COMMERCIAL FRAUD:
CIVIL LIABILITY

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INTRODUCTION

Civil Fraud

1 In *HIH Casualty & General Insurance Ltd & Ors v Chase Manhattan Bank & Ors*¹, Lord Bingham used the following words in relation to cases of civil fraud:

“…. fraud is a thing apart. This is not a mere slogan. It reflects an old legal rule that fraud unravels all: *fraus omnia corrumpit*. It also reflects the practical basis of commercial intercourse. Once fraud is proved, "it vitiates judgments, contracts and all transactions whatsoever"…….. Parties entering into a commercial contract will no doubt recognise and accept the risk of errors and omissions in the preceding negotiations, even negligent errors and omissions. But each party will assume the honesty and good faith of the other; absent such an assumption they would not deal.”

2 A definition adopted by Janet Ulph in her recent work Commercial Fraud is as follows:

“the dishonest non-violent obtaining of some financial advantage or causing of some financial loss”.

Growth

3 The number of cases brought to trial involving allegations of fraud has increased over the last 5 years. A keyword word search using “deceit”, “fraud” and “fraudulent misrepresentation” of civil/commercial cases (excluding insurance) on Lawtel for 2006, 2007 and the first half of 2008 shows the following results for reported hearings including fraud as a liability issue:

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4 This data identifies only those cases that have proceeded to judgment and represents only the tip of the iceberg of those cases in which fraud is pleaded as a cause of action and settle, or are withdrawn, before judgment.

¹ [2003] UKHL 6 @ [15]
² In 13 of these actions, the Court made one or more findings of fraud/deceit. For 2008 to date, the figure is 3 out of 7.
In a digital and information rich age, a fraud may be perpetrated by the dishonest obtaining and use of confidential information as well as by the direct appropriation of funds. The growing confidence in international business in “emerging markets” and in business conducted without no or very limited face-to-face meetings may prove to be a fertile ground for legal work in this area.

It is also generally accepted that during economic downturns, there is an increase in the incidence of commercial fraud. The recent global “credit crunch” may well cause an increase in this area of work.

Scope of this presentation/paper

For reasons of time and space this paper focuses only on the torts of deceit and fraudulent misrepresentation.

It therefore excludes a range of disputes based on civil fraud; e.g.
1. equitable claims against dishonest trustees/fiduciaries and insurance disputes (claims or avoidances) where special rules as to good faith apply;
2. civil claims arising out of conspiracy and bribery;
3. personal and corporate insolvency proceedings;
4. professional liability claims concerning the detection of fraudulent transactions; e.g. those concerning auditors, accountants and solicitors.

THE CAUSES OF ACTION
Deceit and fraudulent misrepresentation

There is no distinction in law between the torts of deceit and fraudulent misrepresentation.

The torts occur:
“Where a defendant makes a false representation, knowing it to be untrue, or being reckless as to whether it is true, and intends that the claimant
should act in reliance on it, then in so far as the latter does so and suffers loss the defendant is liable for that loss. 3

What must be proved?

11 The requisite ingredients of the cause of action are:

1. A false representation of fact made to the claimant 4;
2. A dishonest state of mind by the representor 5;
3. An intention that the claimant relies on the representation 6;
4. Reliance by the claimant on the representation 7;

3 Clerk & Lindsell on Torts 19th Ed para 18-01
4 Analysis of a potential case must start by clearly identifying the representation(s) relied on; e.g. AIC Ltd v ITS Testing Services (UK) Ltd (“The Kriti Palm”) [2006] EWCA Civ. 1601 @ [254]. There are, of course, many cases based on misleading conduct, half-truths and concealment of fact(s). In relation to an ambiguous representation, it is necessary to prove that the representor intended it to be understood in its untrue sense, or at the lowest intended to use the ambiguity to deceive the representee; see e.g. Akerhielm v De Mare [1959] AC, The Kriti Palm [253]-[254].

In this context the word “fact” is deemed to include “present intention”. Thus, a statement of present intention is a representation of fact; see the well-known case of Edgington v Fitzmaurice (1885) 29 ChD 459: “The state of a man’s mind is as much a fact as the state of his digestion.” Whether a statement as to the future contains an implied representation as to present intention can be an interesting and sometimes difficult question.

Statements of opinion and projections as to the future are not, of themselves, representations of fact but are generally treated as including a representation that the maker does genuinely hold that opinion when made. There remains, of course, the forensic difficulty of proving against the representor what his real opinion was. A statement of opinion may also contain an implied representation that the representor believes that facts exist which reasonably justify that opinion; see e.g. The Kriti Palm [2006] EWCA Civ. 1601 @ [255], Barings plc (In Liquidation) & Anr v Coopers & Lybrand (a Firm) [2002] P.N.L.R. 823, [2002] EWHC (Ch) 461. Pure sales talk is excluded.

