

# Illegality: The 'range of factors' test and its likely impact

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## MASTERCLASS TRANSCRIPT

### Overview

This 22-minute video examines the defence of illegality – from its 18th century origins to the radical changes made by the Supreme Court in 2016.

Topics covered:

- An overview of the doctrine of illegality
- The origins of the defence of illegality
- The extent to which the illegality defence is used today
- The 1st limb: Was it illegal or immoral conduct?
- The 2nd limb: Is the cause of action founded upon that illegality?
- The facts of *Patel v Mirza*
- The 'range of factors' test explained
- The likely impact of the new test

Cases referenced:

- *Holman v Johnson* (1775) 1 Cowp. 341
- *Everet v Williams* (1725); see (1893) 9 L.Q.R. 197
- *Beaumont v Ferrer* [2016] EWCA Civ 768
- *Les Laboratoires Servier v Apotex Inc* [2014] UKSC 55
- *Tinsley v Milligan* [1994] 1 A.C. 340
- *Patel v Mirza* [2016] UKSC 42

## Presenter profile

### **Carl Troman, 4 New Square**

Based at 4 New Square, Carl Troman is a commercial litigator with particular expertise and experience in disputes involving insurance, professional liability, classic and super cars (including motorsports), property damage and costs. He is also a formally accredited mediator and acts as an arbitrator.

Carl is recommended as a leading junior in the fields of both insurance and professional negligence by Chambers & Partners 2016 – being described as "super-intelligent with great interpersonal skills", and "very user-friendly and good on tactics". Carl is also ranked in the 2016 Legal 500 and has been described as "outstanding" and "an accomplished advocate".

Before joining chambers in 2003, Carl taught law to undergraduates at the University of Reading.

## Introduction

**Carl Troman:** Hello and welcome to this masterclass on the subject of illegality. My name is Carl Troman and I'm a barrister and mediator in practice at chambers at 4 New Square. I'm a commercial litigator and my practice focuses on insurance disputes, professional negligence disputes and other commercial litigation.

I'm going to be talking today on the topic of illegality. In particular, I'm going to be identifying the background and history to the defence; some examples of how the defence has been applied in particular cases; the relevance of the defence to litigation and dispute resolution today; and some of the radical changes that have been made to the scope of the doctrine over the last couple of years, in both the Court of Appeal and the Supreme Court.

## An overview of the doctrine of illegality

There are two things to say by way of introduction about illegality:

1. The first is that it's a general defence and it's an absolute defence. So it applies to all different types of claim and it's not partial; it's complete.
2. The second thing to say is that there are two limbs to the defence of illegality. The first is that there needs to be some form of, what's described as 'illegal or immoral conduct'. And the second is that the cause of action that the claimant is advancing needs to rely upon, or be founded upon, that illegality or that immoral act.

## The origins of the defence of illegality

Most of the cases start by looking at the judgment of Lord Mansfield in *Holman v Johnson (1775) 1 Cowp. 341*. But actually, one can trace the defence of illegality further back than that to 1725, a case called *Everet v Williams (1893) 9 L.Q.R. 197*, which is actually worth mentioning because it's quite entertaining.

In that case, two highwaymen decided to form a partnership to rob people in north London and they were extremely successful in doing that. And as thieves do, they fell out. And there being no honour among thieves, one of them kept all of the proceeds. Now you might have thought that the other would take the law into his own hands to get his share. But no, he instructed a solicitor and he issues a writ in Chancery claiming that he would like his share of the partnership proceeds. You won't be surprised to know that the court had no truck with that, and it was struck out as scandalous and impertinent. But what also follows is the court was so incensed that this illegal claim should be brought, that they fined the solicitor who brought it a fairly large sum and committed him to the Fleet Prison until he paid the sum off. And that case, they all ended badly. Both of the highwaymen were eventually hanged and the solicitor was convicted of robbery and transported. So illegality has an interesting history.

