

# When will a briber have to disgorge his profits?

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## Abstract

The recent decision of the English Court of Appeal (Longmore, Moore-Bick, and Lewison LJ) in *Novoship (UK) Ltd v Mikhaylyuk* [2015] 2 WLR 526 concerned, among other things, the question of the availability of the remedy of an account of profits against a defendant, such as a briber, who had dishonestly assisted a breach of fiduciary duty. The Court held that the remedy of an account of profits is, in principle, available. However, the briber will only be required to disgorge profits 'effectively caused' by his dishonesty and, even then, the remedy of an account of profits is a matter of discretion. What remains unclear following this decision is the application in practice of the test of causation adopted by Court of Appeal and the circumstances in which the discretion will be exercised in the defrauded claimant's favour.

The facts of the *Novoship* case were complex (and were in dispute on the appeal). Reduced to their essentials (as found by the trial judge (Christopher Clarke J) whose findings were upheld by the Court of Appeal), they were as follows.

The appeal concerned the activities of a Mr Mikhaylyuk, a Mr Nikitin, and a Mr Ruperti. Mr Mikhaylyuk was the general manager and commercial manager and a director of the first claimant, Novoship (UK) Ltd ('NOUK'). NOUK was a subsidiary of the Russian shipping company JSC Novorossiysk Shipping Co. NOUK acted as the agent of various other subsidiaries, each of which owned a vessel in the JSC Novorossiysk Shipping

Co group's fleet, in arranging charters of those vessels. Thus Mr Mikhaylyuk owed fiduciary duties both to NOUK and to the relevant shipowning companies. Each of the relevant shipowning companies was also a claimant in the action.

Mr Mikhaylyuk arranged a series of schemes by which he defrauded the claimants and enriched himself and others, including Mr Nikitin, by the receipt of bribes from those who chartered the shipowning claimants' vessels. Among these bribes were payments made by Mr Ruperti in return for time charters of various vessels to Mr Ruperti's companies. Mr Ruperti paid the bribes both to companies owned or controlled by Mr Mikhaylyuk and to a company owned or controlled by Mr Nikitin, Amon International Inc ('Amon'). Mr Ruperti made the payments to Amon, for the benefit of Mr Nikitin, because Mr Mikhaylyuk required him to do so. The payments to Amon amounted to US\$410,379 and Mr Nikitin was aware of the payments and of the reasons for them and, as the trial judge and the Court of Appeal found, acted dishonestly in receiving and retaining them.

At the same time that Mr Mikhaylyuk, Mr Ruperti, and Mr Nikitin were acting dishonestly in relation to the charters to Mr Ruperti's companies, Mr Nikitin was negotiating with Mr Mikhaylyuk for time charters of other vessels to a further company which he, Mr Nikitin, controlled, *viz*, Henriot Finance Ltd ('Henriot'). The Court of Appeal upheld the trial judge's findings and conclusions that, in negotiating the Henriot charters with Mr Nikitin while continuing to act dishonestly in relation to Mr Ruperti's

charters, Mr Mikhaylyuk acted dishonestly in breach of his fiduciary duty to his principals (NOUK and the relevant shipowning companies). As the Court of Appeal put it (in paragraph 53 of the judgment):

‘...[Mr Mikhaylyuk’s] whole relationship with Mr Nikitin was corrupt and...corruption rots the entire business relationship between principals once the agent through whom negotiations are conducted is known to have taken bribes. That is so even if the bribes are given by a principal to other transactions, but the bribes are known about (and shared in) by the parties to the transaction in question.’

The trial judge had found that Mr Nikitin had conducted negotiations for the Henriot charters in the knowledge that Mr Mikhaylyuk had not informed his principals of the bribes which had been paid by Mr Ruperti. The Court of Appeal upheld the trial judge’s findings that constituted dishonest assistance in Mr Mikhaylyuk’s dishonest breach of fiduciary duty: ‘the dishonesty here is continuing to negotiate with an agent from whom one has already received an illegitimate benefit in a prior transaction’ (paragraph 58 of the Judgment).

