# Whether Solicitors Should Be Indemnified for a Claim to Recover Their Own Costs: *RSA v Tughans*

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## INTRODUCTION

The extent to which solicitors are entitled to an indemnity for claims relating to their own costs has, until now, been the subject of differing opinions and scant authority. The judgment of Foxton J in *RSA v Tughans* (2022) EWHC 2589 brings some welcome clarity.

**This note considers the judgment and its implications**

## THE FACTS

Elements of the background remain opaque, but the facts can be sketched in outline. Tughans are a firm of solicitors based in Belfast. Ian Coulter was their managing partner. RSA was their PI insurer. The underlying dispute arose from the sale of the property loan book of a 'bad bank' established by the Irish government. The bank was advised by the Northern Ireland Advisory Committee, of which Frank Cushnahan was a member.

Mr Coulter agreed to facilitate the sale. He enlisted the assistance of Tuvi Keinan, a partner in the London office of Brown Rudnick. Mr Keinan found a buyer in the US. The buyer set up an SPV for the purchase. Brown Rudnick sent an engagement letter to it. The letter recited that the SPV would pay a success fee of up to €16m on completion. The fee was to be split three ways between Brown Rudnick, Tughans and Mr Cushnahan. The SPV pulled out of the transaction. It was suggested that this was because of concerns about payments to Mr Cushnahan, but the Judge made no finding on the point.

A new buyer emerged. This time, the engagement letter recorded that the buyer would pay Brown Rudnick a success fee of £15m on completion and that Brown Rudnick would, in turn, pay 50% of the fee to Tughans for services rendered. The letter contained a series of warranties to the effect that Brown Rudnick had not engaged in corrupt practices. It agreed to procure the same warranties from Tughans, which it did.

The purchase proceeded to completion. The buyer paid the success fee to Brown Rudnick. It in turn paid £7.5m to Tughans. It was alleged that, thereafter, Mr Coulter:

- reported to his partners that he had earned a fee of £1.5m in a confidential transaction
- paid the other £6m into the account of an offshore company which he had incorporated
- intended to share that sum with Mr Cushnahan
- later confessed the true position to his partners, repaid the £6m to Tughans and left the firm.

Tughans made a report to the Law Society of Northern Ireland. The firm notified a circumstance to RSA. The Public Prosecution Service brought criminal proceedings against Mr Coulter and Mr Cushnahan, which are currently awaiting trial. Brown Rudnick agreed settlement terms with the buyer. These included an assignment of the buyer's rights against Tughans. Brown Rudnick then advanced claims against Tughans in its own right and as assignee. It sought damages for breach of warranty and misrepresentation by Mr Coulter. These allegations arose from the alleged secret agreement to share Tughans' fee with Mr Cushnahan.

RSA declined cover. It maintained that the claim did not arise *"in connection with the Practice carried out by or on behalf of the Solicitor*". It also maintained that Tughans had suffered no loss. Tughans commenced arbitration proceedings. They won. RSA sought to challenge the award in the High Court. There were three limbs to its challenge. It argued that the arbitrator exceeded his jurisdiction, that his decision involved a serious irregularity which caused substantial injustice and that he was wrong in law to conclude that Tughans had suffered loss for which it was entitled to indemnity. It is the third which is of interest for our purposes.

## THE BATTLEGROUND

Divergent views have been expressed as to the extent to which a solicitor can be entitled to an indemnity for a claim to recoup its own costs. Some have inclined towards the opinion that the entitlement can never arise. Others have recognised a conceptual distinction between, on the one hand, a client which maintains that solicitors have charged for work which they have not done and demands its money back and, on the other, a client which claims costs paid to the solicitors as damages in a negligence claim against them.

Where a client brings a claim against its solicitors on the footing that they negligently advised it to pursue hopeless litigation, it will commonly seek to recover as damages the adverse costs awarded to the other party *and* the costs it paid to the allegedly negligent solicitors. The latter view accepts that both would fall to be covered under a PI policy. Likewise, where a claimant maintains that the solicitor's work was so hopelessly bad that it derived no benefit from it and should be compensated in damages for the costs of the work.

This analysis considers the position to be different where the client's complaint is that the solicitor has overcharged and should repay some of the fees. This, without more, would not usually be thought to attract indemnity.

There has, however, been little authority on point. The only case cited to the Judge was the unusual one of *Mortgage Corporation v SIF* [1998] PNLR 73. There, a solicitor house had granted a charge over his house to secure his own debts and those of his firm. The claimant provided secured refinance to the solicitor and was supposed to get a first charge. His firm, which acted in the transaction, neglected to register the charge so the existing lender retained priority. The issue, in effect, was whether the firm had to give credit for the benefit gained in being able to reduce its debt. In rejecting the argument, Sir John Vinelott observed that it would mean that insurers would in every case be entitled to deduct the fees earned by the defendant from the amount they paid out.

Foxton J affirmed the conceptual distinction and discussed the basis for it. His judgment explored its boundaries, which both parties sought to push.