5 It remains conventional (see The Kriti Palm (supra) @ [256]) to refer to the speech of Lord Herchell in Derry v Peek (1889) 14 App. Cas. 337 @ 376 on this point:
“First, in order to sustain an action in deceit, there must be proof of fraud and nothing short of that will suffice. Secondly, fraud is proved when it is shown that a false representation has been made (i) knowingly, (ii) without belief in its truth, or (iii) recklessly, careless whether it be true or false. Although I have treated the second and third as distinct cases, I think the third is bit an instance of the second, for one who makes a statement under such circumstances can have no real belief in the truth of what he states. To prevent a false statement from being fraudulent, there must, I think, always be an honest belief in its truth.”

The concept of recklessness has been described in this context as “a species of dishonest knowledge, for in both cases there is an absence of belief in truth.” The Kriti Palm (supra) @ [257]. For a recent example of a finding of fraud at trial on proof of recklessness alone; see Facta & Ors v Prew-Smith & Anr [2006] EWHC 730 (Comm) @ [45].

6 Generally, the representation will have been made to the claimant. However, a representation made to a third party with the intention that it would be passed on to the claimant to be acted on and relied on by him will suffice, if it is passed on and acted and relied on. What must be shown is an actual intention to deceive the claimant. The precise identity of the claimant need not be known when the false representation is made, provided that he belongs to a class of persons with the contemplation of the defendant as likely and intended to be deceived by the misrepresentation; Abu Dhabi Investment Company & Ors v H Clarkson Ltd & Ors [2008] EWCA Civ. 699 @ [33] – a corporate structure case.
Financial loss to the claimant caused by the above.

Special relationship/voluntary assumption of responsibility/reasonable foreseeability
12 There is no requirement to prove the existence of a special relationship between the parties, that the defendant voluntarily assumed legal responsibility for his statement or that a loss was reasonably foreseeable. In distinction to claims in negligence for financial loss, the control mechanisms of deceit are the requirements of dishonesty, intention to mislead and reliance by the claimant.

The standard of proof
13 The standard of proof for fraud is the ordinary civil standard of the balance of probabilities. However, in respect of issues dependent on the representor’s state of mind, the courts adopt the approach described in the following well-known extract from the speech of Lord Nicholls in Re H (Minors) (Sexual Abuse): (Standard of Proof): "When assessing the probabilities the court will have in mind as a factor, to whatever extent is applicable in the particular case, that the more serious the allegation the less likely it is that the event occurred and hence the stronger should be the evidence before the court concluded that the allegation is established on the balance of probability. Fraud is usually less likely than negligence ….. The more improbable the event, the stronger must be the evidence that it did occur before, on the balance of probability, its occurrence will be established."

7 There is a (rebuttable) presumption that the recipient of a fraudulent misrepresentation was influenced by it; Dadourian Group International v Simms [2006] EWHC 2973 (Ch). In addition, a finding that the representee would have acted in the same way absent the representation, does not exclude a finding of influence. It has been said that the only sure way for a defendant to avoid liability on the ground of no influence is to show that the representee would have acted in the same way even if he knew the true facts concealed by the representation. The claimant is not required to prove that his reliance was reasonable or that the representation was the sole cause of his action. He need only prove that he did rely on it and that it was a substantial contributing cause of his action.
9 There has been a difference of approach at first instance as to whether this modified burden of proof applies (a) only to issues dependent on the representor’s mind (e.g. absence of belief of truth and intention to mislead) or (b) all the ingredients of the tort. As to approach (a) see Tugendhat J in GE Commercial Finance Ltd v Gee [2005] EWHC 2056 (QB) @ [122]. As to approach (b) see Steel J in Uzinterimpex JSC v Standard Bank plc[2007] EWHC 1151 (Comm) @ [106]
10 [1996] AC 563 @ 586-587
In re B (Children) (FC)\textsuperscript{11}, Lord Hoffman, with whom the other members of the House of Lords agreed, was at pains to make the following clear:

“I think that the time has come to say, once and for all, that there is only one civil standard of proof and that is proof that the fact in issue more probably occurred than not…..

……. I should say something about the notion of inherent probabilities. Lord Nicholls said, in the passage I have already quoted, that

“the court will have in mind as a factor, \textit{to whatever extent is appropriate in the particular case}, that the more serious the allegation the less likely it is that the event occurred and, hence, the stronger should be the evidence before the court concludes that the allegation is established on the balance of probability.”

15. I wish to lay some stress upon the words I have italicized. Lord Nicholls was not laying down any rule of law. There is only one rule of law, namely that the occurrence of the fact in issue must be proved to have been more probable than not. Common sense, not law, requires that in deciding this question, regard should be had, to whatever extent appropriate, to inherent probabilities. If a child alleges sexual abuse by a parent, it is common sense to start with the assumption that most parents do not abuse their children. But this assumption may be swiftly dispelled by other compelling evidence of the relationship between parent and child or parent and other children. It would be absurd to suggest that the tribunal must in all cases assume that serious conduct is unlikely to have occurred. In many cases, the other evidence will show that it was all too likely. If, for example, it is clear that a child was assaulted by one or other of two people, it would make no sense to start one’s reasoning by saying that assaulting children is a serious matter and therefore neither of them is likely to have done so. The fact is that one of them did and the question for the tribunal is simply whether it is more probable that one rather than the other was the perpetrator.”

