ACCOUNT OF PROFITS AGAINST ACCESSORIES

Authored by: Lucas Moore (Partner) and Victor Lui (Associate) - Payne Hicks Beach

What is the scope of the remedy of an account of profits against accessories to wrongdoing that a claimant victim can recover? In this article, Lucas Moore (Partner) and Victor Lui (Associate) examine the recent cases of Lifestyle Equities CV v Ahmed[1] and Hotel Portfolio II UK Ltd v Ruhan.[2]

Account Of Profits

The remedy of an account of profits is discretionary and personal in nature, requiring the wrongdoer to give up their profits made as a consequence of their breach. The measure is the defendant's gain as opposed to the claimant's loss.

This remedy is not generally available for breach of contract or in tort. Damages in contract are usually intended to place a claimant in the position they would have been in had the contract been performed. Damages in tort typically aim to place a claimant in the position they would have been in had the tort not been committed, albeit an account of profits is an established remedy in the infringement of intellectual property rights.

In contrast, an account of profits is a well-established remedy in equitable wrongs such as breach of fiduciary duty or breach of confidence. Where a fiduciary has taken property or exploits an opportunity belonging to the principal, the fiduciary is liable for any unauthorised profits made, held on constructive trust for the principal. The principal is required to elect between an account of profits and equitable compensation, and cannot claim both.[3] It may be favourable to claim an account of profits where: (1) they are evidentially easier to quantify than the loss suffered; (2) the principal may wish to trace into any substitutes; or (3) the principal may wish to gain priority over other creditors of the fiduciary.

However, in the case of accessories, can the law require them to repay profits that were made by the primary wrongdoer, or only the profits that they themselves made? The answer is decidedly the latter in view of recent legal developments.

Accessory Liability

At Common Law

The scope of accessories' liability in tort was clarified in the Supreme Court decision of Lifestyle Equities CV v Ahmed, a case involving the statutory tort of trademark infringement. Lord Leggatt JSC explained that there are two distinct possibilities: (1) where a person knowingly procures another to commit an actionable wrong, they will be jointly liable with that other person for the wrong committed; (2) where a person gives another person more than trivial assistance to commit a tort, pursuant to a common design between the parties, then they will also be jointly

1 [2024] 2 WLR 1297, [2024] UKSC 17

2 [2024] 2 All ER 903, [2023] EWCA Civ 1120

3 Tang Man Sit (decd) v Capacious Investments Ltd [1996] AC 514, 521A-C (Lord Nicholls)

liable. In either case, the accessory must have knowledge of the essential features of the tort to be liable (even where the tort is one of strict liability).[4]

The court further held that the only profits which an accessory could be ordered to account are those which they have made, because the remedy operates to require that defendant to disgorge a gain derived from the wrong, rather than to pay a penalty or a fine.[5]

On the facts of Lifestyle, the claimants sued two companies and their directors for infringement of registered trademarks and passing off, in their having deployed infringing signs in the sale of clothing and footwear. One of the defendant companies, HS, subsequently went into administration. The claimants elected to claim an account of profits against the wrongdoing directors.

The Supreme Court held that the directors had not themselves infringed the claimants' trademarks,[6] nor should they be liable as accessories because there was no finding at trial that they had the requisite knowledge for the infringements committed by HS.[7] The court further held that the following did not constitute profits which should be accounted for: (1) a loan advanced by HS to a director, which was not argued to be a disguised dividend; (2) the salaries paid to the directors, which were not alleged to be beyond their fair market value.[8]

In Equity

Hotel was a case concerning dishonest assistance of a breach of fiduciary duty. The Court of Appeal similarly held that, while such an assistant is jointly and severally liable with the fiduciary for the principal's loss, the assistant can only be liable to account for their own profits and not for those of the fiduciary.[9]

The facts involved a company HPII which owned a hotel portfolio and was directed by Mr R. HPII entered into an agreement to sell the portfolio at market value to a company CM that was owned by Mr S, who was in fact Mr R's nominee. Mr R had not disclosed his involvement in CM. Subsequently, CM sold the hotels for a profit and made further investments. After HPII entered liquidation, the liquidator brought proceedings against Mr R for breach of fiduciary duty for the original sale of the hotels, and Mr S for dishonestly assisting the misapplication of those profits. At HPII's election, the trial judge ordered Mr R to account for the profits realised for the sales by CM and Mr S to pay equitable compensation in an equivalent amount.

On appeal, the court held that Mr S was not so liable for two reasons: (1) the original sale was inextricably connected to the profits said to be misapplied, such that HPII suffered no loss;[10] (2) it was inconsistent for the claimants to elect for an account of profits as against the fiduciary (Mr R) but seek equitable compensation against the dishonest assistant (Mr S).[11] HPII was granted permission to appeal to the Supreme Court,[12] so the interplay between these remedies awaits further consideration.

Uncharted Territory

Underlying Rationale?

Lord Leggatt JSC referred to two possible rationales of why an account of profits is ordered: (1) deterrence – a defendant should not be allowed to keep profits made dishonestly by knowingly infringing another's rights, so the remedy should remove any such incentive; (2) purposive – intellectual property rights exist to encourage and reward creativity and innovation, and this purpose is promoted by allocating profits made from exploiting the right to the owner. He viewed the second rationale as more cogent but left open whether the first was a viable justification.[13]

The second rationale would, however, appear to support the availability in principle of an account of profits by way of remedy for a wider array of torts than is countenanced by the present state of the law. It may be said that denying a defendant's profits made from property torts (e.g. conversion, trespass) may promote the owner's peaceful enjoyment of their property; or that disgorging profits made from economic torts (e.g. procuring a breach of contract, conspiracy) would better protect legitimate economic interests. Different public policies may be in play for each type of tort, so it would be necessary to examine individually whether the remedy is justified.

Scope Of The Account?

While the court's discretion as to whether to grant an account of profits has to be exercised in accordance with clear principles,[14] it may be preferable that the law allows wider considerations to accommodate the justice of each case.

With respect to Lord Leggatt JSC's ruling, even where an accessory employee receives a fair salary from a company that manufactures infringing goods, it should still be possible to argue that the employee's salary was an effective gain when the infringement has contributed to the company's liquidity or solvency. Instead of categorically rejecting salary as a form of profits, this could have been left as an evidentiary matter for the claimant to prove.[15]

To seek advice on commercial litigation, please contact Lucas Moore or Victor Lui, or alternatively, telephone on 020 7465 4300.

4 Lifestyle, [120], [131]-[137]
5 Lifestyle, [158]-[161]
6 Lifestyle, [33]
7 Lifestyle, [143], [181]
8 Lifestyle, [170]-[173], [182]
9 Hotel, [43]-[45], [60]
10 Hotel, [63]-[69]
11 Hotel, [70]-[72]
12 On 31 January 2024: https://www.supremecourt.uk/pta/permission-to-appeal-2024-01.html
13 Lifestyle, [152]-[155]
14 Lifestyle, [145]
15 C.f. Lifestyle, [173]-[174]