Claims against professionals: Negligence, dishonesty and fraud: Speech by the Rt. Hon. Sir Athony Clarke, Master of the Rolls

Introduction

1. Shortly after I was appointed as Master of the Rolls only just over six months ago I received an invitation from Mark Simpson to give today's keynote speech, which I do with great pleasure. Mark is both an extremely good advocate (not always on the winning side) and also a better golfer than me.
2. I perhaps owe a few words of explanation as to the subject matter of my address: the title is certainly a broad one. You will be pleased to hear that I do not propose to speak to the whole topic, which would in any event be an impossible task. Indeed I know that this conference is focusing in part at least upon professional negligence, about which a great deal has been said and written over the years. I hope I will be forgiven for focusing on one issue which has posed difficulties for courts, practitioners and academics alike. I intend to focus on the nature of dishonest, or if Lord Millett's view and its historical name are to be preferred, knowing assistance in the breach of trust. Before doing so I would like to pay tribute to John Sorabji who is responsible for all the good bits in this afternoon's lecture. I take full responsibility for all the errors.
3. As the world becomes more and more complex, as financial markets and transactions become more and more sophisticated and as professionals increasingly provide services in a global market place where both their clients and other professional engaged in particular transactions may be separated by great distances, it seems to me to be more likely than not that the number and value of claims for dishonest assistance will increase, perhaps to a marked extent. An increasingly complex world unfortunately offers the unscrupulous ever more opportunities to profit from fraud and dishonesty.
4. To my mind therefore there is a distinct possibility that complex frauds, which involve claims for dishonest assistance, such as those which arose in Al-Sabah v Grupo Torras [2001] Lloyd's Rep. (PN) 117 (CA) (which I will call Grupo Torras), or Abou-Rahmah & Others v Abacha & Others [2005] EWHC 2662 (QBD) will become more common. If this is right it becomes ever more important that the legal test for a claim for dishonest assistance is clear. It needs to be clear so that the courts can apply it in both a consistent and straightforward manner. Equally, it needs to be clear so that professionals, whether solicitors, bankers, financial advisors, accountants or others, are aware of their obligations and can thus ensure that their conduct properly conforms to their obligations. Finally, it needs to be clear so that professional indemnity insurers and their advisers can properly assess insurance risks and the stance to take where litigation is contemplated.
5. The issue on which I wish to focus is the nature of the test for dishonest assistance. That test has recently been revisited by the Privy Council in Barlow Clowes International Ltd (in liquidation) & Others v Eurotrust International Ltd [2006] 1 ALL ER 333 (PC) (which I will call Barlow Clowes); a decision which seeks to explain the Privy Council's previous decision in Royal Brunei Airlines v Tan [1995] 2 AC 378 (which I will call Royal Brunei) and the House of Lords' decision in Twinsectra v Yardley [2002] 2 AC 164 (HL) (which I will call Twinsectra).

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Background

6. Dishonest assistance is a form of liability imposed on those who assist, who are accessories to, breaches of trust by trustees or breaches of fiduciary obligations by those such as company directors or bankers. It is sometimes called accessorial liability but, speaking for myself (as they say in the Court of Appeal) that is not an expression I care for. It is a fault-based form of liability, which requires an individual to provide compensation for wrongdoing (see Royal Brunei per Lord Nicholls at page 393 and Twinsectra per Lord Millett at para 107). It is not therefore a form of liability which arises in restitution. It is akin, as Lord Millett in his dissenting judgment in Twinsectra rightly stated, to the economic torts, although liability arises in equity (at para. 127).
7. A typical form of dishonest assistance is that which was alleged to have taken place in Twinsectra:

Solicitor A acts for a property developer. The property developer deposits money with A in respect of a property purchase. The money is deposited on the explicit understanding that it will only be used to fund that purchase. The money is, simply put, held subject to a trust by solicitor A. Solicitor A passes the money to solicitor B. He does not do so in order to fund a property purchase. Solicitor A has thus breached the terms of the trust. Solicitor B is aware that the money is subject to a trust and is aware of the undertaking that solicitor A can only use the money to fund property purchases. Solicitor B dissipates the funds, either for a legitimate or illegitimate purpose. The purchaser has a clear cause of action against solicitor A for breach of trust. Can liability also be imposed on solicitor B?

8. Before the Privy Council's decision in Royal Brunei the leading statement was that of Lord Selbourne LC in Barnes v Addy (1874) LR 9 Ch. App 244 at 251, which had been decided no less than 120 years earlier. In his celebrated obiter dictum Lord Selbourne said this:

   "(A trustee's responsibility) may no doubt be extended in equity to others who are not properly trustees, if they are . . . actually participating in any fraudulent conduct of the trustee to the injury of the cestui que trust. But . . . strangers are not to be made constructive trustees merely because they act as the agents of trustees in transactions within their legal powers, transactions, perhaps of which a court of equity may disapprove, unless those agents receive and become chargeable with some part of the trust property, or unless they assist with knowledge in a dishonest and fraudulent design on the part of the trustees."