## COSTS AS DAMAGES

The Judge started with the indemnity principle. That is that an insured is entitled to an indemnity for its actual loss but no more than its actual loss. In the case of charging for work that has not been done, the claim is one for restitution. For an English firm subject to the SRA Minimum Terms, such a claim would be outside the policy definition of *Claim* as, *"a demand for, or an assertion of a right to, civil compensation or damages…."*[1] But there is another, equally fundamental bar. The Judge drew on

[1] 'Claim' was not defined in Tughans' policy, to which the Minimum Terms did not apply

observations made by the editors of *Colinvaux's Law of Insurance* and authorities from outside the professional indemnity context to the effect that there can be no actual loss in a restitutionary claim, where the very essence is that the insured holds money to which it has no entitlement.

He added, however, that the suggestion in *Colinvaux* that *"it might be thought that a claim by the assured for loss of professional fees is not one covered by a liability policy*" needs qualification. He accepted that, where a negligent solicitor is sued for damages which include wasted fees, the liability for the fees would ordinarily be capable of constituting loss for the purposes of a PI policy. This, he said, reflected the fact that the solicitor had accrued a contractual right to the fees by doing the work. He was also satisfied that uplift charged on an unsuccessful application in ultimately successful litigation would be loss for those purposes, as would costs contingent on obtaining judgment if the judgment proved unenforceable.

## COSTS TO WHICH THERE IS NO CONTRACTUAL RIGHT

In the Judge's view, all of these scenarios were to be distinguished from one in which the solicitor never had any contractual right to the money. He was not impressed with Tughans' argument that a loss would be triggered for policy purposes if money which should not have been paid to the solicitors was paid away or committed elsewhere by them. This, he said, would involve a series of fine judgments more suited to the law of unjust enrichment than the law of insurance. He went on to describe the complexities which would arise when partnership monies were declared, distributed and disbursed on, "*holidays, fine wines, tasteless art or charitable donations, or used to make investments whose value fluctuated over time".*

Quite why it should be assumed that partners in law firms have poor taste in art is unclear, but be that as it may, the Judge concluded that the need on this approach to consider subjective devaluation, revaluation and surviving value was a strong sign that the argument had ventured down a wrong path.

He did not accept that the result would be different if the claimant - perhaps mindful of coverage - framed its claim as one for damages without alleging that the amount was never due in the first place. This chimes with the view expressed in *Cannon & McGurk on Professional Indemnity Insurance*[2], although the distinction which they draw between a claimant seeking to make good a loss and one seeking to deprive the insured of unauthorised profits appears more inclusive than the Judge's analysis.

## NATURE OF THE CONDITION PRECEDENT

RSA's contention that Tughans were never entitled to the success fee ultimately fared no better. Tughans' accepted that there was a condition precedent for payment of the success fee. But it maintained that this was that warranties and representations be *provided*, not that they be true. This seems, at first blush, a little too ingenious to be sustainable and RSA was able to direct the Judge to *Collidge v Freeport* (2008) IRLR 697 where the same argument failed.

But that was a different case. It involved a CEO of a company leaving under a cloud. The company agreed to pay him off subject to warranties, expressed to be a strict condition of the agreement, that he was unaware of any circumstances which would entitle the company to dismiss him. These were untrue.

On the facts of that case, the Judge found it unsurprising that the point failed. In the instant case, he considered the arguments finely balanced, but construed the letter of engagement in favour of Tughans.

[2] Brendan McGurk appeared with Ben Hubble KC for RSA

## RELEVANCE OF PROCUREMENT BY FRAUD

RSA's fallback argument was that the letter of engagement and/or the payment of the success fee were procured by fraudulent representation. Therefore, it contended, Tughans never had any lawful right to the fee. The difficulty with that, as the Judge noted, was that a contract induced by misrepresentation is voidable, not void. The claimants had elected to treat the contract as subsisting and sue for damages.

He illustrated the fallacy of RSA's argument with a scenario in which a solicitor negligently or fraudulently misrepresented his firm's expertise, leading a client to embark on litigation which it would otherwise have avoided. It could not, he concluded, be said that the misrepresentation would deprive the firm of an indemnity if the client sued to recover the fees as damages.

RSA countered that the position would be different if the client asked for confirmation of the solicitor's experience before paying its bill and the solicitor dishonestly gave assurances. The Judge disagreed. He concluded that this had no effect on the solicitor's contractual right to payment and, in turn, its right to indemnity.

## CONCLUSIONS

Subject to the point being taken to the appellate courts, it is now clear that the suggestion that a solicitor can never be entitled to an indemnity for its own costs is an overreach. It is necessary to distinguish between a claim for compensatory damages and one for restitution.

In principle, an insured will be entitled to an indemnity where costs to which it was contractually entitled are claimed against it as damages to make good a loss. Where, conversely, the claim is one for restitution, it falls outside the definition of 'Claim' in the Minimum Terms and does not involve the insured in actual loss for which it has a right to indemnity.

The way in which the claimant frames its case is not determinative. It is necessary to look at the substance. If, on analysis, the solicitor had no contractual entitlement to the costs being claimed as damages, it will not be entitled to indemnity. However, where the retainer was procured by misrepresentation, even a fraudulent one, the misrepresentation would not, without more, deprive the Insured of indemnity.

Nor is it relevant whether the solicitor has since spent the money received or committed it elsewhere.

### Further Information

Given the generality of the note it should not be treated as specific advice in relation to a matter as other considerations may apply.

Therefore, no liability is accepted for reliance on this note. If specific advice is required, please contact one of the Partners at Caytons who will be happy to help.

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