

Barring civil claims by reason of criminal conduct by the Claimant: the decision of the Supreme Court in *Stoffel & Co v. Grondona* [2020] UKSC 42

1. In what circumstances will a Claimant be barred from succeeding in an otherwise valid claim by reason of some criminality on his or her part at or around the time the cause of action arose? In other words, what is the test for the defence of illegality?
2. As is well known, in 2016, the Supreme Court rejected the ‘reliance principle’ identified by the House of Lords in *Tinsley v. Milligan* [1994] 1 AC 340 and replaced it with a ‘policy-based approach’: *Patel v. Mirza* [2017] AC 467. On Friday, the Supreme Court put further flesh on the bones of this new approach in *Stoffel & Co v. Grondona* [2020] UKSC 42.
3. *Stoffel* concerned a mortgage fraud which the Supreme Court accepted would have been an offence under the then section 15 of the *Theft Act 1968*. *Stoffel*, a firm of solicitors, were unaware of the fraud and were instructed by the borrower, the lender and the vendor of the property. They negligently failed to register the transfer to the purchaser, the mortgagee’s charge and the release of a charge to a former lender. The purchaser defaulted under the mortgage and was sued by the lender. She brought Part 20 proceedings against *Stoffel* on the basis that if they had not been negligent, she would have held unencumbered property which would have been sufficient to satisfy the claim. *Stoffel* accepted that the cause of action was made out but said that recovery was barred by the defence of illegality.
4. The Supreme Court started with the following passage from the judgment of Lord Toulson in *Patel*:

“The essential rationale of the illegality doctrine is that it would be contrary to the public interest to enforce a claim if to do so would be harmful to the integrity of the legal system ... In assessing whether the public interest would be harmed in that way, it is necessary (a) to consider the underlying purpose of the prohibition which has been transgressed and whether that purpose will be enhanced by denial of the claim, (b) to consider any other relevant public policy on which the denial of the claim may have an impact and (c) to consider whether denial of the claim would be a proportionate response to the illegality, bearing in mind that punishment is a matter for the criminal courts.”

5. At paragraph 26 of the judgment, the Court added the following gloss on this ‘trio of necessary considerations’. It emphasised that they were not directed to evaluating the merits of a particular policy in a vacuum. Instead the policies were important ‘...because of their bearing on determining whether to allow a claim would damage the integrity of the law by permitting incoherent contradictions’. It said that the trio should not become another mechanistic process but went on to give each of them further content. It said:

“...In the application of stages (a) and (b) of this trio a court will be concerned to identify the relevant policy considerations at a relatively high level of generality before considering their application to the situation before the court. In particular, I would not normally expect a court to admit or to address evidence on matters such as the effectiveness of the criminal law”

in particular situations or the likely social consequences of permitting a claim in specified circumstances. The essential question is whether to allow the claim would damage the integrity of the legal system. The answer will depend on whether it would be inconsistent with the policies to which the legal system gives effect...to ascertain whether to allow it would be inconsistent with those policies or, where the policies compete, where the overall balance lies. In considering proportionality at stage (c), by contrast, it is likely that the court will have to give close scrutiny to the detail of the case in hand

6. The Court then went on to examine each of the three factors:
 - (a) The Court identified two policies behind the criminalising of mortgage fraud: deterrence and protection of the public (particular mortgagees). However, in relation to the former it said that it doubted whether that policy would be undermined to any significant extent by denying the claim. It said that the risk created by the denial of such claims would be 'most unlikely' to feature in the thinking of mortgage fraudsters. In relation to the latter it pointed out that the loss to the lender would have already occurred by the time of the negligent events and so denial of a remedy would not protect it. On the contrary, the Court pointed out that registration of a transfer would be in the interests of the mortgagee in addition to the interests of the fraudster so '*...it can at the very least be said that the denial of such a claim...would not enhance the protection offered to mortgagees.*';
 - (b) The Court identified two countervailing policy considerations. First that solicitors should not escape liability for negligence in the conduct of their client's affairs unless that would be legally incoherent. The Court said that mortgage fraud would be more likely to be prevented if solicitors are diligent in relation to potential irregularities in transactions. It said that it was unable to accept the submission that there were no potential irregularities in the relevant transaction '*...which could have put [Stoffel]...on notice of the possibility of fraud.*' Secondly, property passes under an illegal transaction. It followed that the law would recognise the lender / purchaser's equitable interest in the property. The Court said that it would be incoherent for the law to recognise that interest notwithstanding the illegality but refuse a remedy in respect of a failure to protect that interest, based on the same illegality;
 - (c) The Court's decision at the third stage is relevant primarily for its discussion of whether the respondent's illegal conduct was 'central'. It decided that the wrongdoing simply provided background to the claim. The manner in which the finance was obtained was, it said, irrelevant to the solicitor's obligation to register the title. However, the Court went on to consider the 'reliance' reasoning from *Tinsley v. Millgan*. It said (paragraph 43) that reliance was no longer determinative but '*...the question of reliance may have a bearing on the issue of centrality.*' It said that in the present case the essential facts could be established without reference to the illegality.
7. At the end of the judgment, the Supreme Court considered an argument that because the Claimant would get something out of the claim (albeit confined to compensation for losses) to allow the claim would permit her to profit from her own wrongdoing. The Court had three relevant comments to make about that argument. First, it said that it would be objectionable for the court to lend its processes to the recovery of an award of damages

calculated by reference to the profits that would have been obtained if an illegal scheme had succeeded. Secondly, that was not this case. To permit a claimant to recover losses caused by negligence was not to assist her to profit from her wrongdoing. However, thirdly, the court went on to say that '*...while profiting from one's own wrong remains a relevant consideration it is no longer the true focus of the enquiry... [it]...is unsatisfactory as a rationale of the illegality defence...*'. It said judges should instead focus on '*...the question whether to permit recovery would produce inconsistency damaging to the integrity of the legal system...*'.

8. This case provides a useful guide to how this new approach to the illegality defence should be applied. However, there remain questions as to how far-reaching the change will prove to be. One area of potential uncertainty that is relevant to offshore practitioners is the extent to which and the manner in which it might apply to the establishment and administration of trusts.

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