9. It is of course well known that in this dictum Lord Selbourne sets out the basis for both knowing receipt and, what was then called, knowing assistance. Liability for knowing assistance arose where; i) a trustee was dishonestly and fraudulently in breach of trust (although it was not until Belmont Finance Corporation Ltd v Williams Furniture [1979] Ch 250 that the inclusion of a fraudulent design was confirmed as a necessary element of the action) and ii) a third party with knowledge of that dishonest and fraudulent breach of trust assisted in the scheme. By contrast with knowing receipt, there is no requirement that the third party should actually receive trust property. Lord Selbourne's test may well have been an obiter dictum in an unreserved judgment but in the not unusual way of things in our common law system it became firmly established as the test for knowing assistance. It acquired the status, as Charles Harpum has put it, of a 'legislative test' (LQR (1995) 111 (Oct) 545), or as Lord Nicholls put it in Royal Brunei at page 386, of a statute. In doing so it engendered a large body of jurisprudence, which sought amongst other things, to establish the appropriate level of knowledge required of the third party accessory to give rise to liability: see for instance Baden v Sociètè Gènèrale [1992] 4 ALL ER 161.
10. In Royal Brunei the Privy Council fundamentally altered the test for knowing assistance. It did so in two ways. First, it rejected the requirement that the breach of trust must arise as the result of a dishonest and fraudulent scheme. This aspect of its judgment has not proved contentious, or at the least has not, so far as I am aware, been the subject of further appellate consideration. It is not that part of the decision upon which I want to focus today. Secondly, it rejected the requirement that the third part needed to be aware of the breach of trust. It replaced that requirement with a dishonesty test and in doing so renamed the cause of action 'dishonest assistance'. The new test as formulated by Lord Nicholls, who gave the judgment of the Privy Council, said at 392:

    "A liability in equity to make good resulting loss attaches to a person who dishonestly procures or assists in a breach of trust or fiduciary obligation. It is not necessary that, in addition, the trustee or fiduciary was acting dishonestly, although this will usually be the case where the third party who is assisting him is acting dishonestly."

11. Lord Nicholls' test can thus be simply put and is straightforward - a point which was emphasised by the Court of Appeal in a judgment of the court in Grupo Torras at page 109 when it held that:

    "The Royal Brunei test is not difficult to understand or apply."

12. That judgment was handed down in November 2000 at which time only four cases post-Royal Brunei had been to the Court of Appeal. One of those cases was of course Twinsectra, which was to be heard by the House of Lords in October 2001. At that time the Court of Appeal could no doubt feel relatively secure in its conclusion that that the test was not difficult either to understand or to apply.

Any such confidence was premature.

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Royal Brunei - Dishonesty

13. The fundamental difficulty surrounding the test arose from Lord Nicholls' treatment of dishonesty. Before looking at its treatment by the House of Lords in Twinsectra and the Privy Council in Barlow Clowes it is instructive to return to Lord Nicholls' judgment and look at it unencumbered by later judicial explanation.
14. Lord Nicholls initially dealt with the concept of dishonesty (at page 389) by distinguishing it from what that concept means in other contexts. He held that:

    "Whatever may be the position in some criminal or other contexts (see, for instance, Reg. v Ghosh [1982] QB 1053), in the context of the accessory liability principle acting dishonestly, or with lack of probity, which is synonymous, means simply not acting as an honest person would in the circumstances."

15. On the face of it Lord Nicholls appears to be making two connected points here: the first, that the concept of 'dishonesty' is not susceptible of one interpretation: its meaning is context dependent. What it means, in for instance the criminal law, is not necessarily what it means in equity. His second point is that, what it means in equity is determined by an objective standard, by looking at how an honest man would act in the circumstances. The meaning of objective standard in the context of accessorial liability is then further explained by Lord Nicholls:

    "This (the honest man test) is an objective standard. At first sight this may seem surprising. Honesty has a connotation of subjectivity, as distinct from the objectivity of negligence. Honesty, indeed, does have a strong subjective element in that it is a description of a type of conduct assessed in the light of what a person actually knew at the time, as distinct from what a reasonable person would have known or appreciated. Further, honesty and its counterpart dishonesty are mostly concerned with advertent conduct, not inadvertent conduct. Carelessness is not dishonesty. Thus for the most part dishonesty is to be equated with conscious impropriety. However, these subjective characteristics of honesty do not mean that individuals are free to set their own standards of honesty in particular circumstances. The standard of what constitutes honest conduct is not subjective. Honesty is not an optional scale, with higher or lower values according to the moral standards of each individual. If a person knowingly appropriates another's property, he will not escape a finding of dishonesty simply because he sees nothing wrong in such behaviour."

