UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

PASHA S. ANWAR, *et al.*, Plaintiffs, v. FAIRFIELD GREENWICH LIMITED, *et al.*, Defendant. This Document Relates To: All Actions	Master File No. 09-cv-118 (VM)

AFFIDAVIT OF ROBERT MILES, Q.C.

Exhibit 5

BUTTERWORTHS COMPANY LAW CASES

2004

Volume 2

EDITOR
D D PRENTICE MA, LLB, JD
of Lincoln's Inn, Barrister
Allen & Overy Professor of Corporate Law
Fellow of Pembroke College, Oxford

CONSULTANT EDITOR
MARY STOKES MA, BCL, LLM
of Lincoln's Inn, Barrister

SERIES MANAGER
HELEN BRITTON BA

LexisNexis®
Butterworths

Gardner v Parker

[2004] EWCA Civ 781

COURT OF APPEAL, CIVIL DIVISION

MANCE, NEUBERGER LJJ AND BODEY J

26, 27 MAY, 23 JUNE 2004

Director – Breach of fiduciary duty – Breach of duty causing loss to both shareholder/creditor of company and to company – Whether shareholder/creditor debarred from recovering his loss by rule against recovery of reflective loss

The defendant owned 85% of the issued shares of a company (BDC), the remaining 15% being held by trusts created for the benefit of the claimant and his family. BDC's two largest assets were 9% of the issued share capital of a company (S Ltd) and a debt of £799,000 owed to BDC by S Ltd. The defendant, who was in substance the sole director of both BDC and S Ltd, owned the remaining 91% of S Ltd's issued shares. In December 1992 the defendant procured the transfer by S Ltd of an asset it owned to another company in which he had an interest. Subsequently, BDC went into liquidation and, by its liquidator, assigned to the claimant all BDC's rights of action in respect of shares, properties and other assets and the benefit of all other rights of action and choses in action The claimant brought proceedings against the defendant claiming damages for breach of fiduciary duty alleging that the transfer by S Ltd had been at a substantial undervalue, that the defendant's purpose in procuring it was to extract from S Ltd its most valuable asset to the detriment of BDC or to cause damage to BDC and that as a result of the transfer S Ltd became insolvent and subsequently went into administrative receivership. He further alleged that as a consequence of the transfer BDC's assets were substantially reduced and its holding in S Ltd and the value of the loan due from S Ltd was reduced to nothing or a negligible amount. The judge determined as preliminary issues that the duties, facts and matters pleaded by the claimant in relation to the transfer were capable of amounting to a breach by the defendant of the pleaded fiduciary duties owed by him to BDC as its director but that the claimant was debarred from recovering the damages claimed, ie BDC's loss, under the no reflective loss principle, since the breach of duty also caused the company loss which it was entitled to recover from the defendant. The claimant appealed against the judge's finding that the rule against recovery of reflective loss defeated his claim contending (i) that the rule did not apply to a claim for breach of a fiduciary duty since the nature of the relief granted for such breach was equitable or proprietory in nature which was different in kind from the relief accorded in a common law claim, (ii) that, even if the rule would otherwise apply in the present case it had ceased to apply because, by his actions, in particular by joining in a settlement releasing him from any liability, the defendant had effectively disabled S Ltd from bringing

proce
BDC,
preser
since
sued
a rela
by BI
as a r
breac
duty t
S Ltd
loss,
recov

Held
cause
and t
wheth
its ap
reflect
case f
the b
same
that a
claim
at [46
[2003
(2)
wrong
the m
settlec
justify
S Ltd
liabili
from
had b
S Ltd
compe
loss v
[60]–[
313 a
(3)
shareh
an en
receiv
reason
of the
based
follow
Johns

proceedings for recovery of its loss, as a result of which the shareholder, BDC, was entitled to do so, and (iii) that the rule did not apply to the present claim in so far as it related to the loss or irrecoverability of the loan since there was no reason to extend the rule to a claim by a person who sued as a creditor rather than a shareholder of a company in which he had a relatively small interest. The defendant contended that any loss suffered by BDC was loss that it suffered as a shareholder in, and creditor of, S Ltd, as a result of his alleged actions, and, while those actions would have been breaches of his duty to BDC, they would also have been breaches of his duty to S Ltd, and could properly found the basis of a claim against him by S Ltd and, accordingly, that the damages claimed by the claimant, ie BDC's loss, was reflective loss which BDC, and therefore the claimant, could not recover as a matter of principle.

Held – (1) The rule against reflective loss was not concerned with barring causes of action as such but with barring recovery of certain types of loss and therefore whether the cause of action lay in common law or equity and whether the remedy lay in damages or restitution made no difference as to its applicability. Furthermore, since the foundation of the rule against reflective loss was the need to avoid double recovery, there was a powerful case for saying that it should be applied in a case where, in its absence, both the beneficiary and the company would be able to recover effectively the same damages from the defaulting trustee/director. Accordingly, the fact that a claim was brought for breach of fiduciary duty did not prevent the claim being barred by the application of the rule against reflective loss (see at [46], [49], [53], below); *Shaker v Al-Bedrawi* [2002] EWCA Civ 1452, [2003] 1 BCLC 157 applied.