Having dismissed the appeal on the facts, the Court of Appeal turned to ‘what one suspects is the real focus of this appeal from the parties’ point of view, namely whether the judge was correct to award an account of profits on the Henriot vessels’ (paragraph 61).

One reason for the focus on the availability of this remedy was that the time charters of the relevant vessels to Henriot were, broadly speaking, at rates and on terms consistent with prevailing market rates and terms. Thus the claimants were not able to show that they had suffered loss as a result of Mr Mikhaylyuk’s breaches of fiduciary duty or Mr Nikitin’s dishonest assistance in those breaches. However, having taken the vessels on time charters, Mr Nikitin then traded them on the spot market, entering, in the case of each vessel, into a series of very profitable voyage charters. Mr Nikitin’s success in this regard was the result, at least in part, of a substantial upturn in shipping rates following the

conclusion of the time charters. The profits which Henriot made amounted to approximately US\$100 million and the claimants sought disgorgement of those profits and sought the payment of interest on them of about a further US\$50 million.

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Previous first instance authority had held that, where a bribe had been paid to a fiduciary, a remedy of an account of profits was available against the briber as a dishonest assister in the breach of fiduciary duty. The English authorities on this question were *Fyffes Group Ltd v Templeman* [2000] 2 Lloyd’s Rep 643 (Toulson J), *Ultraframe (UK) Ltd v Fielding* [2006] FSR 293 (Lewison J), *Tajik Aluminium Plant v Ermatov (No 3)* [2006] EWHC 9 (Ch) (Blackburne J), *OJSC Oil Co Yugraneft v Abramovich* [2008] EWHC 2613 (Comm) (Christopher Clarke J), *Fiona Trust & Holding Corp’n v Privalov* [2010] EWHC 3199 (Comm) (Andrew Smith J) and *Okritie International Investment Management Ltd v Urumov* [2014] EWHC 191 (Comm) (Eder J). Against these were *obiter dicta* of Rimer J in *Sinclair Investment Holdings SA v Versailles Trade Finance Ltd* [2007] 2 All ER (Comm) 993.

For Mr Nikitin, various arguments were put forward:

First, it was contended that none of these cases was binding on the Court of Appeal (which was correct) and that, apart from the *Sinclair* case, they were wrong. The Court of Appeal disagreed. The Court, citing *Snell’s Equity*, considered that both a liability to make good loss and a liability to account for profits ‘follow from the premise that the defendant is held liable to account as if he were truly a trustee to the claimant’ (paragraph 75 of the Judgment). This, the Court considered, was a position supported by both policy and authority as had been articulated by Gibbs J in *Consul Development Pty Ltd v DPC Estates Pty Ltd* (1975) 132 CLR 373 at page 397:

‘If the maintenance of a very high standard of conduct on the part of fiduciaries is the purpose of the rule it would seem equally necessary to deter other persons from knowingly assisting those in a fiduciary position to violate their duty. If, on the other hand, the rule is to be explained simply because it would be contrary to equitable principles to allow a person to retain a benefit that he had gained from a breach of his fiduciary duty, it would appear equally inequitable that one who knowingly took part in the breach should retain a benefit that resulted therefrom. I therefore conclude, on principle, that a person who knowingly participates in a breach of fiduciary duty is liable to account to the person to whom the duty was owed for any benefit he has received as a result of such participation.’

The Court of Appeal held that the decision in *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 PC, while altering the conditions to be satisfied before accessory liability would arise, did not alter the nature of the liability:

‘The nature of the liability, as it seems to us, is that the knowing recipient or dishonest assistant has, in principle, the responsibility of an express trustee. That responsibility would include, in an appropriate case, a liability to account for profits.’ (Paragraph 82 of the Judgment.)