16. Lord Nicholls is here making a number of points. The least contentious one is that the objective standard employed is not the same as the objective standard applicable in negligence. The accessory's conduct is not to be assessed by the standard of the reasonable man, and thus by inference by what 'a reasonable man would have known or appreciated'. The reason is that while the test is objective, it involves an assessment of the accessory himself. The objective standard for dishonesty in equity, has 'a strong subjective element'. While the nature and interrelation of the objective and subjective aspects of the dishonesty test has proved to be the focus of appellate debate, Lord Nicholls seems to me to be making the simple point that the court should attribute to the honest man, to whom the accessory is to be compared, what the accessory knew at the relevant time. And as for knowledge, that included what is commonly referred to as Nelsonian knowledge:

    ". . . an honest person . . . (does not) deliberately close his eyes and ears, or deliberately not ask questions, lest he learn something he would rather not know, and then proceed regardless."

17. These points are emphasised and explained later in Lord Nicholls' opinion (at pages 390 - 391), where he says this:

    "What does honesty require (an individual) to do?
    The only answer to (this) lies in keeping in mind that honesty is an objective standard. The individual

is expected to attain the standard which would be observed by an honest person placed in those circumstances. . . An honest person would have regard to the circumstances known to him, including the nature and importance of the proposed transaction, the nature and importance of his role, the ordinary course of business, the degree of doubt, the practicability of the trustee or the third party proceeding otherwise and the seriousness of the adverse consequences to the beneficiaries. The circumstances will dictate which one or more of the possible courses should be taken by an honest person. . .
Likewise, when called upon to decide whether a person was acting honestly, a court will look at all the circumstances known to the third party at the time. The court will also have regard to personal attributes of the third party, such as his experience and intelligence, and the reason why he acted as he did."

18. What conclusions can be drawn from this elaboration of the nature of the objective standard of dishonesty? On the face of it, and again I stress without recourse to later appellate authority, Lord Nicholls appears to be stating that the test for dishonesty rests solely on the assessment of whether the individual in question acted consistently with the standard an honest person in the same circumstances would have attained. In making that assessment the individual's own knowledge and experience form part of the relevant circumstances, which form part of the honest man's standard. It appears to me that that was most succinctly, and accurately summarised by Mance J (as he then was) at first instance in Grupo Torras (at page 326) where he held that Royal Brunei established that:

    ". . . dishonesty in the context of a knowing assistance claim is an objective standard. . . The individual is expected to attain the standard which would be observed by an honest person placed in the circumstances he was . . . But those circumstances include subjective considerations like the defendant's experience and intelligence and what he actually knew at the time."

19. Interestingly, put this way the test does resemble a test known to the criminal law. It is not, however, the test for dishonesty as laid down in Ghosh. As has been pointed out by Alistair Spiers of the University of Newcastle in Escape from the Tangled Web [2003] 3 Web JCLI, Lord Nicholls' test, which focuses on whether an honest man with the same characteristics as the individual in question would have acted as he did, is strikingly similar if not the same test as is established in the criminal law for the defence of provocation as established by Lord Diplock in R v Camplin [1978] AC 705 at 718 and applied by R v Morhall [1996] AC 90. As he puts it, that test is:

    ". . . objective in that the question is 'whether the provocation was enough to make a reasonable man do as the defendant did' but permits characteristics of the accused (such as age or addiction) to be attributed to the reasonable man."

20. I shall refer to this test, as it was set out in Camplin and Morhall as the provocation test. The analogy drawn appears to be a valid one. In both that case and in Lord Nicholls' judgment we have an objective test, which incorporates subjective characteristics, rather than simply focusing on what a reasonable man ought to have known or what characteristics a reasonable man ought to have had. In both cases we have tests that on the face of it appear straightforward and clear.
21. I should pause at this point. Given the confusion in this area caused by comparisons with tests for dishonesty in other areas of the law it is perhaps infelicitous to draw such an analogy. With that caveat in mind I turn to the House of Lords' decision in Twinsectra.

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Twinsectra – Dishonesty

22. Lord Nicholls' propositions stood unexamined by the English appellate courts for approximately six years. During that time it was applied by the courts. According to some, such as Robert Hunter, it was a test 'everybody seemed to understand.'[1] According to others it was difficult to understand. As Tjio and Yeo noted in 2002 at first instance and in the Court of Appeal in both Grupo Torres and in Twinsectra different interpretations of his dicta were canvassed.[2] The problem was the approach to

take in interpreting the nature of a test which was on the one hand said to be objective, but on the other seemed in some way to incorporate subjective factors. That problem was faced and the test interpreted by the House of Lords in Twinsectra.