(2) Although the rule against reflective loss did not apply where the wrongdoer had disabled the company from pursuing its claim against him, the mere fact that the company chose not to claim against the defendant, or settled with him on comparatively generous terms, did not, without more, justify disapplying the rule. In the circumstances there was no evidence that S Ltd or the receivers had been pressurised to release the defendant from liability for any wrongdoing by the settlement or that S Ltd was prevented from pursuing him because of its impecuniosity or that such impecuniosity had been caused by any wrongdoing by him. Moreover, the mere fact that S Ltd was in administrative receivership did not of itself prevent that company from starting an action. Accordingly, the rule against reflective loss would not be disapplied as a result of the settlement (see at [55], [60]–[64], below); *Johnson v Gore Wood & Co (a firm)* [2001] 1 BCLC 313 and *Giles v Rhind* [2002] EWCA Civ 1428, [2003] 1 BCLC 1 applied.

(3) The rule against reflective loss was not limited to claims brought by a shareholder in his capacity as such but also applied to him in his capacity as an employee of the company with a right or even an expectation of receiving contributions to his pension fund. There was therefore no logical reason why it should not apply to a shareholder in his capacity as a creditor of the company expecting repayment of his debt. Accordingly the claim based on the loan was therefore barred by the rule against reflective loss. It followed that the appeal would be dismissed (see at [70], [71], [76], below); *Johnson v Gore Wood & Co (a firm)*[2001] 1 BCLC 313 applied.

Decision of Blackburne J [2003] EWHC 1463 (Ch), [2004] 1 BCLC 417 affirmed.

Cases referred to in judgments

Christensen v Scott [1996] 1 NZLR 273, NZ CA.

Foss v Harbottle (1843) 2 Hare 461, 67 ER 189.

Giles v Rhind [2002] EWCA Civ 1428, [2003] 1 BCLC 1, [2002] 4 All ER 977, [2003] Ch 618, [2003] 2 WLR 237, CA; *rvsg* [2001] 2 BCLC 582.

Humberclyde Finance Group Ltd v Hicks [2001] All ER (D) 202 (Nov).

Johnson v Gore Wood & Co (a firm) [2001] 1 BCLC 313, [2001] 1 All ER 481, [2002] 2 AC 1, [2001] 2 WLR 72, HL; *rvsg in part* [1999] Lloyd's Rep PN 91, CA.

Lucking's Will Trusts, Re, Remwick v Lucking [1967] 3 All ER 726, [1968] 1 WLR 866.

Medforth v Blake [1999] 3 All ER 97, [2000] Ch 86, [1999] 3 WLR 922, CA.

Prudential Assurance Co Ltd v Newman Industries Ltd (No 2) [1982] 1 All ER 354, [1982] Ch 204, [1982] 2 WLR 31, CA.

Shaker v Al-Bedrawi [2002] EWCA Civ 1452, [2003] 1 BCLC 157, [2002] 4 All ER 835, [2003] Ch 350, [2003] 2 WLR 922, Ch D and CA.

Walker v Stones [2000] 4 All ER 412, [2001] QB 902, [2001] 2 WLR 623, CA; leave to appeal given 11 June 2001, [2001] 1 WLR 1341, HL.

Appeal

The claimant, Rodney Mark Gardner, appealed from the judgment of Blackburne J ([2003] EWHC 1463 (Ch), [2004] 1 BCLC 417) given on 26 June 2003 dismissing his claims against the defendant, Alan Parker, for damages for breach of fiduciary duty on the ground that his claims were barred by the no reflective loss principle. The facts are set out in the judgment of Neuberger LJ.

Alan Steinfeld QC and *Stuart Adair* (instructed by *Willan Bootland*, Manchester) for the claimant.

Peter Crampin QC and *Ulick Staunton* (instructed by *Eversheds*, Leeds) for the defendant.

Cur adv vult

23 June 2004 The following judgments were delivered.

NEUBERGER LJ (delivering the first judgment at the invitation of Mance LJ).

[1] This appeal raises, not for the first time, the ambit and limits of the rule against reflective loss discussed in *Johnson v Gore Wood & Co (a firm)* [2001] 1 BCLC 313, [2002] 2 AC 1. In other words, it is concerned with the extent to which a shareholder or creditor of a company who has suffered loss, as the result of a breach of duties owed both to him and the company by a defendant, is none the less debarred from recovering that loss, because the breach of duty also caused the company loss, which it is or was entitled to recover from the defendant.

THE FACTS

[2] The present proceedings were begun on 18 August 1998 by Mr Rodney Gardner against Mr Alan Parker. The re-amended statement of claim contains the following allegations of fact.

[3] Mr Parker owned 85% of the issued share capital of a company called Barclays Development Corp plc (BDC). The remaining 15% of the issued shares in BDC were owned by trusts created for the benefit of Mr Gardner and his family.

[4] BDC's two largest assets were: (i) 9% of the issued share capital of a company called Scoutvale Ltd (Scoutvale); (ii) a debt of £799,000 owed to BDC by Scoutvale (the loan). The remaining 91% of the issued shares in Scoutvale were owned by Mr Parker who was, in substance, the sole director of both BDC and Scoutvale.

[5] On or about 8 December 1992, Mr Parker procured the transfer by Scoutvale of an asset it owned, namely 80% of the issued share capital of a company called Old Hall Estates Ltd (the Old Hall shares) to Bweralley Ltd (Bweralley), a company in which Mr Parker had an interest. In this transfer (the transfer) the consideration for the transfer of the Old Hall shares was stated to be £400,000, the payment of which was deferred. The audited accounts of Scoutvale for the financial year ending 30 April 1991 placed a value on those shares of approximately £5m.