\textbf{Contributory negligence}

15 This defence is inapplicable to a claim in fraud\textsuperscript{12}. A defendant is not, for example, permitted to defend a case on the basis that the representee undertook his own investigation/due diligence into the relevant facts\textsuperscript{13} or was simply foolish to take him at his word.

\textsuperscript{11} [2008] UKHL 35
\textsuperscript{12} Law Reform (Contributory Negligence) Act 1945, \textit{Standard Chartered Bank v Pakistan National Shipping Corp’n} (Nos 2 & 4) [2003] 1 AC 959, [2002] UKHL 43
\textsuperscript{13} \textit{Abu Dhabi Investment Company & Ors v H Clarkson Ltd & Ors} [2008] EWCA Civ. 699 @ [28], “There is no principle that a party who undertakes due diligence necessarily ceases to rely on representations that have been made”, [30]
LIABILITIES

Personal

An individual making a fraudulent misrepresentation or acting deceitfully is personally liable in tort regardless of the fact that he may also act as an agent or officer of a company or other entity; *Standard Chartered Bank v Pakistan Shipping Corp.* 14 where Lord Hoffman used the following words [22]:

“No one can escape liability for his fraud by saying “I wish to make it clear that I am committing this fraud on behalf of someone else and I am not to be personally liable.”

The live issue is usually whether an employing party, principal or other entity is also liable for fraudulent acts and statements by the individual.

Joint

Aside from the tort of conspiracy, two persons may be (jointly and severally) liable in respect of the same dishonest act or enterprise 15. The fact that two or more individuals act in pursuit of a joint enterprise may be inherently less probable than a single individual acting alone. However, subject to that point on the standard of proof, findings of fraud and joint and several liability may be found without proof of a conspiracy; see e.g. *Abu Dhabi Investment Co. & Ors v H Clarkson & Co. Ltd & Ors.* 16

Vicarious

The principle of vicarious liability applies in respect of the dishonest acts or statements of an employee. The starting point is therefore that an employer is liable in tort if the facts said to constitute the fraud took place during the course of the individual’s employment 17.

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15 “It would appear that the question of whether a person is a party to a combination constituting a conspiracy is essentially the same as whether he is liable as a joint tortfeasor in procuring a wrong, by reason of a common design” Clerk & Lindsell on Torts 19th Ed @ 25-120
16 [2007] EWHC 1267 (Comm) @ [263], [271]
17 Lister v Hesley Hall Ltd [2002] 1 AC 215, [2001] UKHL 22. In *Credit Lyonnais Nederland NV v Export Credits Guarantee Department* [2000] 1 AC 486 a claim in fraud was dismissed because the individual acted only as an accomplice to the fraudster for whom the employer was not liable. See also
In relation to fraud this general principle has been limited by the further requirement that it must be shown that the dishonest individual had actual or ostensible authority to make the fraudulent statement\textsuperscript{18}.

**Attributed**

A company may also be directly liable for dishonest acts by reason of the attribution to it of its dishonest “mind and will”\textsuperscript{19}. The essential difference between the concepts of vicarious liability and attribution lies in the degree to which the relevant agent is identified with the company. If a junior employee commits a fraud in the course of his employment, the company will be vicariously liable for the fraud, but the fraud will not automatically be imputed to the company itself. However, if the board of directors resolves on the commissions of a fraud by the company their dishonesty will be attributed to it and the company will be directly liable.

**Principal and agent**

A principal is not liable in tort for its agent’s dishonesty. For a principal to be liable in contract for the fraudulent tort of his agent it must be shown that the representations were made within the scope of the agent’s actual or ostensible authority\textsuperscript{20}.

**PLEADING FRAUD**

The courts have emphasised consistently that “charges of fraud should not be lightly made or considered”\textsuperscript{21}. A plea of fraud must be properly particularised and permit the recipient to respond to a series of specific allegations without any embarrassment\textsuperscript{22}. A specific recent example of the application of this rule was the refusal to grant permission for an

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\textsuperscript{18} e.g. \textit{Armagas Ltd v Mundogas SA} [1986] AC 717

\textsuperscript{19} Meridian Global Funds Management Asia Ltd v Securities Commission [1995] 2 AC 500, Moore Stephens (a firm) v Rolls & Stephens Ltd (in liquidation) [2008] EWCA Civ. 644 @ [24]

\textsuperscript{20} see e.g. Bowstead & Reynolds on Agency (17th Ed) @ 8-183

\textsuperscript{21} e.g. \textit{Mason v Clarke} [1955] AC 778 @ 794 (Viscount Simonds)

\textsuperscript{22} e.g. \textit{Belmont Finance Corp Ltd v Williams Furniture Ltd} [1979] Ch 250
amendment to plead fraud (and fraudulent breach of trust) in an action between the two well-known Russian oligarchs, Berezovsky and Abramovich, on the ground that there was no draft claim making this case “explicit”23. This requirement has become all the more important since the introduction of the requirement that a party must support his Statement of Case with a Statement of Truth.