23. In Twinsectra, simply put, the court had to assess whether a solicitor, Mr Leach, was liable for assisting in the breach of a trust by another solicitor Mr Sims. Carnwath J at first instance held that there was neither a trust nor dishonest assistance. The Court of Appeal reversed both of these findings. The House of Lords upheld the finding that a trust had arisen. It however held that Mr Leach was not dishonest. In arriving at its decision on the dishonesty issue the Lords explained Lord Nicholls' test. In doing so two different interpretations were advanced: the majority view was developed by Lords Hutton and Hoffman, with whom Lords Slynn and Steyn agreed; the minority view by Lord Millett.
24. Looking first at the majority judgments, they interpreted Lord Nicholls' test as having two limbs. It was not a simple, straightforward objective test. It was a test which incorporated both an objective and a subjective aspect. It was a test which was in fact analogous to the test for dishonesty in the criminal law as set out in R v Ghosh. In Ghosh at page 1064 Lord Lane CJ stated the test for dishonesty to require the prosecution to prove:

    " . . whether according to the ordinary standards of reasonable and honest people what was done was dishonest. If it was not dishonest by those standards, that is the end of the matter and the prosecution fails.

    If it was dishonest by those standards, then the jury must consider whether the defendant himself must have realised that what he was doing was by those standards dishonest. In most cases, where the actions are obviously dishonest by ordinary standards, there will be no doubt about it. It will be obvious that the defendant himself knew that he was acting dishonestly. It is dishonest for a defendant to act in a way which he knows ordinary people consider to be dishonest, even if he asserts or genuinely believes that he is morally justified in acting as he did"

25. On this basis the majority in Twinsectra understood Lord Nicholls' test as one which required a court to ask itself two questions: first, was the defendant's conduct dishonest by the standards of reasonable and honest people (the objective element); and secondly, if it was, did the defendant realise that his conduct fell below that objective standard (the subjective element). Given what Lord Nicholls said about R v Ghosh and his seemingly explicit rejection of drawing analogies between equity and tests for dishonesty in other branches of the law this might appear, to say the least, a somewhat unusual conclusion to draw.
26. Lord Hutton's judgment gives the most detailed account of the majority view. He first noted (at para 27) that there were three possible ways in which dishonesty could be characterised: purely subjectively, the so-called Robin Hood standard, which is set by the individual himself; the purely objective, where the standard is the ordinary standard of reasonable and honest people; and a combined test – the Ghosh test. It might be noted at this point that Lord Hutton does not consider whether there is a fourth way to characterise dishonesty: that suggested by the provocation test.
27. He then went on to reject Lord Millett's analysis of Lord Nicholls' test as one which interpreted it as 'purely objective'. The upshot of this, he concluded, was that Lord Millett's analysis rendered dishonesty redundant and left liability once more resting simply on 'knowledge'. To my mind this was a striking conclusion to draw and a striking interpretation of Lord Nicholls' test if it accurately captures the essence of Lord Millett's analysis. Having rejected Lord Millett's analysis Lord Hutton then sought to explain the meaning of dishonesty by placing Lord Nicholls' reference to an objective standard in the wider context of his analysis. First, Lord Hutton noted that looked at 'in the context of the remainder of the paragraph' within which it was introduced the objective standard was being contrasted to the 'purely subjective standard' (at para 31). It is in this context that Lord Nicholls introduced his observation that 'Honesty has a connotation of subjectivity, as distinct from the objectivity of negligence.' Secondly, he noted that Lord Nicholls then went on to state that:

    "Ultimately, in most cases, an honest person should have little difficulty in knowing whether a proposed transaction, or his participation in it, would offend the normally accepted standards of honest conduct."

28. Lord Hutton concludes from this that Lord Nicholls must have intended the combined test:

> "The use of the word "knowing" in the first sentence would be superfluous if the defendant did not have to be aware that what he was doing would offend the normally accepted standards of honest conduct, and the need to look at the experience and intelligence of the defendant would also appear superfluous if all that was required was a purely objective standard of dishonesty. Therefore I do not think that Lord Nicholls was stating that in this sphere of equity a man can be dishonest even if he does not know that what he is doing would be regarded as dishonest by honest people."

29. Looked at in isolation I can see the force of Lord Hutton's conclusion. However it could be said that, looked at in context, Lord Nicholls was stating the exact opposite. Immediately after the sentence which Lord Hutton just quoted from Lord Nicholls' speech Lord Nicholls goes on to say this:

> "Likewise, when called upon to decide whether a person was acting honestly, a court will look at all the circumstances known to the third party at the time. The court will also have regard to personal attributes of the third party, such as his experience and intelligence, and the reason why he acted as he did."

30. Taking the two passages together, in the first Lord Nicholls adverts to what an honest person should know as he conducts his affairs. He should know what is honest or dishonest conduct, he should know this as he should have little difficulty in knowing what is honesty determined objectively. This passage focuses on how individuals should conduct their affairs. In the second passage Lord Nicholls focus turns to the Court. It turns to its task in assessing an individual's honesty: there is no question there of what the individual himself thought about his conduct. The court is to assess honesty by taking account of the individual's experience, his knowledge and his reasons for so acting. The court takes account of individual circumstances in making its assessment. There is no reference to the individual's self-knowledge. Taken together the two passages could just as well be interpreted as supporting the provocation test rather then the Ghosh combined test.
31. Finally, Lord Hutton concluded (at paras 35 - 37) that policy considerations lent further support to the combined test, to wit:

> "A finding by a judge that a defendant has been dishonest is a grave finding, and it is particularly grave against a professional man, such as a solicitor. Notwithstanding that the issue arises in equity law and not in a criminal context, I think that it would be less than just for the law to permit a finding that a defendant had been "dishonest" in assisting in a breach of trust where he knew of the facts which created the trust and its breach but had not been aware that what he was doing would be regarded by honest men as being dishonest."