[6] On 10 August 1998, BDC, acting by its liquidator, assigned to Mr Gardner all BDC's rights of action in respect of shares, properties and other assets and the benefit of all other rights of action and choses in action. Mr Gardner's claim is accordingly based on this assignment, and he is seeking to recover damages to which, on his case, BDC is entitled to recover from Mr Parker.

[7] In para 7 of the re-amended statement of claim, it is alleged that, as a director of that company, Mr Parker 'owed fiduciary duties to act at all times in good faith in the interests of and for the proper purposes of [BDC] and not to allow his own interests to conflict with those of [BDC]'. In para 10, it is contended that Mr Parker 'procured the sale by Scoutvale of its 80% shareholding in Old Hall [Estates Ltd] to Bweralley Limited, a company controlled by Mr Parker at a substantial undervalue'.

[8] In para 11 of the re-amended statement of claim it is alleged that Mr Parker's purpose in that connection was 'to extract from Scoutvale its single most valuable asset to the detriment of [BDC]', or 'to cause damage to [BDC]'. Paragraph 13 contains the allegation that 'as a consequence of the Transfer, Scoutvale became insolvent and subsequently went into administrative receivership'.

[9] The damage which BDC is said to have suffered as a result of this is set out in para 14 of the re-amended statement of claim in these terms:

> 'Further, as a consequence of the transfer [BDC's] assets were substantially reduced: (i) [BDC's] 9% shareholding in Scoutvale was reduced in value from £450,000 to nothing, or a nominal value; (ii) the value of [the Loan] due from Scoutvale was reduced to nothing, or a negligible amount.'

[10] Paragraph 15 alleges that, in procuring the transfer, Mr Parker acted in breach of fiduciary duty, and that 'he acted deliberately in furtherance of his own interests at the expense of [BDC] and its assets'. Paragraph 16

quantifies the loss at £1.249m. In the prayer for relief, Mr Gardner claims from Mr Parker 'damages or compensation for breach of fiduciary duty', and he seeks orders that Mr Parker pays £1.249m together with interest and costs.

[11] In his defence Mr Parker, while admitting the existence and terms of the transfer and the insolvency of Scoutvale, denies most of the other allegations in para 10 and following of the re-amended statement of claim. In particular, he denies that the transfer involved the Old Hall shares being sold at an undervalue and he further denies that Mr Gardner has suffered any loss or damage.

[12] The case proceeded to trial in the normal way, with disclosure, inspection, exchange of witness statements, and preparation of bundles – ten in all. A quick perusal of the evidence suggests that there would have been a substantial conflict between the parties as to many of the issues raised in the re-amended statement of claim.

[13] Before turning to what happened at trial, it is appropriate to refer to one aspect of that evidence, to which relatively little reference was made in the pleadings, but which was referred to in argument, and in the judgment below.

[14] At all material times, Westpac Banking Corp plc (Westpac) was a creditor of Scoutvale (and, indeed, of BDC). In that capacity, Westpac had been granted a fixed and floating charge over all Scoutvale's assets by a mortgage debenture dated 7 July 1989.

[15] On 5 August 1993, Westpac appointed administrative receivers (receivers) over Scoutvale's property. On 19 May 1994 Westpac commenced proceedings against Bweralley under s 423 of the Insolvency Act 1986, alleging that the transfer was a transaction at an undervalue entered into for the purpose of putting assets, namely the Old Hall shares, beyond the reach of Westpac. By those proceedings (the s 423 proceedings) Westpac sought the return of the Old Hall shares to Scoutvale. By virtue of s 424(2) of the 1986 Act, those proceedings were deemed to have been brought on behalf of all 'victims' of the transaction, which would, in principle, have included BDC at least in its capacity as a creditor of Scoutvale pursuant to the loan.

[16] The s 423 proceedings were compromised by a settlement dated 2 March 1995 (the 1995 settlement) to which Westpac, Scoutvale acting by the receivers, Mr Parker and his wife, Old Hall Estates Ltd, Bweralley and N M Rothschild & Sons Ltd ('Rothschilds', to whom the Old Hall shares may have been charged by Bweralley as security) were parties. By the 1995 settlement, a payment of £350,000 was to be made to Westpac, Westpac agreed to discontinue the s 423 proceedings, and Mr Parker was released from all claims which Westpac or Scoutvale might have might have against him:

> '... save that nothing in this agreement shall operate to release [inter alia, Mr Parker] from claims that vest solely in the liquidators of Scoutvale and the Receiver's having no authority in that regard.'

Following payment of the £350,000 to Westpac, the s 423 proceedings were discontinued on the agreed terms on 9 May 1995.

[17] Shortly before the present claim was due to come on for hearing, it appears that counsel for the parties agreed to invite the court, at the beginning of the trial, to determine two preliminary issues. This was

presumably on the basis that, if either issue was resolved in Mr Parker's favour, the claim would be dismissed.

[18] The two preliminary issues were:

> '(1) whether the duties, facts and matters pleaded by Mr Gardner in relation to the Transfer are capable of amounting to a breach by Mr Parker of the pleaded fiduciary duties owed by him to BDC as its director; [and] (2) whether on Mr Gardner's pleaded case, assuming that the Transfer was in breach of the fiduciary duties owed by Mr Parker to both BDC and Scoutvale, the losses identified in paragraphs 14 and 16 of the reamended statement of claim are recoverable by Mr Gardner.'