24 The current (8th Ed) of the Code of Conduct (Part VII – Conduct of Work by Practising Barristers) provides as follows:

“704. A barrister must not devise facts which will assist in advancing the lay client's case and must not draft any statement of case, witness statement, affidavit, notice of appeal or other document containing:

(a) any statement of fact or contention which is not supported by the lay client or by his instructions;
(b) any contention which he does not consider to be properly arguable;
(c) any allegation of fraud unless he has clear instructions to make such allegation and has before him reasonably credible material which as it stands establishes a prima facie case of fraud;”

25 An important qualification on para 704(c) is that the evidence establishing a prima facie case need not be admissible in court, and may, for example, be protected by legal professional privilege24.

26 Conduct of a fraud claim will involve a closer analysis of the Statements of Case than in a comparable civil claim where fraud is not pleaded. The respondent to a plea of fraud should ensure that the cause of action is set out with a high degree of specificity. There are, of course, also tactical reasons why a party responding to a plea of fraud will want to examine the evidence available to the party alleging fraud at the first opportunity.

23 Berezovsky v Abramovich [2008] EWHC 1138 (Comm) @ [13]
EXCLUSION OF LIABILITY FOR FRAUD

Personal, vicarious and attributed liability

For reasons of public policy, a contracting party is not permitted to exclude liability for his own fraud in inducing the making of a contract; see e.g. *HIH Casualty & General Insurance Ltd & Ors v Chase Manhattan Bank & Ors*.

Principal and agent

*HIH Casualty* did not finally decide that the same rule should apply to a contracting party who sought to exclude liability for the fraud of his agent inducing a contract between it as principal and the counter-party. However, Lord Bingham said that very clear evidence of a shared intention between the contracting parties would be required to permit exclusion:

“For it is in my opinion plain beyond argument that if a party to a written contract seeks to exclude the ordinary consequences of fraudulent or dishonest misrepresentation or deceit by his agent, acting as such, inducing the making of the contract, such intention must be expressed in clear and unmistakable terms on the face of the contract.”

The House found an exclusion clause in the following terms inadequate to exclude liability for the fraud of an agent:

“the Insured will not have any duty or obligation to make any representation, warranty or disclosure of any nature, express or implied (such duty and obligation being expressly waived by the insurers) and shall have no liability of any nature to the insurers for any information provided by any other parties”

SOME EVIDENTIAL POINTS

The inherent nature of a fraud allegation, the skill and experience of the alleged fraudster and the exacting legal requirements as to proof all require a party prosecuting a case in fraud to take steps to ensure it has access to the fullest documentary (paper and electronic) evidence available.

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25 [2003] UKHL 6 @ [16]. For a recent application, see *Six Continents Inc. v Event Hotels GmbH* [2006] EWHC 2317 (QB) @ [48]
26 Ibid
This requirement is heightened by the requirement that the Statement of Case is supported by a Statement of Truth and by the specific professional guidance applicable to pleading allegations of bad faith (see paragraphs 24–25 above).

This paper considers below two evidential issues considered recently by the courts:

**Pre-action disclosure**

An application under CPR 31.16(3) for pre-action disclosure in respect of a prospective plea of fraud is governed by the same principles as an application in respect of a non-fraud case. In *Black & Ors v Sumitomo Corp. & Ors*, Rix LJ said:

“At a general level there are clearly concerns that allegations of dishonesty are not lightly made, that a defendant to an allegation of dishonesty knows plainly what it is that is alleged against him, and also that dishonesty does not spread its cloak over the means by which it can be detected and revealed. It is not plain how these concerns are to be reconciled in any particular case in the context of pre-action disclosure but it would seem to me that a court which is asked to grant such disclosure should be careful to pay proper regard to each of them. In any event it cannot be right that an allegation of fraud should assist the potential claimant to obtain pre-action disclosure, unless his allegations carry both some specificity and some conviction and his request for disclosure is appropriately focused”.

The usual basis of an application is that it “is desirable in order to dispose fairly of the anticipated proceedings” (CPR 31.16(3)(d)(i)).

In *First Gulf Bank v Wachovia Bank National Assoc.*, the court declined to make an order on this ground saying it was:

“not persuaded that without pre-action discovery First Gulf cannot plead a case against FUNB” and had concluded that “what First Gulf really seeks is further material to improve their case and to allow them to be better informed in deciding whether or not to proceed”.

These are often the very reasons why such disclosure is sought pre-action.

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27 [2001] EWCA Civ. 1819
28 [2005] EWHC 2827 @ [17]
It is unlikely in a potential fraud case that an applicant will be able to persuade a court to order pre-action disclosure on the basis that production is “desirable in order to assist the dispute to be resolved without proceedings” (CPR 31.16(3)(d)(ii)) or “to save costs” (CPR 31.16(3)(d)(iii)).

A similarly restrictive approach was taken by the court in *Cheshire Building Society v Dunlop Haywards (DHL) Ltd* when rejecting an application for pre-action disclosure that included a request for similar fact documentation. In that case, there was no draft pleading of fraud presented to the court and it was said [43] that:

“It should not be for [the respondent] to decide what documents it would have to disclose by way of standard disclosure in circumstances where the plea of fraud has not been formulated”.