32. Turning from Lord Hutton, what did Lord Hoffman say? In his speech he explicitly agreed with Lord Hutton that Lord Nicholls' test required a dishonest state of mind on the part of a defendant. In other words a defendant would have had to have been conscious of the fact that he was "transgressing ordinary standards of honest behaviour" (at 20): he supported the combined test. He furthermore explicitly rejected Lord Millett's judgment on the grounds that it departed from the 'principles laid down in Royal Brunei. . .' He held it departed from those principles because it held that:

> ". . . liability as an accessory to a breach of trust does not depend upon dishonesty in the normal sense of that expression. It (was) sufficient that the defendant knew all the facts which made it wrongful for him to participate in the way in which he did."

33. The majority view appears to be unequivocal: Lord Nicholls intended to introduce a combined test for dishonesty; and Lord Millett's analysis was to be rejected as it construed the test as purely objective.
34. Lord Millett took a different line. He opened his analysis by stating quite clearly that Lord Nicholls used the term dishonesty in an 'objective sense' (at para 114) - not a purely objective sense, but an objective sense. He also took the view that the reference to the Ghosh test by Lord Nicholls was not intended to introduce that test into equity. On the contrary he held that Lord Nicholls adverted to it in order to draw out a distinction between dishonesty as a state of mind and dishonesty as a course of action. The former, encapsulated by the combined test in the criminal law, was applicable to some

aspects of civil law, such as civil fraud (at para 116). Equally it could have applied to dishonest assistance if Lord Nicholls had maintained the requirement that the principal needed to be 'guilty of a fraudulent breach of trust' to give rise to accessorial liability. That element of dishonest assistance had however been rejected in Royal Brunei. The latter he held underpinned what Lord Nicholls meant by dishonesty. A number of points were identified as supportive of this view.

35. First, Lord Millett identified a number of instances where Lord Nicholls referred to a defendant's conduct in assessing liability. He noted, for instance, reference to 'acting dishonestly', 'advertent conduct' and the requirement that an individual must 'act honestly' (at para 118) in Lord Nicholls' opinion. Equally he noted that while Lord Nicholls opined that it would be usual to find that there was 'conscious impropriety' on the part of those liable for dishonest assistance, such a finding was not a condition of liability (at para 118). It is easy to see on this analysis how Lord Millett could conclude that the subjective element of the Ghosh test was not intended to form part of the test for dishonesty in dishonesty assistance. How could it, if consciousness of impropriety was no more than something that would usually be present where there was a finding of dishonesty? That which is usually, and thus not always, present cannot amount to a necessary condition of liability. Secondly, unlike the majority, Lord Millett found support in Lord Nicholls application of the test in Royal Brunei itself. He specifically noted that satisfaction of the second limb was not something which arose in that case (see para 120). If it had been, Lord Nicholls might have been expected to have addressed the issue. As he put it (at para 120):

    "There was no evidence and Lord Nicholls did not suggest that the defendant realised that honest people would regard his conduct as dishonest. Nor did the plaintiff put its case so high. It contended that the company was liable because it made unauthorised use of trust money, and that the defendant was liable because he caused or permitted his company to do so despite his knowledge that its use of the money was unauthorised. This was enough to make the defendant liable, and for Lord Nicholls to describe his conduct as dishonest."

36. In these circumstances I can readily see why Lord Millett would draw the conclusion that he then did at paras 121 - 122 that:

    ". . . Lord Nicholls was adopting an objective standard of dishonesty by which the defendant is expected to attain the standard which would be observed by an honest person placed in similar circumstances. Account must be taken of subjective considerations such as the defendant's experience and intelligence and his actual state of knowledge at the relevant time. But it is not necessary that he should actually have appreciated that he was acting dishonestly; it is sufficient that he was . . .

    The only subjective elements are those relating to the defendant's knowledge, experience and attributes. The objective elements include not only the standard of honesty (which is not controversial) but also the recognition of wrongdoing. The question is whether an honest person would appreciate that what he was doing was wrong or improper, not whether the defendant himself actually appreciated this."