[19] Those two issues were argued before Blackburne J when the case came on for hearing on 10 June 2003. In his reserved judgment dated 26 June 2003 (see [2003] EWHC 1463 (Ch), [2004] 1 BCLC 417), the judge found in favour of Mr Gardner on the first issue. He said that Mr Parker 'was as much in a position of conflict as a director of BDC (as between his duty to that company and his personal interests through Bweralley as the proposed transferee of the shares) as he was as a director of Scoutvale' if he had permitted the transfer to be effected at a substantial undervalue. Mr Parker does not seek to challenge that decision, to my mind rightly.

[20] The judge went on to find in favour of Mr Parker on the second issue, holding that 'Mr Gardner's claims are barred by the no reflective loss principle'. It is against that decision that Mr Gardner now appeals.

[21] Mr Parker's basic contention is that any loss suffered by BDC was loss that it suffered as a shareholder in, and creditor of, Scoutvale, as a result of his alleged actions, and, while those actions would have been breaches of his duty to BDC, they would also have been breaches of his duty to Scoutvale, and could properly found the basis of a claim against him by Scoutvale. Accordingly, runs Mr Parker's argument, the damages claimed by Mr Gardner, ie BDC's loss, is reflective loss which BDC, and therefore Mr Gardner, cannot recover as a matter of principle. In other words, he relies on what may be characterised as the rule against reflective loss, which, he contends, serves to defeat Mr Gardner's claim.

[22] As I have mentioned, the judge accepted that proposition and therefore dismissed Mr Gardner's claim. In a full and careful judgment, he referred to, and quoted fairly extensively from, speeches in *Johnson*'s case, and judgments in the two most relevant subsequent decisions of this court, namely *Giles v Rhind* [2002] EWCA Civ 1428, [2003] 1 BCLC 1, [2003] Ch 618 and *Shaker v Al-Bedrawi* [2002] EWCA Civ 1452, [2003] 1 BCLC 157, [2003] Ch 350.

THE RULE AGAINST REFLECTIVE LOSS

[23] The rule against reflective loss originates, at least judicially, in the judgment of the Court of Appeal in *Prudential Assurance Co Ltd v Newman Industries Ltd (No 2)* [1982] 1 All ER 354, [1982] Ch 204. That was a case concerned with the right of a shareholder in a company to bring proceedings against a defendant who had caused harm to the company, which, in turn, had led to damage to the shareholder through the medium of his shares having a reduced or nil value. The Court of Appeal referred to

the uncontroversial proposition that the mere fact that the company had a cause of action against the defendant did not mean that the shareholder had a cause of action against the defendant. As the court said ([1982] 1 All ER 354 at 357, [1982] Ch 204 at 210):

> 'This is sometimes referred to as the rule in *Foss v Harbottle* (1843) 2 Hare 461, 67 ER 189 when applied to corporations, but it has a wider scope and is fundamental to any rational system of jurisprudence.

[24] The Court of Appeal then turned to the more controversial question of the rights of a shareholder where the defendant is in breach of duty not only to the company, but also the shareholder. The Court of Appeal said ([1982] 1 All ER 354 at 366, [1982] Ch 204 at 222–223):

> '[A shareholder] cannot ... recover damages merely because the company in which he is interested has suffered damage. He cannot recover a sum equal to the diminution in the market value of his shares, or equal to the likely diminution in dividend, because such a "loss" is merely a reflection of the loss suffered by the company. The shareholder does not suffer any personal loss. His only "loss" is through the company, in the diminution in the value of the net assets of the company, in which he has (say) a 3% shareholding.'

[25] This principle, which I have called the rule against reflective loss, was considered in a number of subsequent cases at first instance and in the Court of Appeal, and was authoritatively discussed by the House of Lords in *Johnson's* case. In that case, Mr Johnson, who owned virtually all the shares in a company, sought to recover damages from solicitors who had, he claimed, caused damage to both him and the company in breach of their duty owed, separately, to him and the company. The company had issued proceedings against the solicitors, and those proceedings were settled. Mr Johnson then brought proceedings against the solicitors. One of the preliminary issues in those latter proceedings was the extent to which his claims were barred by the rule against reflective loss

[26] The speeches of Lord Bingham of Cornhill and Lord Millett in *Johnson's* case have been so extensively quoted in a number of reported (and unreported) cases that it is unnecessary to set them out again in full. The kernel of the reasoning of those two speeches are to be found per Lord Bingham ([2001] 1 BCLC 313 at 337–338, [2002] 2 AC 1 at 35–36) and per Lord Millett ([2001] 1 BCLC 313 at 365, 368–369, [2002] 2 AC 1 at 61–62, 65–66), from which extensive passages were quoted, for instance, in the judgment of Waller LJ in *Giles v Rhind* [2003] 1 BCLC 1 at [23]–[26], [2003] Ch 618 at [23]–[26].

[27] In light of the arguments which have been addressed in this case, I should, however, refer to a few short extracts from those speeches. Lord Bingham said ([2001] 1 BCLC 313 at 337, [2002] 2 AC 1 at 35):

> 'A claim will not lie by a shareholder to make good a loss which would be made good if the company's assets were replenished through action against the party responsible for the loss, even if the company, acting through its constitutional organs, has declined or failed to make good that loss.'