In relation to the request for similar fact evidence it was said also that, whilst such evidence may be admissible in due course, the court could not be clear of this at that stage.

**Similar fact evidence**

The leading case in this area, as for claims involving other causes of action, is the House of Lords decision in *O’Brien v Chief Constable of South Wales*; viz that such evidence is admissible if it is relevant and “potentially probative” on an issue in the action and can be case managed so as to avoid any prejudice to a fair trial. This test was applied in the civil missing trader fraud case of *Silversafe Ltd (in liquidation) & Anr v Hood & Ors*. In *Abbey National plc v JSF Finance & Currency Exchange Co. Ltd*, the Court of Appeal found that similar fact evidence was and would in all likelihood be relevant and probative on the issue of “blind eye” knowledge in a cheque fraud case.

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29 [2007] EWHC 403 (QB)
30 [2005] 2 AC 534
31 [2006] EWHC 1849 (Ch)
32 [2006] EWCA Civ. 328
THE TRIBUNAL

40 A claim in fraud may be pursued in either litigation or arbitration. It is now established beyond doubt that, subject always to the precise language of the arbitration clause/agreement, an arbitration tribunal has jurisdiction to decide disputes concerning whether the contract the subject matter of the reference was entered into as a result of fraud or bribery. An exception will be the case where the main agreement and the arbitration agreement are said to be invalid on the same grounds; e.g. by forgery of a signature on a document containing both agreements.

SUMMARY DETERMINATION

41 It is rare for the court to make a summary determination of fraud. This caution was recently expressed in the following terms:

“I do not underestimate the importance of a finding adverse to the integrity to one of the parties. In itself, the risk of such a finding may provide a compelling reason for allowing a case to proceed to full oral hearing, notwithstanding the apparent strength of the claim on paper, and the confident expectation, based on the papers, that the defendant lacks any real prospect of success. Experience teaches us that on occasion apparently overwhelming cases of fraud and dishonesty somehow inexplicably disintegrate. In short, oral testimony may show that some such cases are only tissue paper strong.”

42 However, the Court stressed that a summary determination on an issue of bad faith may be appropriate when the evidence is before the court saying that “the seriousness of the allegation … does not oblige the court to dismiss the application for summary judgment”.

33 Fiona Trust & Holding Corporation & Ors v Privalov & Ors [2007] UKHL 40 (a bribery case) in which Lord Hoffman @ [13] said:

“In my opinion the construction of an arbitration clause should start from the assumption that the parties, as rational businessmen, are likely to have intended any dispute arising out of the relationship into which they have entered or purported to enter to be decided by the same tribunal. The clause should be construed in accordance with this presumption unless the language makes it clear that certain questions were intended to be excluded from the arbitrator's jurisdiction.”

34 Wrexham Ass. Football Club Ltd v Crucial Move [2006] EWCA Civ. 237 quoted with approval in The Cheshire Building Society v Dunlop Haywards (DHL) Ltd & Anr [2008] EWHC 51 (Comm), a case in which summary judgment was granted where the fraudulent representations were not denied but only “not admitted”.
In *Marlwood Commercial Inc. v Kozeny & Ors*\(^\text{35}\), the Commercial Court judge concluded his 192 paragraph judgment dismissing a claim for summary judgment in respect of a claim for alleged bribery of Azeri government officials in the following way:

“This application joins that list of heroic attempts to achieve a summary disposal of a large case which fail because the court cannot determine everything (or at least not enough) at a summary stage and the case ought to go to trial”.

In practice, summary judgment cases are principally restricted to cases where there has been a relevant criminal conviction in a respected jurisdiction; see e.g. observations in *Marlwood*\(^\text{36}\) or factual simple cases that depend on the construction of signed documentation where there is no allegation of forgery.

**REMEDIES**

**Damages**

The measure of damages in a fraud claim is the loss directly flowing from the claimant’s reliance on the defendant’s statement. There is a requirement of causation over and above inducement. However the recoverability of losses is not governed by a test of foreseeability. This was described in *Smith New Court* as “a special rule or remoteness developed by the courts in the context of deceit”.\(^\text{38}\)

The claimant is entitled to be put back in the position he would have been had the fraud not been committed and/or he had not relied on any fraudulent statement. It follows that it is not relevant to investigate the claimant’s position had the representation had been true. The recoverable losses are reliance losses and not expectation losses.

\(^{35}\) [2006] EWHC 872 (Comm) @ [192]

\(^{36}\) (supra) @ [101-102]

\(^{37}\) This is a feature of the deterrent aspect of a finding of fraud. See e.g. in *Smith New Court*, Lord Hoffman @280 and Lord Browne-Wilkinson @ 264-267 “it does not lie in the mouth of the fraudulent person to say that [the losses] could not reasonably have been foreseen.”

\(^{38}\) *Smith New Court* (supra) @ 285

\(^{39}\) *Smith New Court Securities Ltd v Citibank N.A.* [1997] AC 254 @ 281-2.
Although it need scarcely be emphasised, the tort is complete when the victim sustains loss. It is not necessary for the fraudster to benefit from the fraud; e.g. because his co-fraudster has made off with the gains\textsuperscript{40}.