37. A number of conclusions can be drawn from this. The most obvious is that Lord Millett hardly seems to be advocating a 'purely objective' reading of the test as the majority suggested. His explanation of the test is much more akin to the provocation test than a straightforward reasonable man test as that is understood in tort. Equally, it hardly seems to advocate the view that knowledge is the key to dishonest assistance. Lord Millett does not seem, as characterised by Lord Hutton, to seek to revert to the knowledge test rejected by Lord Nicholls. What Lord Millett does do is reject the use of 'dishonest' in the name of the action. He does this on the basis that courts are likely to be wary of labelling professionals dishonest (see para 133); which of course underpins Lord Hutton's analysis of the test. A warning about the power of words is one thing, whether it is also a conclusion that the substantive nature of a cause of action should change is another.
38. Whatever the relative merits of the majority and minority judgments, it might have been thought that Twinsectra would have been the end of the matter. However almost from the moment judgment was handed down the decision was the subject of sustained criticism from both the legal professional and academic communities. The complaints ranged from the charge that the majority misunderstood Lord Nicholls and Lord Millett i.e., that Lord Nicholls had not intended to introduce a combined test, that

the test was now too difficult to apply effectively, that the majority had once more muddied the waters as to the nature of accessorial liability and retarded its rationalisation across both equity and law, to the charge that the action was ripe for judicial abolition: see for instance: Tjio and Yeo, Knowing what is Dishonesty (2002) LQR 118 (Oct) 502; Panesar, A Loan subject to a Trust and Dishonest Assistance by a Third Party, Journal of International Banking Law (2003) 18 (1) 9; Andrews, The Redundancy of Dishonesty Assistance, Conveyancer and Property lawyer (2003) Sept/Oct 398.

39. This criticism was lent judicial support by obiter comments from the New Zealand Court of Appeal in 2003, when in US International Marketing Ltd v National Bank of New Zealand, the majority cast doubt on whether Twinsectra would be followed in New Zealand.[3] They particularly questioned the utility of the introduction of the subjective element of the Ghosh test into the action.
40. Criticism is one thing. In itself it does not alter the professional advisors' task in advising their clients as to the law and as to their responsibilities. Criticism thus does not have a negative impact on professional advice. However, it may well have had a significant impact on the development of the law because the Privy Council has recently revisited the majority's decision in Twinsectra.

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Barlow Clowes – Dishonesty

41. The Barlow Clowes case arose out of the infamous fraudulent off-shore investment scheme operated during the 1980s. As part of that scheme some of the investors' funds passed through bank accounts maintained by a Manx registered company called International Trust Corporation (Isle of Man) Ltd. The action was brought in the Isle of Man and was based on the allegation that the company and its directors had dishonestly assisted in the misappropriation of the investors' funds. The Acting Deemster, Hazel Williamson QC, held in favour of the investors. The three defendants appealed. Two appeals were dismissed. However one appeal, that of Mr Henwood, who was one of the directors, succeeded on the basis that the finding of dishonest assistance was not supported by the evidence. Barlow Clowes appealed that decision to the Privy Council.
42. The Privy Council's constitution on the appeal was perhaps uniquely qualified to provide guidance as to the appropriate test for dishonesty: both Lord Hoffman, and more importantly Lord Nicholls formed part of the constitution. Lord Hoffman delivered the Privy Council's opinion.
43. Lord Hoffman first of all noted that the Acting Deemster stated the test for dishonesty as set out by Lord Nicholls in Royal Brunei. The Judge's treatment of the test was summarised at paragraph 10 of the opinion in the following terms:

    ". . .(the Judge) said that liability for dishonest assistance requires a dishonest state of mind on the part of the person who assists in a breach of trust. Such a state of mind may consist in knowledge that the transaction is one in which he cannot honestly participate (for example, a misappropriation of other people's money), or it may consist in suspicion combined with a conscious decision not to make inquiries which might result in knowledge: see Manifest Shipping Co Ltd v Uni-Polaris Insurance Co Ltd [2003] 1 AC 469. Although a dishonest state of mind is a subjective mental state, the standard by which the law determines whether it is dishonest is objective. If by ordinary standards a defendant's mental state would be characterised as dishonest, it is irrelevant that the defendant judges by different standards."

44. The Acting Deemster, with whom the Manx appeal court agreed, thus interpreted the test as an objective one. Her judgment is on the face of it consistent with the interpretation given to the test by Mance J in Grupo Torras and by Lord Millett in Twinsectra. It would certainly appear to be inconsistent with Lord Hutton and Lord Hoffman's interpretation of the test in Twinsectra. Lord Neill QC, who represented the respondent, made submissions to that effect to the Privy Council; he highlighted that the test applied by the Acting Deemster made no reference to the subjective element of the Ghosh test.
45. The question was thus live before the Privy Council as to whether the majority in Twinsectra's interpretation was correct or not. Lord Nicholls would, to say the least, have had a unique insight into that question. The Privy Council first of all (at para 10) held that the Manx appeal court had correctly

stated the law. It further rejected (at para 18) Lord Neill's submission that the Acting Deemster had misstated the law. The finding (at para 18) bears setting out:

"Their Lordships . . . reject Lord Neill's submission that the judge failed to apply the principles of liability for dishonest assistance which had been laid down in Twinsectra. In their opinion they were no different from the principles stated in Royal Brunei Airlines v Tan which were correctly summarised by the judge."

