Recovery of legal fees under conditional fee agreements with liquidators (Stevensdrake Ltd v Hunt)

08/08/2017

Restructuring & Insolvency analysis: Can a solicitor recover directly from the liquidator their profit costs or fees under a conditional fee agreement (CFA) for legal services? Following the Court of Appeal's decision in Stevensdrake v Hunt, Hugh Sims QC and Simon Passfield, barristers at Guildhall Chambers, say that insolvency practitioners (IPs) would be well advised not to rely on informal arrangements with solicitors but instead should ensure that any arrangements are formalised and fall within the remit of the CFA. In addition Anton Smith, partner at Ashton Bond Gigg, considers the wider implications for funding these types of cases with CFAs.

Original news

Stevensdrake Ltd (trading as Stevensdrake Solicitors) v Hunt (Liquidator of Sunbow Ltd) [2017] EWCA Civ 1173

In what has proved to be a pyrrhic victory, the Court of Appeal has partially allowed an appeal by a firm of solicitors. The judge below held that those solicitors could not claim from the liquidator personally their profit costs under a CFA for legal services provided in relation to a liquidation of an insolvent company of which Mr Hunt was the liquidator. The trial judge decided that the liquidator was not liable as a matter of contract. The Court of Appeal has overturned this ruling saying that there is no justification for going outside the terms of the CFA and making it subject to contrary terms founded upon other agreements which may have been made. However the Court of Appeal has upheld the finding below that there was an estoppel by convention which based upon all the facts found by the judge was unimpeachable. The result is that the solicitors cannot recover from the liquidator their profit costs or claimed success fees.

What was the background to the appeal?

Hugh Sims QC and Simon Passfield (HS & SP): Stevensdrake sought recovery of legal fees due under a CFA dated 10 April 2008 and entered into between it and the defendant liquidator who worked for Griffins. This related to work to be done in litigation against the former administrators of a company which was now in liquidation. The CFA provided for a success fee of up to 100% on the claimed base costs. The liquidator and Gavin Pickering—who was a solicitor who worked at Stevensdrake—had worked together on insolvency matters for many years. It was not disputed that for a number of cases Mr Pickering agreed to be paid only out of recoveries or realisations made in the litigation.

In April 2006, Mr Hunt as liquidator wrote to Mr Pickering saying that Stevensdrake's fees could only be paid out of realisations and if there were no realisations then he would not be in a position to pay those fees nor would he accept personal liability for them. He added that if Stevensdrake was not willing to act on that basis for all relevant papers to be returned.

Mr Pickering sent an email in reply saying that although Stevensdrake would require disbursements to be paid that he was 'happy to wait for payment of our costs until you make a recovery from any source'. The claim against the administrators was later compromised:

- one administrator agreed to settle for £125,000 (which was paid), and
- the other for £1.9m (which remained unpaid as he was later declared bankrupt)

Each compromise satisfied the definition of 'success' under the CFA. When the first compromise was reached, the money was apportioned between Stevensdrake, retained counsel and the liquidator on a recoveries basis. In its 2014 bill, Stevensdrake claimed base costs of £397,686.24 and a success fee in like amount.

What were the legal issues the Court of Appeal had to decide?

HS & SP: There were these five grounds of appeal:

- Was there an implied term that the CFA was subject to a term that the solicitor's right to payment of its basic charges and success fee was conditional or contingent upon there being funds available from realisations or recoveries?
- Was there an estoppel by convention such that the solicitor would not insist on recovery of its basic charges and success fee unless there were funds available from realisations or recoveries? Was the solicitor estopped from departing from this convention?
- Had the liquidator entered into the CFA under the undue influence of Stevensdrake such that those solicitors could no longer rely on the CFA to recover their fees?

- Had the solicitors been either negligent or acted in breach of a fiduciary duty in failing to take adequate steps to explain the CFA to the liquidator?
- Had the liquidator been contributorily negligent?

In the end, however, the Court of Appeal ruled on the first two of these five issues only.

What did the Court of Appeal decide, and why?

HS & SP: The case concerns an application by a Stevensdrake for payment of approximately £1m claimed to be due and owing from Mr Hunt personally as liquidator. These sums were claimed under the terms of the CFA where the underlying claim had been successful (in that the claim was settled) but there were insufficient recoveries into the liquidation estate.

At first instance on 26 February 2016, HHJ Barker QC (see Stevensdrake Ltd (trading as Stevensdrake Solicitors) v Hunt and another [2016] EWHC 342 (Ch), [2016] All ER (D) 258 (Feb)) concluded that there was a mutual understanding between the parties that the solicitor's right to payment under the CFA was conditional or contingent upon there being funds available from realisations or recoveries.

For further reading on the first instance decision, see News Analysis: Personal liability of liquidators for charges under CFA (Stevensdrake v Hunt).

