

UK SUPREME COURT CONSIDERS WHETHER ILLEGALITY BARS A CLAIM

Patel v Mirza [2016] UKSC 42

Introduction

By a decision handed down on 20 July 2016 in *Patel v Mirza* [2016] UKSC 42, the UK Supreme Court held that a claimant seeking compensation for unjust enrichment was not to be debarred from enforcing his claim simply because the claim sought the recovery of money paid pursuant to a contract for the commission of an illegal activity. The doctrine of illegality has been an important but much-debated area of English law and, in this decision, the Supreme Court held that the rule arising out of previous case law (*Tinsley v Milligan* [1994] 1 AC 340) was no longer to be followed.

Background

The claimant had given the defendant GBP620,000 to place a bet on the share price of a bank using insider information. Such an agreement constituted a conspiracy to commit the offence of insider dealing – which is a statutory offence contained in Section 52 of the Criminal Justice Act 1993. However, because the insider information was not forthcoming, the defendant never placed the bet, and instead kept the money himself. The claimant brought proceedings seeking to recover the money, claiming breach of contract and unjust enrichment.

The High Court, at first instance, dismissed the claim. This was done on the basis that the claim was reliant on an illegal agreement. This “reliance principle” emanated from the decision of the House of Lords in *Tinsley v Milligan* [1994] 1 AC 340.

The claimant appealed against this decision. A majority of the Court of Appeal agreed with the first instance decision that the claim did rely on an illegal contract. However, finding that the illegal scheme provided for in that contract had not in fact been executed, the Court of Appeal allowed the claimant’s appeal and reversed the first instance judgment – requiring the defendant to repay the GBP620,000.

The defendant appealed to the Supreme Court.

Decision

The Supreme Court dismissed the defendant’s appeal against the order requiring him to repay the money.

In reaching this decision, the Supreme Court, in its majority judgment given by Lord Toulson, made several important points regarding the common law doctrine of illegality:

(1) The Supreme Court held that there were two policy reasons for the common law doctrine of illegality as a defence to a civil claim: (a) a person should not be allowed to profit from his own wrongdoing; and (b) the law should be coherent, not self-defeating, and should not

condone illegality;

(2) Rather than resort to an arbitrary principle that no claim which was founded upon illegal conduct could be brought under any circumstances, the English courts should conduct an assessment based on public policy considerations;

(3) The assessment of whether to allow a claim would harm the legal system's integrity would depend on a variety of issues, including: (a) whether the purpose of the prohibited illegality would be furthered by denying the claim; (b) whether to deny the claim might affect other relevant public policies; and (c) whether to deny the claim would be a proportionate response to the relevant illegality;

(4) Whilst there were a wide range of factors that might be relevant to the assessment of those issues, and the Supreme Court did not consider that it would be helpful to establish a definitive list, the Supreme Court recognised that the English courts could not decide cases in an undisciplined manner and that a principled and transparent assessment must be made. Thus, the Supreme Court did try to identify at least some of the potentially relevant factors, including: (a) the seriousness of the illegal conduct; (b) the centrality of the illegal conduct to the contract; (c) whether there was intent behind the illegal conduct; and (d) whether there was disparity in the respective culpability of the contractual parties;

(5) The punishment of wrongdoing was the responsibility of the criminal courts, whereas the civil courts were concerned with the determination of private rights and obligations. The civil courts should not undermine the criminal law's effectiveness nor impose additional penalties that are disproportionate to the nature and seriousness of the wrongdoing;

(6) The English courts had to have regard to the policy factors at play, the nature and circumstances of any illegal conduct and the terms of any relevant statute;

(7) The rule whereby a litigant should not be able to bring a claim where that claim relied on an illegality ('the reliance rule' from *Tinsley v Milligan* [1994] 1 AC 340) was to be overruled;

(8) Instead, the correct approach was to consider whether the policy behind the rule which rendered the relevant contract illegal would be undermined if the claim were to be allowed.

In the instant case, public policy would not require the claimant to give up the monies paid to the defendant, because the claimant was seeking only to unwind the agreement and not to make any profit from it.

Thus, a claimant who could satisfy the usual elements of an unjust enrichment claim ought not to be debarred from enforcing that claim purely on the basis that the money sought to be recovered was paid for an illegal purpose.

A minority of the Supreme Court (Lord Sumption, Lord Mance and Lord Clarke) agreed with the decision that the claimant was entitled to recover the monies but dissented from the reasoning of the majority decision. The minority took the view that the approach adopted by Lord Toulson and the majority, whereby the English courts were to undertake a critical examination of a range of factors to determine whether illegality should or should not bar a claim, was to convert an important legal principle into an exercise of judicial discretion. It

would require the English courts to reach value judgments regarding respective claims of the public interest and the litigating parties. The minority considered that this change in approach was not only unjustified, it was unnecessary for the achievement of justice in the majority of cases. Furthermore, the new approach would give rise to uncertainty, complexity, arbitrariness and opaqueness.

Concluding Remarks

This decision is the latest arena for the difference of opinion that exists at the highest levels of the English judiciary regarding the appropriate test for illegality in English law. In *Hounga v Allen* [2014] 1 WLR 2889 the Supreme Court favoured a general public policy test. However, in *Les Laboratoires Servier v Apotex* [2015] AC 430 and *Bilta v Nazir* [2016] AC 1 it was clear that some of the judges, in particular Lord Sumption, remained of the view that the ‘reliance rule’ should be the English law position.

Notwithstanding the three powerful dissenting judgments in this case, however, it now seems clear that the ‘reliance rule’ has been explicitly and authoritatively departed from. English courts will now undertake a critical examination of public policy factors in order to establish whether, in all the circumstances of any case, a claim should be barred for illegality.

4th October 2016