## The extent to which the illegality defence is used today

Illegality is a defence that is a hot topic actually today. And just by way of example, in the last three or so years there have been at least half a dozen cases on illegality reach the Court of Appeal and the Supreme Court. So it's something that's argued about a lot, not only at first instance. But also the legal basis for it, has been hotly contested, particularly in recent years.

Just to give one example to show that the defence is not used in esoteric areas only, there was a personal injury case called *Beaumont v Ferrer* [2016] EWCA Civ 768 that reached the Court of Appeal last year. And that was a group of individuals who conspired together to avoid paying their taxi fare home after a night out. And the taxi driver, during the course of them leaping out of the taxi without paying, realised what they were doing and attempted to stop them by driving off. They were injured in the process and duly brought claims for personal injury against the taxi driver. Now those were good claims – the taxi driver owed them a duty; he breached that duty and they suffered loss as a result. But his defence of illegality succeeded because their entire claim was based on their own unlawful conduct, and so it was not right that their claims should succeed.

## The 1st limb: Was it illegal or immoral conduct?

The first limb of the illegality defence is looking at what is an illegal or an immoral act. Historically that has been a very difficult, muddled and tangled question, with a lot of inconsistent decisions. And recently, fortunately, we now have the decision of the Supreme Court in a case called *Les Laboratoires Servier v Apotex* [2014] UKSC 55 from last year, 2015. And that has clarified the law.

Lord Sumption gave the leading judgment in that case. And he identified two categories of conduct that count for the purposes of illegality:

1. The first is criminal acts. So acts that are contrary to public law – criminal and statutes.
2. The second is what he described as quasi criminal acts. So whilst not a breach of the criminal law, these are acts that involve some form of dishonesty or corruption.

And it's important to note – he drew the distinction between those two categories of acts on one hand, and then other civil wrongs on the other. So breaches of contract, negligence, nuisance – where there's no dishonesty involved – now they won't count for the purposes of the illegality defence. Whilst it might be regarded as unlawful to breach a contract, that's not enough to deprive somebody of the entirety of their remedy if they have a claim.

## The 2nd limb: Is the cause of action founded upon that illegality?

The second limb of the illegality defence goes back to the word used by Lord Mansfield in the *Holman* case “founding” a cause of action on illegality. And that's a concept that has really troubled the courts over the last 200 and odd years, since Lord Mansfield made that comment. And the problem was really identified by Lord Sumption in the *Apotex* case. He said that the courts have what he described as a “distaste” for applying their own rules. The point being that, in an individual case in front of a court, the judge may well

think that the rule to be applied leads to injustice in the case. And so what happens is the judge tries hard to forge a just remedy in the case.

But that leaves us with a body of case law that is inconsistent and very difficult to reconcile. And that was something that Professor Burrows, in his book<sup>1</sup> from this year, highlighted. He was particularly critical of the resort to Latin maxims to try and decide cases on illegality. What Professor Burrows said was that the courts were moving towards, and ought to move towards, what he described as a 'range of factors' test. Which is aimed at identifying broader policy considerations; looking at the case more generally; looking at all of the circumstances of the case, rather than trying to pin the answer on the application of one rule.

But actually what we have had until this year, is a relatively settled area of the law on founding. And that comes from a case called *Tinsley v Milligan* [1994] 1 A.C. 340. Prior to *Tinsley* there'd been a rather vague 'public conscious' test suggested by the Court of Appeal. But the House of Lords rejected that and identified what they called a 'reliance' test, which was really very straightforward. If a claimant needed to plead and rely upon their own wrongdoing, then their claim would fail for illegality. If on the other hand, a claimant did not need to plead and rely upon their own wrongdoing, then their claim could succeed; the defence of illegality would fail, even if the claimant had been guilty of some wrongdoing in relation to – or in the background of – the case.