[28] He said ([2001] 1 BCLC 313 at 338, [2002] 2 AC 1 at 36):

'On the one hand the court must respect the principle of company autonomy, ensure that the company's creditors are not prejudiced by the action of individual shareholders and ensure that a party does not recover compensation for a loss which another party has suffered. On the other, the court must be as astute to ensure that the party who has in fact suffered loss is not arbitrarily denied fair compensation.'

[29] In his speech ([2001] 1 BCLC 313 at 365–366, [2002] 2 AC 1 at 62), Lord Millett turned to:

'The position is ... different where the company suffers loss caused by the breach of a duty owed both to the company and to the shareholder. In such a case the shareholder's loss, in so far as this is measured by the diminution in value of his shareholding or the loss of dividends, merely reflects the loss suffered by the company in respect of which the company has its own cause of action. If the shareholder is allowed to recover in respect of such loss, then either there will be double recovery at the expense of the defendant or the shareholder will recover at the expense of the company and its creditors and other shareholders. Neither course can be permitted. This is a matter of principle; there is no discretion involved.'

[30] Later, Lord Millett said ([2001] 1 BCLC 313 at 369, [2002] 2 AC 1 at 66):

'[I]f the company chooses not to exercise its remedy, the loss to the shareholder is caused by the company's decision not to pursue its remedy and not by the defendant's wrongdoing. By parity of reasoning, the same applies if the company settles for less than it might have done. Shareholders (and creditors) who are aggrieved by the liquidator's proposals are not without a remedy; they can have recourse to the Companies Court, or sue the liquidator for negligence.'

He then continued in the following terms ([2001] 1 BCLC 313 at 370, [2002] 2 AC 1 at 66):

'But there is more to it than causation. The disallowance of the shareholder's claim in respect of reflective loss is driven by policy considerations. In my opinion, these preclude the shareholder from going behind the settlement of the company's claim. If he were allowed to do so then, if the company's action were brought by its directors, they would be placed in a position where their interest conflicted with their duty; while if it were brought by the liquidator, it would make it difficult for him to settle the action and would effectively take the conduct of the litigation out of his hands.'

[31] I cite three further short passages in the speech of Lord Millett. First, he said ([2001] 1 BCLC 313 at 370, [2002] 2 AC 1 at 66):

'Reflective loss extends beyond the diminution of the value of the shares; it extends to the loss of dividends ... and all other payments which the shareholder might have obtained from the company if it had not been deprived of its funds.'

He added ([2001] 1 BCLC 313 at 370, [2002] 2 AC 1 at 67):

'The same applies to other payments which the company would have made if it had had the necessary funds even if the plaintiff would have received them qua employee and not qua shareholder and even if he would have had a legal claim to be paid. His loss is still an indirect and reflective loss which is included in the company's claim.'

[32] Finally, Lord Millett turned to the claim by the shareholder in that case for pension contributions which would have been made by the company if it had been in funds. He said ([2001] 1 BCLC 313 at 371, [2002] 2 AC 1 at 67):

'For the reasons I have endeavoured to state, Mr Johnson cannot recover the amount of the contributions which the company would have made if it had had the necessary funds; this merely reflects the company's loss and is included in its own claim. Nor can Mr Johnson claim interest in respect of the lost contributions for the same reason.'

[33] I think that the effect of the speeches in *Johnson's* case can be taken as accurately summarised by Blackburne J at first instance in *Giles v Rhind* [2001] 2 BCLC 582 at [27], subject to the qualifications expressed in the judgment of Chadwick LJ in the Court of Appeal (see [2003] 1 BCLC 1 at [61] and [62], [2003] Ch 618 at [61] and [62]). As amended by those two qualifications, it seems to me that Blackburne J's formulation was approved by this court (Keene LJ having agreed with Chadwick LJ) in the following terms, so far as relevant:

'(1) a loss claimed by a shareholder which is merely reflective of a loss suffered by the company – ie a loss which would be made good if the company had enforced in full its rights against the defendant wrongdoer – is not recoverable by the shareholder [*save in a case where, by reason of the wrong done to it, the company is unable to pursue its claim against the wrongdoer*]; (2) where there is no reasonable doubt that that is the case, the court can properly act, in advance of trial, to strike out the offending heads of claim; (3) the irrecoverable loss (being merely reflective of the company's loss) is not confined to the individual claimant's loss of dividends on his shares or diminution in the value of his shareholding in the company but extends ... to "all other payments which the shareholder might have obtained from the company if it had not been deprived of its funds" and also ... "to other payments which the company would have made if it had had the necessary funds even if the plaintiff would have received them qua employee and not qua shareholder" [*save that this does not apply to the loss of future benefits to which the claimant had an expectation but no contractual entitlement*]; (4) the principle is not rooted simply in the avoidance of double recovery in fact; it extends to heads of loss which the company could have claimed but has chosen not to and therefore includes the case where the company has settled for less than it might ...; (5) provided the loss claimed by the shareholder is merely reflective of the company's loss and provided the defendant wrongdoer owed duties both to the company and to the shareholder, it is irrelevant that the duties so owed may be different in content.' (Emphasis added.)