There remains a duty on the claimant to take reasonable steps to mitigate its loss. However, in practice, the standard required of the victim of a fraud is less than in normal contractual cases; but see e.g. \textit{Dadourian Group Int. Ltd \& Ors v Simms \& Ors}\textsuperscript{41}.

**Heads of claim**

\textit{Contract/transaction}

\textit{Acquisition}

Where a claimant enters into a transaction in reliance on a fraudulent representation, he is entitled to recover the losses incurred in entering the transaction and not the amount of profits represented by the defendant\textsuperscript{42}.

Where a claimant acquires an asset by a transaction in reliance on a fraudulent representation, it is entitled to recover the difference between

\begin{quote}
“\texttt{The logic of the decision in Doyle v. Olby (Ironmongers) Ltd. justifies the following propositions: (1) The plaintiff in an action for deceit is not entitled to be compensated in accordance with the contractual measure of damage, i.e. the benefit of the bargain measure. He is not entitled to be protected in respect of his positive interest in the bargain. (2) The plaintiff in an action for deceit is, however, entitled to be compensated in respect of his negative interest. The aim is to put the plaintiff into the position he would have been in if no false representation had been made. (3) The practical difference between the two measures was lucidly explained in a contemporary case note on Doyle v. Olby (Ironmongers) Ltd.: Treitel, "Damages for Deceit." (1969) 32 M.L.R. 556, 558-559. The author said:}

"If the plaintiff's bargain would have been a bad one, even on the assumption that the representation was true, he will do best under the tortious measure. If, on the assumption that the representation was true, his bargain would have been a good one, he will do best under the first contractual measure (under which he may recover something even if the actual value of what he has recovered is greater than the price)."

…

“The legal measure is to compare the position of the plaintiff as it was before the fraudulent statement was made to him with his position as it became as a result of his reliance on the fraudulent statement.”

\texttt{For a recent example, see St Pauls Travellers Insurance Co Ltd \textit{v Okporuah \& Ors} [2006] EWHC 2107 (Ch)\textsuperscript{41} [2006] EWHC 2973 \texttt{@ [754 - 757]}\textsuperscript{42} \texttt{East \textit{v Maurer} [1991] 1 WLR 461,}"

\end{quote}
the price paid and the market value of the asset\textsuperscript{43} and the legal or other costs of entering the transaction.

\textbf{51} A claimant may also recover damages after entering a transaction (whether profitable or not) in reliance on a fraudulent representation if it can show that, absent the fraud, it would have entered an alternative profitable (or more profitable) transaction or otherwise used the money to make greater profits see e.g.\textit{4 Eng Ltd v Harper & Anr} \textsuperscript{44}.

\textbf{52} In respect of a proven alternative profitable transaction, damages may be recoverable for loss of income and capital profits and may in appropriate cases be recovered on a loss of a chance basis\textsuperscript{45}.

\textbf{Disposal}

\textbf{53} Where the claimant has lost or disposed of an asset it is entitled to recover damages being the difference between the market value of the asset and any consideration received\textsuperscript{46}.

\textit{No contract/transaction}

\textbf{54} An award of damages assessed by reference to lost profits may be made not as an exception to the reliance loss principle but as an application of it. In a case where, for example, a party has fraudulently induced another, such as a competitor, to cease or limit a profitable business, such losses are recoverable\textsuperscript{47}.

\textbf{Costs and Expenses}

\textbf{55} In any of the above cases costs incurred as a result of the fraud are recoverable. These may include:

\textsuperscript{43} e.g. \textit{Doyle} (supra) (purchase of a business)
\textsuperscript{44} [2008] EWHC 915 (Ch) \textsuperscript{[41] – [111], JP Morgan Chase Bank v Springwell Navigation Corporation} [2005] EWCA 1044 \textsuperscript{[30] where the allegations of fraud were, in the event, withdrawn shortly before the trial started in 2007, \textit{East} (supra), Clef Aquitaine SARL v Laporte Minerals (Barrow) Ltd [2001] QB 488 (a case where the fraud caused the claimant to enter a profitable transaction)}
\textsuperscript{45} \textit{4-Eng Ltd} (supra) \textsuperscript{[44] - [46] where the loss of a chance was assessed at 80%\textsuperscript{46} \textit{Smith Kline & French Laboratoires v Long} [1989] 1 WLR 1}
\textsuperscript{46} See e.g. \textit{Barley v Walford} (1846) 9 Q.B. 197

\textsuperscript{47} See e.g. \textit{Barley v Walford} (1846) 9 Q.B. 197
(1) sums incurred in mitigation of loss\(^{48}\);

(2) payments made to third parties\(^{49}\);

(3) legal costs incurred in prosecuting or defending claim against or by third parties caused by the fraud\(^{50}\);

(4) costs incurred or paid to third parties after the acquisition in investigating and discovering the fraud\(^{51}\).

