent acting within the scope of his authority on behalf of a known principal, himself owes to third parties a duty of care independent of the duty of care that he owes to his principal. There will be cases where it is fair, just and reasonable that there should be such a duty but, in general, where the principal himself owes a duty of care to the third party, the existence of a further duty of care, owed by the agent, is not necessary. Good reason, therefore, should exist before the law imposes a duty when the agent already owes a duty to his principal which covers the same ground and the principal is responsible to the third party for his agent’s shortcomings. The Court found that there was no good reason for such a duty in normal conveyancing transactions.

The Judge in *Frank Houlgate* identified two significant points: first, that a person who acts in a transaction as agent for a principal may in some circumstances owe a duty of care to the other party in the transaction; the mere existence of agency is not of itself a reason for excluding liability. Secondly, although such a duty is possible, it would normally only arise where the agent chooses to provide information or advice to the other party, and does so in such a way that it can reasonably be inferred that he is undertaking a duty of care in respect of such

information or advice. The Judge then went on to refer to several decisions, including *Hedley Byrne & Co v Heller* and *Henderson v Merrett Syndicates Limited* which, as is widely known, found that the concept of assumption of responsibility was frequently helpful in cases where a party has provided information or advice to, or performed a service for a person without being contractually obliged to do so. In all such cases, of course, it is essential that the recipient of the information or advice or service should rely on it, and that the person providing the information, advice or service should know that the other person was likely to do so. The Judge also referred to the *Capparo Industries PLC v Dickman* case, stressing the importance of the test of sufficient proximity, and the need for any duty to be fair, just and reasonable. He felt that that principle underlined the reasoning of the Vice Chancellor in the *Gran Gelato* case; that is, that in a normal conveyancing transaction it would not be fair and reasonable to impose on a solicitor a duty of care in favour of the other party for a number of reasons:

First, the law relating to solicitors acting in conveyancing and securities transactions is reasonably clear: the solicitor acting for one party in such a transaction would not normally owe a duty of care to the other party; the other party would normally instruct his own solicitor to look after his own interests.

Secondly, an exception to this may occur where a solicitor acting for one party chooses to answer an enquiry made of him by the other party. In such a case, however, it is essential that, objectively speaking, the solicitor who answers the enquiry can be said to have undertaken responsibility to the other party. Whether that requirement is satisfied will depend on the circumstances of the particular case; for example, if the solicitor grants a certificate or appears to undertake the task on his own initiative, it may be easy to draw the inference the responsibility has been undertaken. If, however, the solicitor does no more than pass on information provided by the client, and presents the information as so provided, the inference would be much more difficult.

Thirdly, the general rule relates only to a solicitor's duty of care. If the solicitor becomes aware of dishonesty on the part of his client that amounts to fraud on the other party, he would plainly be under a duty to ensure that he does not further that fraud in any way. If he does anything in furtherance of the fraud, he will be liable to the other party as a participant in the fraud. On this point the Judge emphasised that there is no duty to assume that the solicitor's client might be acting deceitfully and to take reasonable steps to ascertain whether or not that was the case. If, however, the solicitor becomes aware of some fact that points towards a fraud, it is a matter of fundamental professional integrity that he should refuse to act further in a transaction. Indeed, in some cases the duty may go further, in requiring that the solicitor disclose the fraud to some other party. If the solicitor does continue to act, he becomes party to the fraud and he is liable accordingly.

Fourthly, any decision to answer a question by the other side must amount to an undertaking of responsibility towards the other party if a duty is to be imposed.

In the Frank Houlgate case, the Claimants argued that the solicitors impliedly represented, by their conduct throughout the transaction, that they had authority to act for John Bell Cameron (i.e. the true owner) AND that feature was said to justify an exception from the normal rule. However, the Judge rejected this because he found there was no basis for an assumption of responsibility to be based on an implied representation. Furthermore, he said that certain features of the transaction were not unusual per se; it was not especially unusual that the loans were being made to a company owned by one person but the standard security was apparently granted by another. This meant either that a single individual was using two distinct names (which is not uncommon) or two individuals were involved and one was given security for the borrowings of another (again, a frequent occurrence). What is of importance, however, was that the two names were known to the claimants and their solicitors. Crucially, it was open to the claimant's solicitors to ask for an explanation of this

feature of the transaction but there was no indication that they had done so.