(The italicised text is taken from the judgment of Chadwick LJ ([2003] 1 BCLC 1 at [61] and [62], [2003] Ch 618 at [61] and [62].)

a THE ISSU
[34] Ir
threshol
is satisfi
the com
defendar
b source o
was attr
whereas
a directo
[35] O
c ingredier
namely:
suffered
made as
(ii) the
based on
d Hall sha
been ma
The fact
and the
sharehol
differenc
e practice
[36] O
Mr Stuar
rule agai
BDC's sh
the loan
f applicati
from the
sharehol
Secondly,
v Rhind,
g present c
actions,
effectivel
loss, as a
consider
third con
h to the pr
the loan.

THE FIRS
APPLY TC
[37] It
i the duty
was fidu
Mr Stein
least in p
breach o

THE ISSUES

[34] In light of the first, and unchallenged, finding of Blackburne J, the threshold requirement for the engagement of the rule against reflective loss is satisfied, namely that the defendant, Mr Parker, owed separate duties to the company, Scoutvale, and to the shareholder, BDC. In each case, the defendant's liability arose from the fact that he was a director, but the source of each liability was different, in that his liability to the shareholder was attributable to the fact that he was a director of the shareholder, whereas his liability to the company was attributable to the fact that he was a director of the company.

[35] On analysis, the present case appears to contain the two essential ingredients which result in the rule against reflective loss being engaged, namely: (i) the losses claimed to have been suffered by BDC are losses suffered in its capacity as shareholder in, or creditor of, Scoutvale: that is made as clear as could be in para 14 of the re-amended statement of claim; (ii) the damages claimed in these proceedings against Mr Parker, being based on the losses suffered by BDC as a result of the transfer of the Old Hall shares at a substantial undervalue, are damages which would have been made good if Scoutvale 'had enforced its rights against' Mr Parker. The fact that BDC only had a proportion of the issued shares in Scoutvale, and the fact that one may not be able to 'trace' Scoutvale's loss to the shareholders, without effecting some sort of adjustment, cannot make any difference. If it were otherwise, then the reflective loss principle would in practice rarely apply.

[36] On behalf of Mr Gardner, Mr Alan Steinfeld QC, who appears with Mr Stuart Adair, contends that there are none the less two reasons why the rule against reflective loss does not apply to the claim for loss of value in BDC's shares in Scoutvale or to the claim for the loss, or irrecoverability, of the loan. First, he contends that the rule against reflective loss has no application in a case where, as here, the shareholder is seeking to recover from the defendant by virtue of breach of a fiduciary duty towards the shareholder, independent of the defendant's duty to the company concerned. Secondly, he contends that the exception to the rule, as established in *Giles v Rhind*, either applies, or ought to be extended so as to apply, to the present claim. This second contention is advanced on the basis that, by his actions, in particular by joining in the 1995 settlement, Mr Parker effectively disabled Scoutvale from bringing proceedings for recovery of its loss, as a result of which the shareholder, BDC, is entitled to do so. I shall consider those two contentions in turn. I shall then turn to Mr Steinfeld's third contention, which is that the rule against reflective loss does not apply to the present claim in so far as it relates to the loss or irrecoverability of the loan.

THE FIRST CONTENTION: THE RULE AGAINST REFLECTIVE LOSS DOES NOT APPLY TO A CLAIM FOR BREACH OF FIDUCIARY DUTY

[37] The first contention raised on behalf of Mr Gardner is that because the duty owed by Mr Parker to BDC, and allegedly breached by Mr Parker, was fiduciary in nature the rule against reflective loss has no application. Mr Steinfeld justifies that contention, so far as principle is concerned, at least in part by relying on the fact that the nature of the relief granted for breach of a fiduciary duty is equitable or proprietary in nature, which is

different in kind from the relief accorded in a common law claim, for breach of contract or tort, such as that contemplated in the *Prudential* and *Johnson* cases.

[38] Mr Steinfeld reinforces his argument by pointing out the curious practical results if the rule against reflective loss applied in such a case. He puts forward the example of three trustees of a settlement which owned shares in a company of which one of the trustees was a director. If that trustee conducted the affairs of the company in breach of his duty to the beneficiary under the settlement and in breach of his duty as director to the company, it could lead to a curious result, so far as his fellow trustees were concerned, if he could avoid liability to the beneficiary on the basis of the rule against reflective loss. He, as the person principally responsible for the damage to the value of the settlement, could avoid liability to the beneficiary by invoking the rule against reflective loss, whereas his co-trustees, who may have been relatively innocent of any wrongdoing, could not avoid such liability, because, as they were not directors of the company, there would be no question of their being able to invoke the rule against reflective loss.

[39] In my view, the contention that a claim, which would otherwise be defeated by the rule against reflective loss, is not so defeated because it is brought for breach of fiduciary duty must be rejected. That contention was considered and rejected by this court in *Shaker v Al-Bedrawi* [2003] 1 BCLC 157, [2003] Ch 350. In that case, the claimant contended that a substantial number of shares in a company were held on trust for him by the company's sole director. The claimant brought proceedings against the director in respect of a large sum of money which, the claimant contended, represented part of the proceeds of sale of the company's assets, which had been misappropriated by the director and wrongly distributed. At first instance, the judge dismissed the claim on the basis of a preliminary point which he decided in favour of the defendant director, namely that even if the claimant otherwise established his case, his claim was barred by the rule against reflective loss.

