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REMEDIES FOR DISHONEST ASSISTANCE: HEARTBREAK HOTEL

HOTEL Portfolio owned a number of London hotels which had the potential to be redeveloped into luxury residences. The company was in financial trouble, and in December 2004 its creditors authorised its director, Mr. Andrew Ruhan, to accept any bid for the hotels above £125 million. At trial, that was found to be "consistent with an objectively reasonable market valuation of the hotels (with and without planning permission) at that time" ([2022] EWHC 383 (Comm), at [55]). In March 2005, a company known as Cambulo Madeira made a successful bid for the hotels. The sole shareholder of Cambulo Madeira was Euro Estates, a company associated with Mr. Anthony Stevens. Thereafter, the hotels were redeveloped or otherwise on-sold at a profit. The returns via Cambulo Madeira to Euro Estates were then applied by Mr. Stevens towards Mr. Ruhan's other development projects. At all times, Mr. Stevens (and through him, Euro Estates and Cambulo Madeira) was acting as Mr. Ruhan's nominee. Mr. Ruhan concealed his involvement from Hotel Portfolio's other directors, shareholders and creditors. Although the full extent of his reward for assisting Mr. Ruhan remained unclear, Mr. Stevens received at least a payment of £500,000 and a loan of £1 million "repaid" from the proceeds of sale.

Hotel Portfolio was by then insolvent. Through its liquidators, it brought proceedings against Mr. Ruhan and his entities for breach of fiduciary duty and an account of profits; and against Mr. Stevens and his entities for dishonest assistance and equitable compensation. At trial, Foxton J. found that Mr. Ruhan had committed *two* breaches of fiduciary duty in (1) concealing his initial involvement in the transactions, and (2) covertly applying the profits for his own use; and that Mr. Stevens had dishonestly assisted Mr. Ruhan in respect of both breaches ([2022] EWHC 383 (Comm), at [293]). The judge ordered Mr. Ruhan to account to Hotel Portfolio for £7.76 million (in respect of a hotel that was on-sold for a profit) and £94.5 million (in respect of hotels that were redeveloped); and ordered Mr. Stevens to pay equitable compensation in the same amounts of £7.76 million and £94.5 million ([2022] EWHC 1695 (Comm), at [29]).

Mr. Stevens appealed. He did not challenge the conclusion that he had acted as Mr. Ruhan's nominee, and had dishonestly assisted Mr. Ruhan's breaches of fiduciary duty; and he accepted that he was liable to account for the profits he or his entities made themselves. He also accepted that the profits derived from the sale or development of the hotels were held on constructive trust (a "true trust") for Hotel Portfolio, but he denied that there was any separate breach of duty constituted by Mr. Ruhan's failure to account for those profits, or their subsequent misapplication.

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Since the underlying transaction was for fair value, Mr. Stevens claimed that Hotel Portfolio had suffered no loss. Accordingly, he denied that he was liable for equitable compensation. There was no appeal by Mr. Ruhan. Referring to the supposed distinction between "substitutive" and "reparative" compensation, Hotel Portfolio claimed by a respondent's notice that the judge's award was justified because it was "substitutive" compensation for proper performance of the fiduciary's obligations as constructive trustee.

The Court of Appeal (Newey, Males and Birss L.JJ.) allowed Mr. Stevens's appeal ([2023] EWCA Civ 1120). The leading judgment was given by Newey L.J., with whom Males and Birss L.JJ. agreed. His Lordship observed that the judge's order did not "distinguish between different breaches of fiduciary duty by Mr Ruhan" (at [63]). It was thus not apt for Hotel Portfolio to claim that it was "seeking compensation for loss in respect of a different breach of fiduciary duty from that for which it has claimed an account of profits" (i.e. the subsequent misapplication of the profits, rather than the concealed interest in the original sale). Rather, "the sale was inextricably connected to the profits for whose loss [Hotel Portfolio] is seeking compensation", in which "Mr Stevens was involved from the start" (at [64]). Given the nature of property transactions, it was hardly surprising that there was a lapse in time between the sale and realisation of its profits: "there was no interruption in the implementation of Mr Ruhan's overall scheme or Mr Stevens' role in it. It simply took time to carry the scheme into effect" (at [65]).