The Judge went on to conclude that: *“the fact that the matter is peculiarly within the knowledge of one party cannot justify the imposition of a duty of care on that party’s solicitor in favour of the other party. The solicitor may know many things about his client that the other party does not know, and there cannot be a duty to disclose all of them; many of them will be confidential otherwise, short of dishonesty, there is in my opinion no basis for holding that the solicitor should be under a duty of care to disclose personal circumstances to the other party to the transaction. Consequently, unless he is put on notice of dishonesty, a solicitor is in my opinion entitled to assume that his client is behaving honestly.”*

The Judge then noted that the claim had not been pursued for fraud; this, in my view, was the curious feature of this case. The nub of it was that the claimants were trying to establish liability in negligence for something which, if proven, would appear to constitute a liability in fraud, and that was not something the court was prepared to support. There may well have been perfectly good reasons why the claim in fraud was not pleaded, but the result appears to be that the Claimants have no remedy against solicitors who appear to have acted in a most dubious fashion.

5. Limitation

Edehomo v Bowling & Co Solicitors [2011] EWHC 393 Ch

This High Court appeal concerned the question of whether, in a fraudulent property transaction, loss was suffered on exchange or completion. This was pertinent to when time started running under section 2 of the Limitation Act 1980. At first instance, it was held that the Claimant, Rose Edehomo, suffered loss on completion. The Defendant solicitors, Bowling & Co. Solicitors (“Bowlings”) appealed, successfully arguing that loss was suffered on exchange.

By way of background, the Claimant and her (now estranged) husband, Jerome Edehomo bought an investment property in 1989 as joint tenants. In 2002, unknown to the Claimant, Jerome instructed Bowlings to act for him and her in the sale of the property to a third party. The Claimant was unaware of the sale transaction because Jerome forged her signature on documents, and got someone to impersonate her in meetings with Bowlings. The sale of the property went through, with contracts exchanged on 21 November 2002 and completion taking place on 2 December 2002. The Claimant never received any of the proceeds of sale.

On 1 December 2008, Mrs Edehomo issued a claim against both Jerome and Bowlings. Jerome (and the money) had by then 'disappeared', leaving Bowlings the focus of the claim. Her claim against Bowlings was initially framed as breach of a duty of care in both contract and tort, the central particular of which was that that Bowlings had failed to take reasonable or appropriate steps to establish the identity of the persons on whose instructions they were acting. The claim proceeded only in tort - Mrs Edehomo's case being that she was never a client of Bowlings and, accordingly, there was no contract between them.

She issued proceedings just one day within six years of the date of completion, but more than six years from the date of exchange. That distinction became critical since section 2 of the Limitation Act 1980 provides that: *“An action founded on tort shall not be brought after the expiration of six years from the date on which the cause of action accrued.”*

Bowlings defended the claim and contended that if it had been in breach of duty, then the Claimant had suffered damage on and from 21 November 2002 - the date when contracts for sale were exchanged. This was more than six years before the claim was brought and Bowlings argued that it was therefore barred by statute. The County Court Judge held that Mrs Edehomo did not suffer damage until completion, on 2 December 2002, and that her claim had therefore been

brought within six years of accrual of her cause of action, i.e. within the limitation period.

Bowlings' appeal relied on the Court of Appeal authority of ***Nouri v Marvi [2010] EWCA Civ 1107***, which had been decided after the County Court decision.

In *Nouri v Marvi*, the Claimant was the registered owner of a leasehold flat. He allowed the Defendant, Mr Marvi to live in the flat while Mr Nouri was out of the country. While Mr Nouri was abroad, Mr Marvi sold the flat to himself - posing as Mr Nouri in instructing solicitors as vendor, and instructing other solicitors to act for him in his own name as purchaser. Exchange of contracts and completion were simultaneous on 2 April 2001; and on 4 July 2001, Mr Marvi, using a Transfer on which he had forged Mr Nouri's signature, registered title to the flat in his own name. He then went on to sell the flat to an unknowing and unconnected third party. On 2 July 2007, Mr Nouri commenced proceedings against Mr Marvi and also the solicitors who had acted for the 'vendor'. That action was commenced more than six years after exchange and completion, but less than six years after registration.

The Court of Appeal in *Nouri v Marvi* upheld that of the trial judge: that the claim against the solicitors was statute-barred. In the leading judgment it was emphasised that the primary limitation clock could and would start running whether or not a claimant was aware of his or her loss. It held that Mr Nouri had suffered actual damage on completion - it was not, as he had argued, that he was simply exposed to a contingent loss through the contract but which would only crystallise into an actual loss once Mr Marvi applied for registration of title.