[40] The Court of Appeal allowed the claimant's appeal (which was argued on a different footing) on the basis that, without a full trial, it could not be clearly established that the company was in fact entitled to recover the sums claimed by the claimant. The uncertainty principally arose because the company was subject not to English, but to Pennsylvanian, law: see the judgment of the court given by Peter Gibson LJ ([2003] 1 BCLC 157 at [60]–[72] and [84]–[86], [2003] Ch 350 at [60]–[72] and [84]–[86]). Accordingly, as it was unclear that the company had a claim for any loss suffered as a result of the action of the trustee/director, it could not be determined that the rule against reflective loss applied.

[41] While allowing the claimant's appeal on this ground, the Court of Appeal, in their judgment, also considered another argument raised on behalf of the claimant. Peter Gibson LJ said ([2003] 1 BCLC 157 at [73], [2003] Ch 350 at [73]):

> 'The question which therefore arises is whether the [rule against reflective loss] also applies in circumstances where a beneficiary with an equitable interest in a company's shares which are held in trust by a trustee sues the trustee for an account of the profit taken by the trustee,

that profit being moneys in respect of which the company may have a prior claim against the trustee in his capacity as a director of the company for breach of fiduciary duty.'

[42] The Court of Appeal answered that question, where Peter Gibson LJ said ([2003] 1 BCLC 157 at [81] and [83], [2003] Ch 350 at [81] and [83]):

'[81] ... We agree ... that if the claim by [the claimant] for an account is in substance a claim to moneys to which [the company] has a claim against [the defendant], then consistently with the reasoning in *Johnson v Gore Wood & Co (a firm)* the [rule against reflective loss] would bar [the claimant's] claim for what in effect reflects part of the loss suffered by [the company], and it matters not that the causes of action of [the claimant] and [the company] are different. Nor does it matter that [the company] has not yet brought proceedings against [the defendant]: the ... principle still bars a claim reflective of the company's loss ....

[83] In our judgment the [rule against reflective loss] does not preclude an action brought by a claimant not as a shareholder but as a beneficiary under a trust against his trustee for a profit *unless it can be shown by the defendants that the whole of the claimed profit reflects what the company has lost and which it has a cause of action to recover*. As the ... principle is an exclusionary rule denying a claimant what otherwise would be his right to sue, the onus must be on the defendants to establish its applicability. Further, it would not be right to bar the claimant's action *unless the defendants can establish not merely that the company has a claim to recover a loss reflected by the profit, but that such claim is available on the facts* ....' (Emphasis added.)

[43] Thus it appears clearly to have been determined in *Shaker*'s case that, even when the claim is brought by a beneficiary against a trustee for breach of fiduciary duty, it can be barred by the rule against reflective loss. In that connection I would refer to the passages I have quoted from the judgment in that case ([2003] 1 BCLC 157 at [81] and [83], [2003] Ch 350 at [81] and [83]), delivered by Peter Gibson LJ. My reliance on para [81] is, I think, self-explanatory. So far as para [83] is concerned, it seems to me to be borne out by the words I have emphasised at the end of the first and third sentences of my citation of that paragraph.

[44] Mr Steinfeld argues that those observations should not be followed. He suggests that they were obiter, and in any event were inconsistent with the decision and reasoning of Cross J in *Re Lucking's Will Trusts, Renwick v Lucking* [1967] 3 All ER 726 at 731–733, [1968] 1 WLR 866 at 873–875, and the decision and reasoning of this court in *Walker v Stones* [2000] 4 All ER 412 at 438–439, [2001] QB 902 at 932–934. I do not propose to rehearse in detail his arguments in this connection, because they appear to be substantially the same as those which were raised in *Shaker*'s case, and which were considered and discussed by the Court of Appeal in that case ([2003] 1 BCLC 157 at [75]–[81], [2003] Ch 350 at [75]–[81]). As the court in *Shaker*'s case said in the last of those paragraphs, the decisions in *Re Lucking's Will Trusts* and *Walker v Stones* 'were decided prior to the decision of the House of Lords in *Johnson's* case'. In the same paragraph, the Court of Appeal made reference to the fact that the judge at first instance in that case considered that 'at least part of the reasoning in the

Walker case cannot stand with *Johnson's* case' It seems to me that, in the passage which immediately follows those observations, and which I have quoted above, the Court of Appeal effectively agreed with that contention. Indeed, if they had not done so, they could not have reached the decision that they did.

[45] In my view, the conclusion that the rule against reflective loss would have applied in *Shaker*'s case if the company had had a claim against the defendant under Pennsylvania law was part of the ratio decidendi of the Court of Appeal. That is not merely because the court raised the issue, considered it in detail and disposed of it over the course of its judgment (see [2003] 1 BCLC 157 at [73]–[83], [2003] Ch 350 at [73]–[83]). It is also because it was, in terms of case management, necessary to dispose of the issue. As a result of the conclusion that it was unclear whether the company had a claim in Pennsylvania law, the Court of Appeal remitted the case back for trial. If the rule against reflective loss had had no application, it would have been unnecessary for the trial judge below to hear evidence and argument as to whether the company had a claim; if as the court found, the rule did apply, such evidence and argument would be necessary.