The question whether Hotel Portfolio had suffered any loss "should be determined by reference to the total effect of Mr Ruhan's scheme". In that context, "the 'loss' stemming from Mr Ruhan's treatment of the profits must be balanced against the claim to recover those very profits which arose from the same plan" (at [67]). There was "a single and uninterrupted course of conduct which, taken as a whole, caused [Hotel Portfolio] no loss" (at [67]). Since Hotel Portfolio had suffered no loss, it was not entitled to any equitable compensation (at [69]). For that reason, it was unavailing for it to "invoke the (controversial) distinction between 'substitutive' and 'reparative' compensation" (at [69]). Further, where a claimant elects "for an account of profits instead of compensation as against the fiduciary", his Lordship "should not have thought that compensation could be sought from the dishonest assistant", because of the "need to choose between inconsistent remedies" (at [71]). More generally, "for there to be scope for a claim for compensation for loss from a dishonest assistant, the fiduciary should also be so liable" (at [71]).

Males L.J. agreed, and added observations "on the approach to be taken when a defendant has committed two breaches of duty" (at [77]). His Lordship emphasised that there were "two breaches of fiduciary duty by Mr Ruhan, in each of which Mr Stevens assisted" (namely, taking the

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concealed interest in Cambulo Madeira; and accruing the profits from the on-sale of the properties) (at [80]). By reference to *Bartlett v Barclays Bank Trust Co. Ltd. (Nos. 1 and 2)* [1980] Ch. 515 and *Brown v KMR Services Ltd.* [1995] 4 All E.R. 598, his Lordship suggested that there were "apparently conflicting authorities on the question whether a claimant is entitled to recover damages or compensation for a loss suffered as a result of one breach of duty while ignoring a gain obtained as a result of another breach of duty" (at [82]). The key to resolving any discrepancy was to be "found in the analogy with equitable set off, according to which set off arises when a cross claim is so closely connected with the claimant's demands that it would be manifestly unjust to allow the claimant to enforce payment without taking into account the cross claim" (at [84]). On the facts of the case:

> it would be manifestly unjust to hold Mr Ruhan (and hence Mr Stevens) liable to pay compensation for the profits for which he failed to account on sale of the hotels without taking into account that those profits could not have been obtained by [Hotel Portfolio] itself and were only obtained by Mr Ruhan as part of a single scheme to generate a profit from the development of the hotels. (at [85])

Viewed as a whole, the transaction caused Hotel Portfolio no loss, so Mr. Stevens was liable to account, "but only for the profits which he himself has made from assisting Mr Ruhan" (at [86]).

With respect, the Court of Appeal's decision joins a regrettable list of English appellate decisions that depart from fundamental equitable principles, and reward dishonest participation in profitable but insidious breaches of fiduciary duty. Another prominent example is *Novoship (UK) Ltd. v Mikhaylyuk* [2015] Q.B. 499 (see W. Gummow, "Dishonest Assistance and Account of Profits" [2015] C.L.J. 405). There are five main reasons for concern.

First, the prophylactic strength of the "no conflict" and "no profit" rules exists precisely to deter a fiduciary from taking concealed interests on both sides of a transaction, in the hope of future gain. It is common enough for an unauthorised transaction to be entered for fair value, and yet result in a subsequent uplift: see, for example, *Regal (Hastings) Ltd. v Gulliver* [1967] 2 A.C. 134, where directors subscribed for shares in their company; the company was taken over, and the shares were acquired from the directors for a substantial premium. In fields like property development (where gains may take many years to realise), it takes little imagination to see why a person owing fiduciary duties to an under-resourced seller might well be tempted to take a concealed interest in a buyer that is better resourced to complete the development. But the "no conflict" and "no profit" rules are distinct. To take a concealed interest is a breach of the "no conflict" rule even if no profit is ever realised; and

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an unauthorised profit is a breach of duty even if there is nothing furtive about the means by which it was obtained. A course of conduct by an errant fiduciary may involve multiple breaches of duty. It is wrong in principle to assimilate them to a single, original breach. Whether or not any later breaches are "inextricably connected" to the initial breach is irrelevant.

Second, it has always been irrelevant whether the beneficiary could themselves have realised the profits in fact obtained by the fiduciary. At least since *Keech v Sandford* (1726) 25 E.R. 233, it has been inapt to consider – as Males L.J. did – "that those profits could not have been obtained by [Hotel Portfolio] itself" ([2023] EWCA Civ 1120, at [85]). It was accepted that the fruits of Mr. Ruhan's breach of fiduciary duty were all along held on trust for Hotel Portfolio. It is, with respect, a perversion of equitable principle to suggest that the wrong constituted by the unlawful *diversion* of that trust property could be "set off" against the wrong constituted by its unlawful acquisition in the first place.