The Court also mentioned that Lord Nicholls had explained, in *Attorney-General v Blake* [2001] 1 AC 268, at pages 279–280, that the court had a discretion to order an account of profits even in cases which did not involve fiduciaries and that Arden LJ had pointed out in *Murad v Al-Saraj* [2005] WTLR 1573, at paragraphs 46 and 56, that it had long been the law that equitable remedies for the wrongful conduct of a fiduciary differ from those available at common law: ‘Equity recognises that there are legal wrongs for which damages are not the appropriate remedy’ (paragraph 56 of the judgment in *Murad*). The Court of Appeal concluded (at paragraph 84 of the Judgment):

‘Where, as here, the equitable wrong is itself linked with a breach of fiduciary duty we see no reason why a court of equity should not be able to order the wrongdoer to disgorge his profits in so far as they are derived from the wrongdoing.’

A further argument deployed on behalf of Mr Nikitin was that there should be no account of profits unless there had been a misapplication of trust property. As the time charters to Henriot were contracts for services, there was no disposition of trust property. After reviewing the authorities, the Court concluded that the approach of Peter Smith J in *J D Wetherspoon plc v Van den Berg & Co Ltd* [2009] EWHC 639 (Ch) was correct and that that there was no requirement for there to be trust property before liability for dishonest assistance could arise. The Court rejected Mr Nikitin’s arguments on this point, saying:

‘... it would be a triumph of form over substance if a dishonest assistant escaped liability by entering into a time charter but not if he entered into a demise charter, or took a licence of land rather than a lease. ... As we have said, the only question is whether liability as a dishonest assistant in a breach of fiduciary duty has been established. If it has, then an account of profits is one possible remedy.’ (Paragraph 92 of the Judgment.)

In the light of previous (admittedly first-instance) authority, the conclusions of the Court of Appeal on the question of the availability of the remedy of an account of profits against a dishonest accessory to a breach of fiduciary duty may not seem very surprising. The policy considerations—deterrence and the principle that a dishonest assister in a breach of trust should not be permitted to profit—militated in favour of the Court of Appeal’s conclusion. What may give more scope for debate are the conclusions of the Court on the question of causation and on the question whether, in the circumstances of the case, an account of profits should be ordered as a matter of discretion.

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The Court pointed out that a fiduciary's liability to account for a secret profit did not depend on any notion of causation: it was sufficient that the profit fell within the scope of the duty of loyalty to the beneficiary. *Fyffes Group Ltd v Templeman* (*supra*) was relevant in this regard. In that case, Toulson J, while holding that the remedy of an account of profits was available against a dishonest assistant, had declined to grant that remedy. The facts were that the claimant employed a Mr Templeman as its chartering manager and Mr Templeman negotiated a service agreement with Seatrade under which Seatrade was to provide shipping services to Fyffes. Seatrade had bribed Mr Templeman. The question was whether Fyffes could require Seatrade to account for the profit that it had made in providing the shipping services under the service agreement. Toulson J decided that they could not: first, he said that Seatrade would have entered into a service agreement with Fyffes even if Mr Templeman had not been dishonest; second, he said that the ordinary profit which Seatrade made under the service agreement was not caused by the bribery of Mr Templeman; and, third, he did not see the equity of ordering Seatrade to account to Fyffes for the whole of its profit, because that would amount to an unjust enrichment of Fyffes.

These reasons seem to have been questionable. In the normal way in cases involving dishonest fiduciaries, the Court does not inquire into what would or might have happened had there been no dishonesty, not least because of the difficulty inherent in any such inquiry. In *Murad v Al-Saraj* (*supra*) the Court of Appeal had been sceptical of the decision in *Fyffes* and thought that it should, perhaps, be treated as an example of a case where the wrongdoer was entitled to an allowance for his services 'despite his fraudulent conduct' (see *per* Arden LJ, at paragraph 69). That does not appear to have been the basis of

Toulson J's decision and, as Arden LJ's reference to fraudulent conduct may suggest, would have been a dubious basis in any event: one would not expect a fraudster to be given an equitable allowance for his skill or services. Jonathan Parker LJ said that he, like Arden LJ, had difficulty in reconciling Toulson J's reasoning with the authorities (in particular, *Regal (Hastings) Ltd v Gulliver* [1967] 2 AC 134n and *Boardman v Phipps* [1967] 2 AC 46).