46. The Twinsectra majority were thus correct. They were correct because they interpreted the test for dishonesty as an objective test, as stated by the Acting Deemster. The Privy Council implicitly acknowledged that some people, who it might be thought would include Lord Millett, could have been surprised by this. It did so in its discussion of Lord Hutton and Lord Hoffman's judgments. Again I can do no better than cite these passages in full:

"14. In submitting that an inquiry into the defendant's views about standards of honesty is required, Lord Neill relied upon a statement by Lord Hutton in Twinsectra Ltd v Yardley [2002] 2 AC 164, 174, with which the majority of their Lordships agreed:

"35. There is, in my opinion, a further consideration which supports the view that for liability as an accessory to arise the defendant must himself appreciate that what he was doing was dishonest by the standards of honest and reasonable men. A finding by a judge that a defendant has been dishonest is a grave finding, and it is particularly grave against a professional man, such as a solicitor. Notwithstanding that the issue arises in equity law and not in a criminal context, I think that it would be less than just for the law to permit a finding that a defendant had been 'dishonest' in assisting in a breach of trust where he knew of the facts which created the trust and its breach but had not been aware that what he was doing would be regarded by honest men as being dishonest.

"36. ... I consider that the courts should continue to apply that test and that your Lordships should state that dishonesty requires knowledge by the defendant that what he was doing would be regarded as dishonest by honest people, although he should not escape a finding of dishonesty because he sets his own standards of honesty and does not regard as dishonest what he knows would offend the normally accepted standards of honest conduct."

15. Their Lordships accept that there is an element of ambiguity in these remarks which may have encouraged a belief, expressed in some academic writing, that Twinsectra had departed from the law as previously understood and invited inquiry not merely into the defendant's mental state about the nature of the transaction in which he was participating but also into his views about generally acceptable standards of honesty. But they do not consider that this is what Lord Hutton meant. The reference to "what he knows would offend normally accepted standards of honest conduct" meant only that his knowledge of the transaction had to be such as to render his participation contrary to normally acceptable standards of honest conduct. It did not require that he should have had reflections about what those normally acceptable standards were.

16. Similarly in the speech of Lord Hoffmann, the statement (in para 20) that a dishonest state of mind meant "consciousness that one is transgressing ordinary standards of honest behaviour" was in their Lordships' view intended to require consciousness of those elements of the transaction which make participation transgress ordinary standards of honest behaviour. It did not also to require him to have thought about what those standards were."

47. The Privy Council were further bolstered in drawing the conclusion that Lord Hutton intended an objective test by the fact in Twinsectra that there was no discussion of, a finding, of subjective dishonesty by Mr Leach (see para 17). This was a point which, as I mentioned earlier, had been relied on by Lord Millett in his dissenting judgment.
48. In highlighting the ambiguity in Lord Hutton's judgment, and resolving it in favour of an objective approach, the Privy Council appear to have overlooked Lord Hutton's reference to Mrs Justice Steel's interpretation of the dishonesty test at paragraph 37 of Twinsectra. Lord Hutton held that:

". . . I consider that in Abbey National plc v Solicitors Indemnity Fund Ltd [1997] PNLR 306 Steel J applied the correct test. In that case, at p 310, she referred to the test set out in R v Ghosh [1982] QB 1053 and to Lord Nicholls's judgment in the Royal Brunei case [1995] 2 AC 378 and observed that it was to the effect that honesty is to be judged objectively, and she continued:

". . . Having read that case . . . it seems to me that the judgment does not set down a wholly objective test for civil cases. Lord Nicholls particularly refers to a conscious impropriety. The test there, it seems, does embrace a subjective approach, and I have to look at the circumstances to see whether they were such that Mr Fallon must have known that what he did was by the standards of ordinary decent people dishonest. I accept totally that individuals should not be free to set their own standards, but there is in my view a subjective element both in civil and in criminal cases.""

49. Putting that to one side, the simple fact of it seems to be that those who thought that the majority in Twinsectra interpreted the test for dishonesty as a combined test had misunderstood the majority's decision. It might equally be said that the majority and minority in Twinsectra had also misunderstood what each other meant: Lords Hutton and Hoffman misunderstood what Lord Millett held and vice versa. Every one agreed that the test was an objective one, i.e., the test did not require any enquiry into the defendant's subjective assessment of standards of honesty.
50. Equally now it seems that both the majority and the minority agreed that in order to ascertain whether the defendant was dishonest account needed to be taken of what he knew about the transaction. As the Privy Council explained the majority's judgment, in order to assess dishonesty a court needs to enquire 'into the defendant's mental state about the nature of the transaction.' By which it meant (see para 26):

" . . . what (the defendant) knew, said and did, both then and later, including what he said in evidence"

or, as Lord Nicholls originally put it in Royal Brunei:

"a court will look at all the circumstances known to the third party at the time. The court will also have regard to personal attributes of the third party, such as his experience and intelligence, and the reason why he acted as he did"

or, again as Lord Millett put it in Twinsectra:

"Account must be taken of subjective considerations such as the defendant's experience and intelligence and his actual state of knowledge at the relevant time."