Third, although often labelled as "accessorial liability", liability for dishonest assistance is a direct, not derivative, liability imposed on the assistant. The label "accessorial" does "no more than recognise that the assistant's liability depends upon establishing, among other things, that there has been a breach of fiduciary duty by another"; and for that reason, the "relief that is awarded against a defaulting fiduciary and [an] assistant will not necessarily coincide in either nature or quantum" (*Michael Wilson & Partners Ltd. v Nicholls* (2011) 244 C.L.R. 427, 457–58, at [106]). It was an error of principle for Newey L.J. to consider that the available remedies against an assistant could be dictated by the election of a remedy against the fiduciary. A defaulting fiduciary and a dishonest assistant are distinct wrongdoers and commit distinct wrongs. There was no "need to choose between inconsistent remedies" when determining the relief available against the assistant alone ([2023] EWCA Civ 1120, at [71]). To the contrary, a "split election" between fiduciary and assistant is available (*Cassaniti v Ball* (2022) 109 N.S.W.L.R. 348, at [116]; *Xiao v BCEG International (Australia) Pty Ltd.* [2023] NSWCA 48, at [68]–[70]).

Fourth, if Mr. Stevens had *only* assisted in the dishonest abstraction of the proceeds of Mr. Ruhan's original breach of duty (which were accepted to have been held on trust for Hotel Portfolio), there would have been no difficulty in viewing his conduct as having caused loss to Hotel Portfolio (straightforwardly, the loss of the property held on trust). On what basis, then, could Mr. Stevens's position be *improved*, simply because he was involved in the dishonest plan from an earlier point? It seems remarkable to suggest that a latecomer would be exposed to a greater remedy than a person dishonestly involved from the outset.

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Fifth, and relatedly, why was it assumed that Mr. Stevens could not be jointly liable with Mr. Ruhan to account for the profits? The profits in question – from which Mr. Stevens was himself paid – "brought to fruition the scheme on which Mr Ruhan had embarked with the acquisition of the hotels", in which Mr. Stevens "was involved from the start" ([2023] EWCA Civ 1120, at [64]). There was "no interruption in the implementation of Mr Ruhan's overall scheme or Mr Stevens" role in it" (at [65]). Any gain and loss was "inextricably connected" as "part of a single scheme to generate a profit from the development of the hotels" (at [85]). The answer, in England at least, may be the apparent persuasive force of *Ultraframe (UK) Ltd. v Fielding* [2005] EWHC 1638 (Ch). But that is not the only available approach. Elsewhere, if a fiduciary and an accessory act in concert to secure a mutual benefit, they may be jointly and severally liable to account for the profits made (*Grimaldi v Chameleon Mining (No 2)* (2012) 200 F.C.R. 296, 416, at [558]). In the case of Mr. Stevens, the judge was "far from satisfied" that he had the "full picture" of the benefits he "derived from agreeing to act as Mr Ruhan's nominee" ([2022] EWHC 383 (Comm), at [269]). That underscores the wisdom of the Full Court's observation in *Grimaldi* – the bench including the late Paul Finn – that "when wrongdoers so entangle their affairs … the law as a matter of legal policy might wish to make it their responsibility – and not a claimant's – to untangle them for accountability purposes" ((2012) 200 F.C.R. 296, 416, at [558]).

Finally, the decision reveals a deeper conceptual problem. The "cardinal principle of equity" is that "the remedy must be fashioned to fit the nature of the case and the particular facts" (*Warman International Ltd. v Dwyer* (1995) 182 C.L.R. 544, 555). The technique of equity involves broadly expressed normative principles and flexible remedies, which are applied in a contextual and case-specific way so as to uphold – not undermine – the fundamental equitable duties of honesty and fair dealing on the part of fiduciaries. It is regrettable that, at least in some English courts – and not uniquely at the hand of judges – equitable principles are reduced to arid rules and empty catchphrases ("direct causal connection", "true trust", "substitutive" or "reparative" compensation). It is striking that the aridity of thought seems so often to operate in favour of, and not against, dishonest wrongdoers.

Equitable compensation is no narrow remedy, and it is not to be assimilated to rigid common law conceptions of damages or loss. Particularly in the case of actual dishonesty, it is difficult to see why a court of equity would strain to favour a wrongdoer. As McLachlin J. observed in *Canson Enterprises Ltd. v Boughton & Co.*: "[t]he basis of the fiduciary obligation and the rationale for equitable compensation are distinct from the tort of negligence and contract. … The fiduciary relationship has trust, not self-interest, at its core, and when breach

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occurs, the balance favours the person wronged" ([1991] 3 SCR 534, 543). Where an accessory's dishonest conduct assists the fiduciary to spirit away property held on trust and acquired in breach of duty, the justice of awarding equitable compensation seems clear.

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