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In the *Novoship* case, the Court of Appeal considered that the Court in *Murad* had proceeded on the assumption that precisely the same principles as regards causation applied in the case of a dishonest assister as applied in the case of a true trustee. However, since the question whether that assumption was correct had not been before the Court in *Murad* and had not been explicitly considered, the Court of Appeal in *Novoship* did not consider that *Murad* established that assumption was correct. The Court of Appeal in *Novoship* distinguished, for the purposes of causation (as the Supreme Court had done for the purposes of limitation: see *Williams v Central Bank of Nigeria* [2014] AC 1189) between the position of a fiduciary and the position of an accessory. In the case of the fiduciary, the duty not to make a profit was enforced by ordering the fiduciary to account to the beneficiary for all profits made. In the case of the dishonest assister, there was no duty not to make a profit and so the normal rules of causation applied:

'Where a claim based on equitable wrongdoing is made against one who is not a fiduciary, we consider that, as in the case of a fiduciary sued for breach of an equitable (but non-fiduciary) obligation, there is no reason why the common law rules of causation, remoteness and measure of damages should not be applied by analogy.'

Following this reasoning, the Court pointed out that the common law did not usually apply a simple ‘but for’ test of causation but, rather, distinguished between a breach which was the effective cause of the loss and one which was ‘merely the occasion for the loss’ (paragraph 108 of the Judgment). This distinction was a question of ‘the application of common sense’.

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A perhaps arresting feature of the Judgment, particularly bearing in mind the policy considerations referred to above, is the application of this common sense test to the facts of the *Novoship* case itself. Of course, each case will be different and causation is always heavily fact-dependent. Nevertheless, the Court’s approach may be thought to have significance for the availability of the remedy of an account of profits in many cases of bribery. It is worth setting out the Court’s reasoning in full (it is not lengthy):

‘We agree with the judge that if Mr Nikitin (or his companies) had not entered into the Henriot charters, the profits would not have been made. In other words, “but for” entry into the charters the profits would not have been made. But in our judgment the simple “but for” test is not the appropriate test. In our judgment what Mr Nikitin acquired as the result of his dishonest assistance (and also as a result of Mr Mikhaylyuk’s breach of fiduciary duty) was the use of the vessels at the market rate. That was merely the occasion for him to make a profit. The real or effective cause of the profits was the unexpected change in the market. As the judge recognized . . ., Mr Nikitin made the profits “because he judged the market well”.’

Does this approach have significance beyond the facts of the *Novoship* case? It suggests that, in many cases in which a dishonest assister has paid a bribe in order to secure business, it is likely that the Court will—if it follows the approach of the Court of

Appeal in *Novoship*—have to conclude that any profit made by the briber was not ‘effectively caused’ by the bribery, but rather that the bribery ‘merely provided the occasion’ for the making of the profits.

It may be suggested that such an approach hardly accords with reality. The distinction between the bribe being the cause of the profits and the bribe ‘merely’ providing the opportunity to make profits seems a fine one. But, in any event, it is not immediately apparent why a dishonest assister whose bribe presents him with the opportunity to make profits should be entitled to keep them, at least if the underlying policy is, at least in part, deterrence. Where a bribe is paid, it is usually the case that it is paid in order to secure business, rather than to secure business at a cheap price: in other words, the purpose of the bribe is to secure the opportunity to make money, rather than the certainty of making money. As a result, in a great many cases, the defrauded principal will probably not be able to demonstrate that he has suffered any loss (beyond the amount of the bribe, which the law deems to be the measure of the principal’s loss in the absence of proof of more extensive loss). Whether, having secured the business, the briber is able to make money from it will usually be a matter of his own ability: no doubt there will be situations in which a profit is almost guaranteed, but many more in which that will not be the case.

