Stevensdrake Limited v Hunt - CFA not binding on liquidator

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Case: Stevensdrake Limited (trading as Stevensdrake Solicitors) v Stephen Hunt and Stephen Hunt as liquidator of Sunbow Limited [2016] EWHC 342 (Ch) and [2016] EWHC 1111 (Ch)

Synopsis: A liquidator was not bound by the terms of a conditional fee agreement entered into with a firm of solicitors where collateral dealings between the liquidator and the firm were inconsistent with those terms. This case demonstrates the importance of clarity as to the exact terms of a conditional fee agreement, particularly if they significantly depart from previous dealings. It is also a reminder that whilst there may be a general understanding that, in minimal value or no asset insolvency cases, parties act on a recoveries only basis with no attaching personal liability, this is not a formal agreed practice in insolvency litigation; the indemnity principle being key.

Topics covered: Liquidator's powers and duties; Litigation funding and costs

The Facts

Stevensdrake Limited, which carried on business as Stevensdrake Solicitors (SL) claimed against Stephen Hunt (SH) for outstanding fees due under a Conditional Fee Agreement (CFA) made between SL and SH dated 10 April 2008. The CFA related to work done in furtherance of an application under s212 IA1986 against the former administrators of Sunbow Ltd, of which SH had become liquidator. The partner acting at all material times on behalf of SL was GP. The CFA provided for an uplift of 100% on SL's base costs as a success fee.

The original terms of SL's engagement in 2005 were on the basis of a general retainer, signed and returned by SH, which modified SL’s standard terms of business by providing an assurance that, except in relation to out-of-pocket expenses, SL would wait for payment of its charges until recovery of any assets in the estate, regardless of source. In April 2006, SH sent GP a letter stating that SL's fees could only be paid out of realisations; if there were no realisations, he would not be in a position to pay those fees, nor would he accept personal liability for them and that if SL was not willing to act on that basis, all relevant papers should be returned to him. GP replied by email, stating that, although he would require disbursements to be paid, he was "happy to wait for payment of our costs until you make a recovery from any source".

In 2008, the litigation was ongoing and GP sent a CFA to SH, which included provisions that SH would be personally liable for fees, disbursements and a success fee, should the litigation be successful, which SH signed.

In 2009 and 2011 the first and second administrators each settled the claims against them. Each compromise satisfied the definition of "success" under the CFA. When the first compromise was reached, the money was apportioned between SL, SH and counsel on a proportionate basis. SL issued a bill with base costs of £397,686.24 and a 100% success

fee in 2014.

SH and GP had worked together on insolvency matters for many years. SH argued that there was a recognised and established practice in the field of insolvency litigation against estates where there are minimal or no assets of value which is summarised as follows:

- to secure instructions, solicitors and counsel offer to provide their legal services on terms that they will become entitled to payment only out of recoveries made;
- to the extent that there are insufficient recoveries, the entitlement to payment would abate pro rata;
- nevertheless, so as not to breach the indemnity principle, the strict legal rights created by conditional fee agreements stipulate that success in litigation triggers liability to pay fees; and
- it is known and understood that the parties will not enforce their strict legal rights but operate Recoveries Only Liability (the Practice).

SH argued that the Practice was an established method of working between SH and GP, and was expressly adopted in relation to the Sunbow liquidation and the s212 claims against the former administrators. He claimed that if the court found him personally liable the claim should be barred by:

- estoppel by convention (the solicitors had previously agreed to be paid on a recovery basis); and/or
- undue influence, negligence and breach of fiduciary duty on the part of SL for not highlighting the more onerous terms of the CFA.

Therefore the main issue to be considered by the court was whether the terms of the CFA were affected by the terms of the April 2006 letter and GP's reply which acknowledged waiting for recoveries in the estate before invoicing.

The Decision

Terms of the CFA

The court ruled that the agreement reached between SL and SH in 2008 could not be ascertained from the terms of the CFA alone and that, on the facts, the consistent conduct of the parties over a long period of time imported a term that SL's fees would only be paid out of the realisations (such that an invoice could not be rendered until a recovery was made) and that SH has no personal liability for those fees.

In reaching this decision and considering the conduct of the parties the court referred to *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50 [14]. This case established that the key to constructing a commercial contract is to determine what the parties meant by the language they used, assessed by considering what a reasonable person, having all the background

knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract, would have understood the parties to have meant.

It was also noted that the court could not improve the terms of the CFA, and that implication of a term is not to have the effect of adding to the CFA, but only spelling out what it actually means (*Attorney General of Belize v Belize Telecom Ltd* [2009] UK PC 10),

The judge recognised that his decision ran contrary to the express terms of the CFA and to the principles governing construction of and the implication of terms into, a contract. However, he said that the sheer volume, and weight of the contemporaneous evidence of the parties' actions and behaviours was in favour of this decision and did not allow any other conclusion.

Obiter

The court's comments on other points in SH's defence were obiter, given the decision reached, but contain some useful points to remain mindful of when using CFAs. Had there been a been a need to address the further points, the following was observed:

- Whilst the judge recognised the Practice as being a practical means used in the public interest which he described as *"the elephant in the room",* it did not override the indemnity principle;

- the numerous communications, written and verbal, between SH and SL supported SH's argument that the solicitors were estopped by convention from recovering their fees personally from SH. It would be unjust to allow the solicitors to depart from this (applying *Republic of India and Others v India Steamship Company Ltd* [1997] UKHL 40 and *Dixon and another v Blindley Heath Investments Ltd and another* [2015] EWCA Civ 1023).

- SL would have been presumed to have exercised undue influence over SH when introducing the CFA which imposed personal liability on SH for the first time in a retainer with SL and contrary to previous agreed working arrangements. The solicitors could not, in good conscience, do other than expressly draw this to SH's attention, particularly given that SH had made it clear to the solicitors on a number of occasions earlier in their professional relationship that, if the solicitors proposed that he take on personal liability for their fees, he would terminate their retainer. This failure would also be considered negligent and in breach of solicitor's fiduciary duty to SH.

Consequential Judgment

Following the handing down of judgment, SL sought an order for the payment by SH of a sum equal to the monies which had been apportioned to SH and counsel following the settlement with the first administrator, on the basis that SL was entitled to receive all realisations.

In a second judgment, HHJ Barker QC rejected that claim. He held that by entering into the agreed apportionment, SL clearly and unequivocally agreed to permanently forego its rights in relation to those monies and that the doctrine of promissory estoppel applied.

Comment

This case illustrates the care needed generally by solicitors when entering into fee retainers and the need for actions in practice to fully reflect the written terms agreed. This case was extremely fact specific and the weight of the evidence supporting the recoveries only analysis was significant. The obiter comments regarding breaches SL may have committed if the CFA had operated on its express terms serve as a useful reminder for both insolvency practitioners (IPs) and their advisors to have absolute clarity as to the effect of a CFA. This clarity between IP and advisor is even more important given that IPs are now no longer able to recover their CFA success fee from the other party as part of a costs award.

The post script considers whether working on a recoveries only basis offends the indemnity principle. However, whilst the Judge did not endorse the public interest practice of working on a recoveries only basis, he did recognise that such a practice exists. It therefore remains an available tool in future cases, provided the terms are express.