It's best to give an example of that, I think. And probably *Tinsley v Milligan* provides the best example to find. In *Tinsley* a couple conspired together to defraud the Social Security Office. What they did is, they bought a home and put it in the name of only one of them, so that housing benefit could be claimed. Now when they fell out, there was a dispute as to who owned the property. The one of them who was registered said, well it's mine. And the other said, no, no I want my interest in that property; I contributed towards the property and there was a common intention between us that I should have an interest. And that claim for an interest in the property was defended by the registered owner, on the basis of an illegality defence; saying that the person claiming an interest was involved in wrongdoing – that being the defrauding of the Social Security Office – and so the claim should fail.

Now in the House of Lords, the claim succeeded and the illegality defence failed, because all the claimant needed to do was establish two things. Firstly, that she had contributed towards the property. And secondly, that there was a common intention that she should have an interest in the property, though not registered as the owner. And she didn't have to plead or rely on the fact that the background to that was defrauding the Social Security Office. And so because there was no need to rely on her own wrongdoing, the defence of illegality failed.

Now that has provided us, up until this year, with a relatively certain and settled basis upon which to look at the question of founding. Though it is fair to point out that there's been a lot of criticism of *Tinsley*. And one of the – to my mind – fair criticisms is that it can produce quite arbitrary results. And an example of that is that if the claimant in *Tinsley* had been the parent of the registered owner, then there would've been the presumption of advancement in relation to the contributions. Now in order to rebut that presumption, the parent would have had to have explained why those advances, those contributions, had been made, and that would have involved the parent relying upon their own wrongdoing. So it might be said that it's a rather

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<sup>1</sup> Prof. Andrew Burrows, *A Restatement of the English Law of Contract* (Oxford University Press, 2016)

arbitrary result, that on exactly the same facts one claim might succeed and one claim might fail for illegality. And that's – in part – why the decision has been criticised. But it did at least give certainty.

## The facts of *Patel v Mirza*

The big change for the defence of illegality this year, is the decision of the Supreme Court in *Patel v Mirza* [2016] UKSC 42. And that has radically changed the test for what it is to found one's cause of action on illegality. It's worth just mentioning the facts of *Patel v Mirza*. What happened in that case is that two people conspired to engage in some insider dealing. And to that end, the claimant transferred a large sum of money to the defendant to invest with insider information. Well these two were not only dishonest, but it turns out reasonably incompetent as well, because they couldn't actually get hold of the insider information. So there were no trades made using the money that the claimant advanced.

But as thieves do, they fell out with each other. And the defendant decided to trouser the cash and the claimant wanted it back. So the claimant sued for the return of the money on the basis of unjust enrichment; the failure of consideration for the contract. And predictably was met with the illegality defence; that this was a conspiracy to commit a criminal offence – insider trading being a criminal offence – as well as dishonesty. What happened in the case is that the defence of illegality failed and the claim succeeded.

Now that might be thought to be a surprising result. Because if one were applying the law from *Tinsley v Milligan*, the claimant in *Patel v Mirza* needed to explain to the court why the money had been transferred to the defendant, in order to show that the defendant had been unjustly enriched. And in order to explain why the payment had been made, the claimant would have had to have relied upon his own wrongdoing – in fact did have to rely upon his own wrongdoing. So under the *Tinsley* reliance test, the illegality defence would have succeeded, and the claim would have failed. But that's not what happened. The Supreme Court rejected the *Tinsley* reliance test, and instead applied what it described as the 'range of factors' test. And it was Lord Toulson who took the lead in applying the range of factors test.

## The 'range of factors' test explained

The range of factors test from *Patel v Mirza*, as described by Lord Toulson in the Supreme Court, means that one has to take account much more broadly of all of the circumstances of the case. It is not simply a question of whether the claimant is relying upon their own wrongdoing. And in particular, it's not just the circumstances of the case, but its wider policy considerations. So Lord Toulson said that the court has to look at not only the policy of preventing wrongdoers profiting from their own wrongs, but also more broadly at the integrity of the courts system, and whether denying or granting a remedy would, as it were, bring the court into disrepute. And so a much broader range of policy factors is brought into play. And what Lord Toulson drew on was the range of factors that Professor Burrows had identified in his book from this year.