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In what situations will there be scope—following the Court of Appeal’s approach—for the ordering of an account of profits? Arguably, very few. If that is the case, then, of course, this will be welcome news for bribers: they may have to pay over the amount of the bribe (as the deemed loss caused by the bribery), but are likely often to have strong arguments, based on the *Novoship* analysis, that the profits which they have derived were not effectively caused by their (or the



bribed fiduciary's) dishonesty and that they should be entitled to keep them.

### *Will be welcome news for bribers*

The further point which the decision in *Novoship* raised in relation to the remedy of an account of profits was, as mentioned, the question of discretion. Here, too, the claimants failed. The Court of Appeal considered two aspects of this: first, the question of the 'rationale' for the awarding of an account of profits; second, the 'particular form and extent of the wrongdoing'.

Previous authority had been reasonably clearly to the effect that the fact that the defrauded principal or beneficiary would not or could not have made the profits in question for himself was beside the point: a purpose of the remedy of the account of profits is to strip the defaulting fiduciary of his gains, rather than to compensate the principal or beneficiary for his loss. The remedy of an account of profits is available and imposed 'pour encourager les autres', as Arden LJ pointed out in *Murad* (at paragraph 74). Again, the Court of Appeal in *Novoship* thought that this principle did not apply where one was dealing with an accessory, as opposed to a fiduciary: when dealing with an accessory, there was a discretion whether to order an account of profits.

As regards the 'rationale' point, the Court of Appeal pointed out that what the relevant claimants had wanted to do was to charter their vessels on time charters at market rates in order to avoid the risk of fluctuating rates for freight: they 'wished to secure a long-term income, they necessarily wished to lay off the risk on to the charterer' (paragraph 117 of the Judgment). Therefore, the Court of Appeal said, the profits which Mr Nikitin had made:

'... were the kind of profits that the shipowning companies deliberately decided to forgo. In our judgment they cannot be described as profits which ought to have been made for the beneficiary, and therefore they fall outside the rationale for the ordering of an account.'

Again, to what extent will this approach will have a wider significance? Presumably, it will frequently be possible to argue that, where a principal has contracted with a briber, he has done so having decided that he himself wants the benefit of the contract rather than the opportunity which the briber has secured by entering into the contract. In that event, it seems, any profits which the briber makes will not be regarded as falling within 'the rationale for the ordering of an account' and so, as a matter of discretion, an account will be refused and the briber permitted to keep the profits.

The Court of Appeal also exercised its discretion against the claimants by reference to the particular form and extent of the wrongdoing. The Court said (at paragraph 119):

'One ground on which the court may withhold the remedy is that an account of profits would be disproportionate in relation to the particular form and extent of the wrongdoing. ... In our judgment that is the case here.'

This appears to be a separate point from the 'rationale' point referred to above since the 'rationale' point does not relate to the 'particular form and extent of wrongdoing': rather it relates to the fact that the defrauded principal has chosen not to make the profits in question.

What aspects of the wrongdoing are relevant when it comes to considering the 'particular form and extent of the wrongdoing'? The Court of Appeal did not provide any guidance on this point. The form of the wrongdoing was, as the Court found, dishonesty in relation to a breach of fiduciary duty by an agent. Was there something about Mr Nikitin's and Mr Mikhaylyuk's dishonest conduct which rendered it less reprehensible than other forms of dishonesty? If so, we are left in the dark as to the applicable criteria by which to judge such matters.

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As to the ‘extent’ of the wrongdoing, it might be tempting to ask whether a significant point was the size of the bribe (some US\$410,000) when compared to the size of the profits and interest (some US\$150 million)? But it surely cannot be the case that, if a briber has made an enormous profit by comparison with the size of the bribe, he is permitted to keep his profits, but if he has been less successful he must disgorge them. One has only to reflect that such an approach would give rise to nice questions as to what ‘bribe:profit ratio’ is acceptable to the Courts in any particular case to realize that the Court of Appeal cannot have had this in mind. But what they did have in mind in this regard is very unclear.