In *Edehomo v Bowling*, Bowlings' appeal was allowed. The Court followed the reasoning in *Nouri v Marvi*, albeit noting that when Mr Nouri was found to have suffered loss "*on completion*" that reflected the fact that nothing in that case turned on the distinction between exchange and completion since they were simultaneous. It held that Mrs Edehomo had suffered loss from the date of exchange, such that she could

have started proceedings against Bowlings at that stage. It reasoned that no potential purchaser would choose to enter a binding obligation to buy an interest in property at its open market value if he or she were told that the property had already been sold to someone else, but that the other sale could simply be disregarded because the vendor's signature on the earlier contract had been forged. The potential purchaser could not know whether that was correct, and would face a need to investigate and/or run the risk of becoming involved in litigation. From exchange of contracts onward, there was "a blot" on the title and the value of the property was blighted. Her loss having been suffered on exchange, more than six years before she commenced the action, Mrs Edehomo's claim was time-barred.

This case confirms that cause of action in tort accrues when loss is first suffered as a consequence of the breach of duty. In particular it highlights that in a property action where there has been mischief involved, the cause of action will typically accrue at exchange. In relation to section 2 of the Limitation Act 1980, claims will have to have been issued within six years of exchange of contracts. This may be critical to conveyancing professionals and their insurers, and potentially also to lenders.

6. **Employers' vicarious liability for the fraudulent activities of employee**

Quinn v CC Automotive Group Ltd (t/a Carcraft) [2010] EWCA Civ 1412

This is a Court of Appeal decision which concerned the relevance of whether the victim of a fraud perpetrated by the employee of a car dealership was 'put on inquiry' about the fraud by virtue of some curious aspects of the fraudster's conduct. In summary, the Court of Appeal found that the first instance judge had erred in relying upon an inquiry test; there was no room nor any need for such a test where the fraudster had acted with the apparent authority of the dealership, and the victim had been entirely innocent.

Briefly, the facts were that the victim car purchaser believed he was buying a car via a financing arrangement through the dealership. The car salesman took the victim's own car in part exchange, but then informed the victim that the finance had been turned down. This was incorrect; the victim had entered into a binding contract with the finance company but, in the meantime, the fraudster had sold the car to another innocent purchaser. The result was that the victim had lost his own car, had not obtained the new car, and had been left with an apparent debt to the finance company. The victim sued the dealership, which sought to defend the claim on the basis that the fraudster was not acting within his apparent authority and also the victim was 'put on inquiry' by the fraudster's suspicious behaviour. That conduct was concerned with the fraudster's attempt to extract a further £700 from the victim; the victim had said he could afford £400 extra, and the fraudster had accepted that and taken this additional sum.

The first instance decision was that although the fraudster did have apparent authority to sell the car and deal with related matters such as the part-exchange, the victim had been 'put on inquiry' by the fraudster's behaviour. This was notwithstanding the fact that the judge accepted that the victim had been entirely innocent and unsuspecting.

The appeal was allowed, on the basis that the concept of being 'put on inquiry' had no place in the test of whether a principle is liable to a third party for the fraudulent acts of his agent or employee. The principles of law had been well settled; the genesis could be traced back to a dictum of Holt CJ from 1700:

“Seeing as somebody must be a loser, by this deceit, it is more reason that he that employs and puts a trust and confidence in the deceiver should be a loser, than a stranger.”

However, an employer will plainly not be liable for all deceits or frauds of his employees; only where the acts fall within the

actual or apparent authority of the employee. This also applies to liability for fraudulent misrepresentations.

The Court of Appeal considered that another way of looking at the matter was to concentrate upon the closeness of the connection between the work the employee had been engaged to do and the torts committed. If that connection is sufficient, then the torts may be regarded as having been committed within the scope of employment. This analysis avoided the paradox that the greater the fault of the servant, the less the liability of the master.

This decision also reaffirms that the courts will take a broad approach to the scope of the employee's employment, and in doing so, they should avoid the use of hindsight.

Furthermore, in the context of fraudulent misrepresentation, liability of the principal can only be established if the victim relied upon the fraudster's misrepresentation.

Having outlined these principles, the Court of Appeal found that it was clear that the 'inquiry' test was inappropriate and played not part in the question of the principal's liability to the victim.

The reiteration of these established principles is to be welcomed and, furthermore, I believe justice was done in this case. However, looking more broadly at the implications in the context of professional liability claims, it obviously means that the professionals whose employees/agents have defrauded victims will not be able to rely on the 'inquiry' line of defence. They may, of course, still be able to assert that the agent/employee was acting outside of the scope of their duties. This brings us back to the principles referred to earlier, in the context of the illegality defence used in cases such as *Nayyar*.