

Dispute Resolution
Case Law Update
Rosling King LLP



Background

Ms Grondona (the “Claimant”) and Mr Mitchell entered into a contract, in 2000, whereby the Claimant agreed to take out finance on his behalf, secured by way of mortgages over four properties.

The claim relates to one of the properties. The freehold was purchased by an unconnected party for £82,000 in 2001., Following this, in or about July 2002 Mr Mitchell paid £30,000 for the grant of a 125 year lease from the freeholder. Mr Mitchell entered into a loan agreement with BM Samuels for the sum of £45,000 secured by way of mortgage over the property for six months. BM Samuels registered their charge at the land registry.

Three months later, the Claimant purported to purchase the leasehold interest from Mr Mitchell for £90,000 being three times the sum he had paid for the leasehold interest in July 2002. The Claimant entered into a loan agreement with Birmingham Midshires (the “Lender”) who advanced the Claimant the sum of £76,500 in order to purchase the leasehold. The Lender intended to secure the charge over the leasehold interest in the property.

Stoffel & Co (the “Defendant”) acted as solicitor in the transaction for the Claimant, the Lender and the Defendant. The Defendant paid the proceeds of the sale to BM Samuels to discharge their interest in the property. BM Samuels provided the Defendant with a DS1 in order to do so. However, the Defendant failed to register the TR1 transferring the leasehold title into the Claimant’s name, they failed to register the DS1 removing BM Samuels’ charge and had failed to register the charge on behalf of the Lender.

Mr Mitchell failed to maintain the monthly mortgage payments as agreed in his original contract with the Claimant. As such, the Claimant fell into arrears and the Lender proceeded to seek a money judgment against her. The Claimant brought a Part 20 claim against the Defendant seeking a contribution or indemnity.

The Defendant argued that the principle of *ex turpi causa non oritur actio* (“*ex turpi causi*”) applied. The Latin phrase translates as “no claim rises from a disgraceful cause” and is also known as the defence of illegality. The Defendant argued that the Claimant intended the purpose of the transaction to be mortgage fraud and, as such, the defence applied.

Court of Appeal Decision

The High Court applied the test set out in the case of *Tinsley v Milligan* [1994] 1 AC 340 to assess whether illegality applied. Considering that the Claimant did not have to rely on the illegal act in order to bring a claim against the Defendant, the High Court found that the Defendant could not rely on the defence.

However, subsequent to the High Court decision and prior to the appeal, the test applied by the High Court had been overruled by the Supreme Court decision in the case of *Patel v Mirza* [2016] UKSC 42. The Supreme Court found that in order to determine whether or not the principle of *ex turpa causi* applies, the following should be considered:

- a. The underlying purpose of the prohibition which has been transgressed;
- b. Whether any other public policies will be rendered ineffective or less effective if the claim is denied; and
- c. Proportionality.

Gloster LJ applied these considerations in the judgment of *Stoffel & Co v Grondona*. She stressed the serious nature of mortgage fraud and the importance of reaching a decision that should not enable or encourage “dishonest applicants for mortgages” to abuse the system. However, she also held that it would be against public interest to allow negligent solicitors, previously unaware of the illegality, to use the coincidence to avoid their professional obligations. As such, she believes that the onus is on solicitors to be more inquisitive and more perceptive as to irregularities in a transaction in order to avoid mortgage fraud, as far as possible, in the first place.

Furthermore, Gloster LJ found that there was a “genuine public interest in ensuring that clients who use the services of solicitors are entitled to seek civil remedies” against a defendant with whom they entered into a lawful retainer particularly under the circumstances where the Claimant was not seeking to gain from the fraud but to ensure that the Lender’s charge was correctly registered.

With regards to proportionality, Gloster LJ considered the non-exhaustive factors set out by Lord Toulson in *Patel v Mirza* [2016] UKSC 42 and found the following factors applied in her considerations:

- a. The Lender made no allegations of fraud;
- b. The solicitor that provided a witness statement on behalf of the Defendant did not allege fraud in his statement;
- c. The Claimant did not seek to evade her obligations under the Lender’s mortgage agreement;
- d. The Claimant’s illegal acts of fraud were not relevant to the breach of her retainer with the Defendant;
- e. The Claimant’s claim against the Defendants was intended for the purpose of offsetting the whole or part of her liability to the Lender; and
- f. Enforcing her claim would not undermine the integrity of the legal justice system.

As such, the Court of Appeal found that the principle of illegality did not apply and that the Defendants had been negligent.

Commentary

In this case, the guidelines set out in the case of *Patel v Mirza* [2016] UKSC 42 provided some clarity as to what was required in order to allow the Defendant to rely on the principle of *ex turpi causa*. There was clear separation between the mortgage fraud and the negligent service of the Defendant and, furthermore, to decide otherwise would have been to prevent the recovery of the losses incurred by the innocent Lender. However, whilst *Patel v Mirza*



[2016] UKSC 42 has provided clearer guidelines as to factors to consider in cases where *ex turpi causa* is argued, Lord Toulson's non-exhaustive list of what constitutes proportionality exemplifies the difficulties in applying the approach to the individual facts of a case. Ultimately, what can be taken from the Court of Appeal's decision is that, in cases of professional negligence, the illegality must be linked to the breach of the retainer or, at the very least, more closely connected.

For further information, please contact Georgina Squire or the Partner with whom you usually deal.