Various passages from the Judgment make plain the Court’s consistency in its deprecation of bribery and corruption. Indeed the Judgment opens with a reference to what may have been the first recorded instance of a successful bribe (Polyneices’ bribery of Eriphyle, mentioned in *The Odyssey*) and continues:

‘... centuries later, bribery is still prevalent and pervasive however much legislators and judges try to stamp it out.’

Further, as mentioned, the Court of Appeal approved the passage of the judgment of Gibbs J in *Consul Developments* cited above which set out the deterrent basis for the imposition of a liability to account for profits on a dishonest assister in a breach of fiduciary duty. The Supreme Court, in *FHR European Ventures LLP v Cedar Capital Partners LLC* [2014] 3 WLR 535 reiterated the policy considerations (albeit in the context of a dishonest fiduciary, rather than a dishonest accessory):

‘Secret commissions are . . . objectionable as they inevitably tend to undermine trust in the commercial world. That has always been true, but concern about bribery and corruption generally has never been greater than it is now: see for instance, internationally,

the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions 1999 and the United Nations Convention against Corruption 2003, and, nationally, the Bribery Acts 2010 and 2012.’ (Paragraph 42 of the judgment of the Court.)

It may, perhaps, be questioned whether the Court of Appeal’s approaches to questions of causation and discretion in the context of bribery—which appear favourable to the dishonest assistant and briber and to provide very considerable scope for such a person to succeed in retaining profits which he would not have made ‘but for’ the bribery—will assist in the legislators’ and judges’ endeavours.

There is a further point of interest in the *Novoship* case. This relates to the ability of a principal to claim an account of profits from a briber where the bribed agent has more than one principal.

As mentioned, Mr Mikhaylyuk owed fiduciary duties both to NOUK and to the shipowning companies. NOUK itself also owed fiduciary duties to the shipowning companies. Each shipowning company individually sought the profits which had been made by Mr Nikitin/Henriot on that company’s particular vessel on the basis that Mr Mikhaylyuk had acted in breach of the duties which he owed to that company and Mr Nikitin had dishonestly assisted in that breach. For its part, NOUK sought an account of all profits made on all vessels on the basis that Mr Mikhaylyuk had acted in breach of the fiduciary duties he owed to NOUK and Mr Nikitin had dishonestly assisted in those breaches. (Obviously, the claimants did not seek double-recovery.)

However, two of the shipowning companies were not parties to the proceedings: these companies had been sold by the group prior to the commencement of the proceedings and had then been wound up and dissolved.

The trial judge considered that NOUK was entitled to an account of the profits made on these two companies’ vessels: the fact that NOUK would not have made the profits in question was, he said, irrelevant and it was no bar to the grant of the relief that Mr

Mikhaylyuk and Mr Nikitin might also be liable to the two companies (or might have been liable had those companies remained in existence).

The Court of Appeal disagreed. Relying on *Powell & Thomas v Evan Jones & Co* [1905] 1 KB 11 CA, they held that NOUK was 'not the correct claimant'. They considered that, for NOUK to claim such profits and to retain them for itself would be a breach of fiduciary duty on the part of NOUK *vis-à-vis* the companies. NOUK made plain that it considered that, if it were to recover the profits, it would have to hold them for the two companies. But the Court of Appeal regarded that as 'theoretical': the companies did not exist and it was not known whether they could be revived and, if so, by whom. If the companies were not revived, then there would be an 'unjust enrichment' of NOUK because, again, these were not profits 'which ought to have been made' for NOUK.

Again, this conclusion seems open to question. If the (or a) reason for the imposition of a remedy of an account of profits is deterrence then the question whether the claimant would or could himself have made the profits should be irrelevant. There was still a dishonest breach of fiduciary duty owed to NOUK and dishonest assistance in the breach of that duty. If the two companies had remained in existence and had sued NOUK for breach of the fiduciary duty NOUK owed them, could it have been said that NOUK could not seek to recoup the monies it had to pay to the companies by claiming an account of profits from the dishonest assister? Indeed, it might be said that the fiduciary duties NOUK owed to its principals (the shipowning companies) required it to bring such a claim on behalf of its principals. Why then should the fact that the companies had been wound up alter the position?

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