**Time of assessment and credits**

The general rule is that the claimant’s loss is to be assessed at the time it acted in reliance on the representation; e.g. by purchasing the asset or entering the transaction. This rule may be varied when justice requires. A typical example is where the claimant is locked into the acquisition of the asset or to the transaction and sustains further loss before being able to dispose of the asset or withdraw from the transaction\(^{52}\). In this type of case, a claimant is normally able to recover all reliance losses incurred to the date of disposal/withdrawal.

\(^{48}\) *GE Commercial Finance Ltd v Gee* [2006] 1 Lloyd’ Rep 337, [2005] EWHC 2056 (QB) @ [337]

\(^{49}\) Ibid @ [330]

\(^{50}\) *Dadourian Group International Ltd v Simms (No.2)* [2007] EWHC 454 (Ch)

\(^{51}\) e.g. *4 Eng Ltd v Harper & Anr* [2008] EWHC 915 (Ch) @ [27] – [40]

\(^{52}\) In *Smith New Court* (supra), the facts were as follows:

“The claimant, Smith New Court, had been induced to buy shares in Ferranti by the fraudulent misrepresentations of an employee of the second defendant, Scrimgeour. That fraud was called in the case "the Roberts Fraud". But at the time of the purchase the price of the shares was inflated anyway by virtue of another unrelated fraud which had nothing to do with the defendants and which had actually been committed before the time of the "Roberts fraud". That other fraud was called "the Guerin fraud". The claimant held on to the shares after it had purchased them. Then the "Guerin fraud" was discovered. Subsequently the claimant began to sell the shares slowly on the market. Then in the middle of this exercise it discovered the "Roberts fraud". It carried on selling the shares for some months thereafter. The purchase price of the shares had been 82.25p each. The market value at the time of purchase, apart from the "Roberts fraud", was found by the judge to have been 78p per share. The claimant sold the shares for an average of 44p per share. The question before the House of Lords was whether the claimant should be able to recover the difference between 82.25p and 78p or 82.25p and 44p. The House of Lords, in reversing the Court of Appeal, held it should be the larger figure. The important points to note on the facts are (1) that the loss which the House of Lords said the claimants could recover could not have been apparent until the completion of the sale of all the shares; and (2) between the commission of the "Roberts fraud" and the time that the claimants began to sell the shares on the market, the other unrelated fraud had been discovered and it had had a dramatic effect on the price of the Ferranti shares. They fell from a notional 78p to 49p on 20th November 1989 and then fell further. So it could be said that the fall in value of the shares from 78p to an average of 44p was caused by an entirely unrelated fraud, ie. the "Guerin fraud."
A claimant must give credit against its claim for gains made in reliance on the fraudulent representation\(^{53}\). The burden of proving any such gain is on the defendant\(^{54}\).

On the other hand, a defendant is unable to reduce or extinguish a claim for reliance losses on the basis that, absent the fraud and reliance, the claimant would have made a different unprofitable or even more unprofitable business decision/investment.

**Interest**

It is now established at appellate level that the courts have no power to award compound interest on damages recovered in a claim in deceit where the defendant owes no fiduciary duty in equity\(^{55}\).

This position is in contrast to the power of arbitrators to award compound interest in the exercise of their powers under S49(3) Arbitration Act 1996\(^{56}\).

**Rescission**

In cases of fraud, the successful claimant is entitled to rescission if it so elects subject to the court’s application of general equitable principles (e.g. delay and third party interests).

The successful claimant’s right to rescission is not qualified by the court’s statutory discretion to award damages in lieu under s2(1) Misrepresentation Act 1967.

\(^{53}\) see generally *Smith New Court* (supra) and, for a specific example of a credit, *Komercni Bank AS v Stone & Rolls Ltd* [2003] 1 Lloyd’s Rep 383, [2002] EWHC 2263

\(^{54}\) *Parallel Imports (Europe) Ltd v Radivan & Anr* [2007] EWCA Civ. 1373, *Midco Holdings Ltd v Piper* [2004] EWCA Civ. 476

\(^{55}\) S35A Supreme Court Act 1981, *Black v Davies* [2005] EWCA Civ. 531 @ [89], following *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] AC 669 (not a fraud case). However in *Man Nutzfahrzeuge AG v Freightliner Ltd* [2005] EWHC 2347 (Comm) @ [318 - 321] compound interest was awarded, presumably on the basis that the parties accepted that the court had power in the exercise of its equitable jurisdiction to award compound interest on damages for deceit where money was obtained and retained by fraud.

\(^{56}\) “*The tribunal may award simple or compound interest from such dates, at such rates and with such rests as it considers meets the justice of the case ...*”
An order for rescission permits a party to avoid a contract with full retrospective effect. The contract is deemed not to have been made at all. In a contract for the sale of goods, shares or real property rescission has the effect of revesting any property transferred in the transferor who is the victim of the fraud.

A court will order rescission where it is sought and where it considers it will achieve “practical justice”\(^{57}\). A court will decline to order rescission of a contract if counter restitution\(^{58}\) is not possible, for example where the rights of innocent third parties would be prejudiced\(^{59}\).