But the test is not a precise one. And that's not me criticising it, that's Lord Toulson saying that it's not a mechanistic exercise, applying the test. He laid down no firm guidelines as to which factors a court ought to apply in a given case. Certainly, there's no list that a court has to go through by way of a tick box exercise to see if a factor is present or not. And really what the factors are is a holistic approach for the court to decide whether it thinks it's right to grant or deny relief.

I'll mention a couple of the factors. One is the seriousness of the conduct. And the other is the, what one might call, intentionality of the conduct. Those were two factors particularly identified by Lord Toulson. But even a brief look at those shows that they won't be all that easy to apply.

For example, the seriousness of the conduct. In order for illegality to work, conduct must either be contrary to the criminal law or involve some sort of dishonesty or corruption. It's hard to see how conduct will ever not be serious. And in relation to intention, while there are some crimes that can be committed unintentionally, if one's looking at civil wrongs – that's the quasi criminal category of wrongdoing – that has to involve dishonesty or corruption, and it's very difficult to see how there can be dishonesty or corruption committed unintentionally. So even the factors identified by Lord Toulson are not going to apply in every case, and are certainly not going to necessarily give the answer.

What Lord Toulson was really encouraging the courts to do was take a very broad-brush approach. And actually that picks up on something that Lord Sumption said in the *Apotex* case from last year, which is that if the courts want to move away from their distaste at applying their own rules, what needs to happen is that the rule of illegality needs to be transformed into a power that the court has, whether or not to deny or grant relief.

Now Lord Toulson in *Patel* expressly did not say that the rule was being replaced by a power. He treated the law as if it were a rule and not a power. But it's fair to say that it is a rule that very closely resembles a power. And one example of that, perhaps the key example: Lord Toulson said that it was important for the courts to look at proportionality when applying the rule of illegality. Now proportionality is obviously a well-known idea for the law. For example, in costs – are the costs of a case proportional to the piece of litigation? But that's a novel concept for illegality, which is an all or nothing defence. And so it's quite hard to see how proportionality can come into the question of whether an illegal act ought to prevent a claimant from recovering. But Lord Toulson specifically talked about courts being wary of the risk of "overkill" as he called it. And so this idea of proportionality has come in, which as I say looks very much like the transformation of a rule into a power.

## The likely impact of the new test

It remains to be seen what the impact of the *Patel v Mirza* test is going to be across a broad spectrum of different cases. But one can readily identify that the much broader nature of the range of factors test is very likely to lead to uncertainty in the law. What we had under *Tinsley* was a precise test. It may well be criticised for being arbitrary, but we did at least have the ability to predict with some certainty what the outcome is going to be of a particular case.

Now, under the *Patel* case, we're looking at a range of factors. It's going to be extremely difficult for lawyers to advise their clients which particular factors in a given case are going to be seized upon by a judge as the most important factors, and determinative of the decision. No longer do we have a relatively predictable test.

What we've moved to is the idea of being able to do more justice in a given case. No one can disagree with that as a good idea. But it also means that there is considerable uncertainty as to what the outcome of a case will be. Now that's not desirable for litigants, because it means that litigation is more likely over the question of illegality, because it will be harder to predict what the outcome will be. There will be a broader

range of opinion as to how the range of factors is going to be applied. And in truth, what that means is more cases are likely to settle. Because there are relatively few litigants who have a large appetite for risk, and for taking cases all the way to the end of an expensive and unpredictable trial. And one might say, that if more cases are settling, then that isn't actually doing justice in an individual case. Because the essence of a settlement is not justice being done, it is a commercial compromise between the parties.

And so we come back to what Lord Sumption said in the *Apotex* case, which is if the courts have distaste for applying their own rules, then the rule needs to be transformed into a power. Well in my view, the rule has in effect become a power. Now while that might give a judge a larger number of tools to do what he or she thinks is right in an individual case, I think it is likely to lead to considerable uncertainty.