The Court of Appeal overturned the findings of the judge below that a 'recoveries only' term was incorporated into the CFA as 'a matter of construction or implication' (such term being directly contrary to the express terms of the CFA). However Lord Justice Hamblen (giving the substantive judgment of the Court of Appeal) upheld the ruling of the judge below on his alternative finding that the solicitors were estopped by convention from seeking to enforce the CFA against the liquidator personally.

To what extent is the judgment helpful in clarifying the law?

HS & SP: The judgment adopts a more orthodox approach to the issue of interpretation and emphasises that the courts will be inclined to view CFAs as self-contained documents even if they do not contain entire agreement clauses. The judgment emphasises that the question of whether or not there is an estoppel by convention is a fact sensitive one—largely for determination by the first instance tribunal.

What practical lessons can those advising take away from this judgment?

HS & SP: The judgment highlights the legal and practical issues which arise in relation to the funding of insolvency litigation in 'nil asset' cases. It raises, but does not answer, questions about the validity and enforceability of CFAs which are not expressly 'recoveries only' but are nevertheless subject to a 'gentlemen's agreement' to that effect.

IPs would be well advised not to rely on informal arrangements with solicitors but instead to ensure that any arrangements are formalised and fall within the four walls of the CFA documentation. This is both for protection against a claim by a former solicitor where the relationship has deteriorated or moved on.

Anton Smith (AS): The judgment confirms that where there is sufficiently clear understanding or agreement of a position, notwithstanding the wording of the CFA, then it is at least open to a trial judge to find 'estoppel by convention' on the evidence and thereby limit the extent to which it can be enforced. But in a different case or before a different trial judge it is entirely possible that the opposite outcome could have been reached.

Indeed, both judges in the Court of Appeal expressed doubts about some of the trial judge's other conclusions (with Briggs LJ saying he 'found it to be a very finely balanced question indeed'), but felt unable to interfere with this one because it was a legitimate finding based upon hearing all of the evidence at trial. That was enough to determine the outcome of the appeal in this case but it is of little comfort to other IPs in other cases.

The decision does not assist with how best to record retainer arrangements in a way that is contractually binding and still satisfies the indemnity principle to enable the recovery of costs from a losing party. That was not an issue before the Court of Appeal. Nevertheless, the conundrum illustrated by the obiter postscript paragraph of the decision of the trial judge remains. How can an office-holder enter into a valid CFA that does not make him or her personally liable for the full costs liability in the event of insufficient recoveries, while at the same time being able to claim costs from the other side and share the recoveries fairly with a legal team (including counsel) but limited to the recoveries actually made?

There are various solutions that are used in practice which, to my knowledge, have yet to be considered by the courts at the behest of a party liable to pay costs to an office-holder. Ultimately those solutions too may be found wanting. The sooner a definitive workable solution is found, the better.

How does this case fit in with other developments in this area of the law? Do you have any predictions for future developments in this area?

HS & SP: The case may be said to be part of a trend back to a more orthodox approach to interpretation of contracts and influenced by decisions such as *Marks and Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd* [2015] UKSC 72, [2015] All ER (D) 24 (Dec) in looking sceptically at extraneous material being incorporated or implied into contracts. However it leaves open estoppel as a relief valve in suitable cases. The case is likely to increase efforts on the part of counterparties to challenge non-recovery CFAs adopted by IPs on the grounds that in truth they are nothing of the sort.

AS: The requirements for valid CFAs are relatively settled. In the majority of types of litigation where CFA retainers are commonplace (for instance personal injury, medical negligence and defamation) the problem of a judgment debtor not paying in full is, I perceive, far less of a common problem than it is in the insolvency world. That may explain why these issues have not already been resolved in other areas of civil litigation which could then be imported into insolvency litigation CFAs.

Ensuring that the dialogue surrounding the CFA is sufficient to amount to estoppel by convention, if tested in the future, is far from easy and still may not suffice at a trial many years later. Having all of the precise future-proof arrangements within the CFA itself may encourage such a challenge if it is disclosed in detailed assessment of costs proceedings. Indeed, I suspect it is only a matter of time before a losing party ordered to pay costs challenges an IP's CFA retainer. The submission will be that these sorts of arrangements breach the indemnity principle, represent an invalid retainer and so no costs are recoverable.

Fortunately and following on from this Court of Appeal decision there are already moves afoot within the insolvency litigation community to try to come up with a workable CFA precedent for IPs that deals definitively with these issues. The fruits of those labours will hopefully ensure that there can never be a case similar to this one but in the meantime these issues are far from resolved.

Hugh Sims QC is a commercial and insolvency silk and Simon Passfield a specialist insolvency barrister who undertakes litigation and advisory work in all aspects of corporate and personal insolvency law and acted for the liquidator on this appeal.

Anton Smith advises on all aspects of insolvency law, both domestic and cross-border, representing insolvency practitioners, directors, and creditors of insolvent debtors.

Interviewed by David Bowden.