[46] However, whether or not the decision of this court in *Shaker*'s case on this point was strictly obiter or not, I am satisfied that we should follow it. The court specifically identified the point (see [2003] 1 BCLC 157 at [73], [2003] Ch 350 at [73]), and, in the next paragraph, summarised the contention that the rule against reflective loss should not apply to a claim for breach of fiduciary duty. The court then considered the arguments and the authorities relating to that contention, and rejected it (see [2003] 1 BCLC 157 at [75]–[83], [2003] Ch 350 at [75]–[83]). Particularly as this is a difficult and developing topic, it would, to my mind, require a very cogent case to be made out before this court should refuse to follow its own recent clear, unanimous and fully-reasoned conclusion on an important aspect of the rule against reflective loss.

[47] Mr Steinfeld has not persuaded me that the decision and reasoning of the court on this issue in *Shaker*'s case was wrong, especially when its application to the facts of this case is considered. So far as the decision in *Re Lucking's Will Trusts* is concerned, I do not consider it takes matters any further. First, the rule against reflective loss was not raised, although it is true that a not dissimilar argument was advanced and rejected; secondly, it does not seem to me that the rule against reflective loss was actually applicable on the facts; thirdly, it is a first instance decision, albeit one to be accorded particular respect as it was decided by Cross J; fourthly, it pre-dated the *Prudential* and *Johnson* cases.

[48] As to *Walker v Stones*, it was also decided before *Johnson*'s case. Although it is fair to say that a passage in the judgment of Sir Christopher Slade was cited with approval by Lord Hutton in *Johnson*'s case [2001] 1 BCLC 313 at 354, [2002] 2 AC 1 at 51, that passage represents a general summary of the law, and the decision was otherwise not referred to in any of the speeches in *Johnson*'s case. Further, no doubt was cast in *Walker v Stones* [2000] 4 All ER 412 at 438, [2001] QB 902 at 932–934 on the rule against reflective loss. On the contrary: it was applied to bar another aspect of the claim (see [2000] 4 All ER 412 at 455–456, [2001] QB 902 at 952–953). It seems to me that the rule against reflective loss considered and applied in *Walker v Stones* by Sir Christopher Slade was slightly, but

nat, in the ch I have ontention. e decision

oss would gainst the ıdi of the the issue, ;ment (see It is also ɔse of the company case back , it(ıld ence and ound, the

ker's case ld follow CLC 157 ıised the ɔ a claim ıents and e [2003] ly as this e a very v its own nportant

oning of when its cision in tters any ugh it is on it actually ne to be rthly, it

r's case. istopher [2001] general ɔ in any *Talker v* the rule r aspect 902 at ed and ly, but

a crucially, different from what it was subsequently stated to be by Lord Millett. That appears from Sir Christopher's citation of the principles, and especially principle (5) contained in this court's reasoning in *Johnson*'s case [1999] Lloyd's Rep PN 91 at 98 (see [2000] 4 All ER 412 at 436, [2001] QB 902 at 930–931). This difference is reflected in the fact that the defendant's appeal to the House of Lords in *Johnson*'s case on the reflected b loss issue was, albeit to a limited extent, successful.

[49] It is clear, from the analysis and discussion in the cases to which I have referred, that the rule against reflective loss is not concerned with barring causes of action as such, but with barring recovery of certain types of loss. On that basis, there is obviously a powerful argument for c concluding, as this court did in *Shaker*'s case, that, whether the cause of action lies in common law or equity, and whether the remedy lies in damages or restitution, should make no difference as to the applicability of the rule against reflective loss. Furthermore, given that the foundation of the rule is the need to avoid double recovery, there is a powerful case for saying that the rule should be applied in a case where, in its absence, both d the beneficiary and the company would be able to recover effectively the same damages from the defaulting trustee/director.

[50] As Mr Peter Crampin QC, who appears with Mr Ulick Staunton for Mr Parker, points out, the present facts arguably give rise to rather a stronger candidate than those in *Shaker*'s case for the application of the rule against reflective loss. Here, the nature of the claim by the company, e Scoutvale, against the defendant, Mr Parker, is very similar in nature to that by the shareholder, BDC, against the same defendant. In each case, the claim is for breach of fiduciary duty by a director (in one case as a director of the company, in the other as a director of the shareholder) in permitting an asset of the company to be transferred at a significant undervalue to a third party in which the defendant had an interest. On the other hand, there f was a greater difference between the nature of the claim in *Shaker*'s case, namely a beneficiary's claim against the defendant as a trustee of the settlement, and a company's claim against the defendant as a director of the company. While, as I have said, the nature of the two claims is not the centrally significant matter when deciding whether the rule against reflective loss applies, it seems to me that it is not an irrelevant factor when g considering Mr Steinfeld's contention that, notwithstanding the decision in *Shaker*'s case, the rule should not be applied in the present case. Furthermore, the nature of the remedy appropriate to each of the two causes of action in the present case is arguably much closer than it was in *Shaker*'s case.

h [51] The anomaly raised by Mr Steinfeld gives one pause for thought: on the not unlikely hypothetical set of facts he posits, it would seem surprising that only two of the three trustees could be liable to the beneficiary, particularly when it is the third trustee who, as director of the company, could be said to be the person one would expect to be primarily liable.

[52] However, on reflection, I do not consider that the alleged anomaly i assists Mr Gardner's case. First, although it is perhaps a little more difficult to conceive of circumstances in which it might arise, the same point could be made where three persons are jointly liable in contract or tort to the shareholder, and only one of them is so liable to the company. Secondly, it may well be that, in a case such as that posited by Mr Steinfeld, the