**Proprietary claims – constructive trust and tracing**

The extent to which, in the absence of a fiduciary relationship, a defrauded party has an equitable proprietary claim (via a constructive/resulting trust analysis) against the defendant is not clearly established. The following analysis is however supported by the first instance case-law cited.

A transaction induced by fraud is voidable at the election of the representee\(^{60}\). The effect of rescission is to restore retrospectively to the claimant the equitable title to the property, at least to the extent necessary to support an equitable tracing claim\(^{61}\). To that extent, the defendant is deemed to hold the money or assets in question on trust for the claimant. This analysis permits a defrauded party to exercise an equitable proprietary claim (and thereby to trace his money in equity) and does not depend on any finding that the parties were in a fiduciary relationship.

\(^{57}\) Halpern v Halpern [2007] EWCA Civ. 291 and e.g. Ross River Ltd & Anr v Cambridge City FC Ltd [2007] EWHC 2115 (QB) (a bribery case)

\(^{58}\) Also known as restitution in integrum


\(^{60}\) The contract is not void as the parties intended property to pass.

\(^{61}\) In an equitable tracing claim, unlike a tracing claim at law, the victim can trace its money into an account where it has been mixed with other money (e.g. in the banking system) because equity treats the money in the account as charged with the repayment of the victim’s money.
Therefore in the absence of an unequivocal affirmation of the transaction and subject to equitable considerations (such as delay and third party rights), a claimant may exercise a proprietary remedy against the defendant for return of the property in question, assisted where necessary by the equitable principles of tracing62.

**Costs**

68 A party responsible for prosecuting an unsuccessful claim in fraud may be liable to an adverse costs order on an indemnity basis.63 In *I-Remit Inc. v Far East Express Remittance Ltd*64 the court went further and made an order that a party who had pursued unpleaded allegations of fraud, which had disrupted and lengthened the trial, must pay costs on an indemnity basis and enhanced interest on the claimant’s damages at the rate of 10% pa. A party may also be subject to an adjusted order for costs, on an issue or percentage basis, if it found that it was unreasonable to raise or pursue an allegation of fraud due, for example, to the absence of good supportive evidence65.

**FRAUD ON APPEAL**

69 Where a claim of fraud has been dismissed at first instance, it is highly unlikely in a civil/commercial case that the Court of Appeal will overturn that finding.

70 An appeal court will only displace a decision acquitting a party of fraud where there are “the clearest grounds” and where it considers it right to displace the advantage the trial had in hearing the evidence. This is

62 See e.g. *El Ajou v Dollar Land Holdings* [1993] 3 All ER 717 applied in *London Allied Holdings Ltd v Lee & Ors* [2007] EWHC 2061 (Ch) @ [251] – [280]

63 CPR 44.3, *Balmoral Group Ltd v Borealis (UK) Ltd* [2006] EWHC 2531 (Comm) and e.g. *National Westminster Bank plc v Rabobank Nederland* [2007] EWHC 1742 (Comm)

64 [2006] EWHC 2531 (Comm)

65 e.g. *National Westminster Bank plc v Kotonou & Anr* [2007] EWCA Civ. 223 where an otherwise successful claimant who failed on his claim of fraud was ordered to pay 50% of the defendant bank’s costs.
particularly so where the finding(s) of fraud depended on oral evidence and not merely the interpretation of documentation\textsuperscript{66}.

**Finding of fraud below**

Where a finding of fraud has been made at first instance, the appellant will have to satisfy the usual restrictive rules applicable to appeals on issues of disputed primary fact\textsuperscript{67}. Again, the prospect of a successful appeal is limited if, as is invariably the case, the findings in favour of the defendant depended in whole or in part on oral evidence\textsuperscript{68}.

The very recent decision of the Court of Appeal in *Abu Dhabi Investment Company & Ors v H. Clarkson Ltd & Ors*\textsuperscript{69}, reversing a finding of secondary fact made at first instance as to the knowledge of the fraudulent parties, is an indication that the appeal court will be prepared to intervene to ensure that a victim of proven fraud is not prejudiced by the underlying corporate structures or formal contractual arrangements between the parties, at least where the defendants have some knowledge of this structure.

\footnotesize{66} An appeal was, however, successful in *Advanced Industrial Technology Corp. Ltd v Bond Street Jewellers Ltd & Anr* [2006] EWCA Civ. 923 where there was no relevant criminal conviction but this was a straightforward case as to representation of title to pawned goods.


\footnotesize{68} e.g. *Contex Drouzhba Ltd v Wiseman & Anr* [2007] EWCA Civ. 1201, *Flack v Pattinson & Anr* [2002] EWCA Civ. 1820

\footnotesize{69} (supra); see [38]: “It is only necessary to conclude, as I do, that the Norasia defendants, knowing as they did the structure by means of which ADIC intended to, and did in fact, effect the investment, plainly intended that their representations should be passed on to those parts of the structure, that is ASH and ASMIC, which effected the investment. In fact, of course, those who controlled the special purpose vehicle were the same people who controlled ADIC, so that in reality the passing on of the representations is a lawyer’s construct.”