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Conclusions

51. What conclusions can be drawn from this? The first point which I think can be acknowledged is that the Privy Council in Barlow Clowes found itself in a difficult position. The House of Lords' decision in Twinsectra, in explaining Lord Nicholls' test, had definitively stated the law. While the Privy Council can now, in exceptional circumstances, overrule definitive statements of the law of England and Wales made by the House of Lords, see the recent decision of the Court of Appeal Criminal Division in R v James [2006] EWCA Crim 14 per Lord Phillips CJ, there were no such exceptional circumstances in this case. The House of Lords' decision had however caused concern amongst practitioners and academics. It had resulted in uncertainty. It had resulted in questions being asked as to whether the House of Lords had correctly interpreted Lord Nicholls' test. Twinsectra was however a statement of English law. The Privy Council in Barlow Clowes could have explicitly declined to follow its interpretation of Lord Nicholls' test. It could have done so as that appeal concerned the law of the Isle of Man not England and Wales. Such an approach would have only given rise to further difficulties and uncertainty in the law and the Privy Council did not adopt it. With that in mind it is perhaps not surprising that the Privy Council took the approach it did: it sought to explain Twinsectra and did so consistently with Royal Brunei. It is also perhaps evidence of the strength of our common law system

that it is able to respond reasonably quickly and efficaciously to aspects of the law that are giving cause for concern.

52. The second point that can be made is that the decision has hopefully once more introduced clarity into this aspect of the law. The test is an objective one, but an objective one which takes account of the individual in question's characteristics, experience, knowledge etc. It is an objective test akin to the provocation test, although, mindful of the caveat I made earlier about alluding to tests from one context as a means to elucidate ideas expressed in other contexts, I would not characterise it as such. Nor would I recommend practitioners do so. It is a test which requires a court to assess an individual's conduct according to an objective standard of dishonesty. In doing so a court has to take account of what the individual knew, his experience, intelligence and reasons for acting as he did. Whether the individual was aware that his conduct fell below the objective standard is not part of the test. The wheel has turned full circle. Lord Nicholls is in the ascendant.
53. With that caveat in mind two wider conclusions can be drawn: first, this area of the law has been bedevilled by an inappropriate use of nomenclature. Legal tests have been explained by reference to the terms objective and subjective. These terms themselves are open, as this area of the law has shown so clearly, to multiple interpretations. They thus fail to elucidate the law but themselves stand in need of interpretation. They simply muddy the water. In future it might be better for the courts to eschew the use of such labels and simply say what they mean as clearly and unambiguously as possible. I realise that this may be a counsel of perfection.
54. The second wider conclusion that can be drawn is that arguing by analogy or by reference to related concepts in related disciplines can both assist elucidation and increase our understanding. It can bring the issues into sharp relief and it can highlight the fact that too much attention has been paid to issues that are actually inconsequential. On the other hand, unless care is taken, such an approach can be a source of confusion and error. It can lead the unwary to assume that what is valid in one context is equally valid in another; that a feature which is context-dependent is of universal application. We should exercise caution when drawing upon concepts from one branch of the law in order to elucidate ideas in another branch. We should take especial care where the branch we are examining, is, as equity in the form of dishonesty assistance or knowing receipt is, one where the law is developing. As the great Austrian philosopher Ludwig Wittgenstein might have put it, we should take care not to be bewitched by language.

Postscript

55. After this lecture was completed a note by Yeo in April's Law Quarterly Review came to my attention ((2006) 122 LQR April at 171). Yeo makes many of the points that I have made today although much more shortly and with greater clarity. He expresses uncertainty as to whether the English courts will follow Barlow Clowes. Although I say this without hearing argument on the point, my present view is that, as a unanimous decision of the Judicial Committee of the Privy Council, which included both Lord Nicholls, who was the progenitor of the test in Royal Brunei, and Lords Hoffman and Steyn, who formed half of the majority in Twinsectra, Barlow Clowes is likely to be followed by the English courts.
56. With that in mind I wait to see how the Barlow Clowes decision is greeted by practitioners, academics and the courts. I simply hope that this important area of the law will find the certainty it deserves. As we all know, hope springs eternal.

Footnotes

R Hunter, The Honest Truth about Dishonesty, Private Client Business 2002, 6, at 391.[Back to footnote 1]

Tjio and Yeo, Knowing what is Dishonesty, LQR (2002) 118 at 503.[Back to footnote 2]

[2004] 1 NZLR 589 [Back to footnote 3]