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# Rukhadze v Recovery Partners GP: no more unto the breach

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Status: **Published on 02-Apr-2025** | Jurisdiction: **England, Wales**

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In this article, David Schmitz of Ten Old Square discusses the recent Supreme Court judgment in *Rukhadze and others v Recovery Partners GP Ltd and another [2025] UKSC 10*. David considers the distinct approaches taken by the judges in their unanimous decision to dismiss the appeal and whether the decision may be able to be distinguished in the future, in a more sympathetic case.

In *Rukhadze and others v Recovery Partners GP Ltd and another [2025] UKSC 10*, the Supreme Court was asked to overturn the rule that fiduciaries who acquire profits or gains which have a connection with their former role as fiduciaries are automatically obliged to account for them to their principals and to hold them on trust. The appellants (defendants) contended that fiduciaries should not have to account for their gains where they can prove that a gain had not accrued from a breach of fiduciary duty. They proposed that the court should be able to apply a "but for" test and to consider "counterfactuals" when considering what profits they would have made if there had been no breach.

The court unanimously dismissed the appeal but from the judgments of the seven-judge panel, four distinct approaches can be seen. Three of these require examination here, not just because they are interesting, but because, given that the defendants' case on the facts was less attractive than those in earlier cases, it is necessary to ask whether a future tribunal might be able to distinguish *Rukhadze*, if a more sympathetic case were to come before it. (The judgment by Lady Rose is not covered here because it is directed primarily at the issues which arise from the role of the appellants as company directors, rather than at the issues with which this article is concerned.)

In *Rukhadze* itself there were two proposed counterfactuals. One was that the defendants should not have to account for anything because they could have resigned from their fiduciary positions before they made any profits. The other, supported by a finding of fact at first instance, was that a profit-sharing arrangement would have been concluded between the parties if the defendants had waited for this to materialise before ending the fiduciary relationship. Had such an agreement actually been made, so the argument went, there would have been no breach because the claimant principal would *ex hypothesi* have consented to the defendant fiduciaries retaining whatever benefit had been agreed.

For the facts, see Lord Burrows at paragraph 240 and (in greater detail) Lord Briggs at paragraphs 8 to 14. In essence, the defendants had been company or limited partnership directors of the claimants' predecessors in title. By virtue of those positions, the defendants owed fiduciary duties to those predecessors. While they were still in those positions, they obtained and set up for subsequent exploitation by themselves, a business opportunity which was properly that of the predecessors, to provide financial services for the family of a deceased billionaire. The defendants then resigned their positions and carried out those services making profits for themselves. For further discussion of the facts and background of the case, see Legal update, Supreme Court rejects "but for" counterfactual test when assessing accountable profits in hands of fiduciary.

The defendants admitted that they had thereby breached their fiduciary duties, but they contended that their gain had not been caused by that breach. They accepted (see paragraph 7) that for the court to countenance this defence, it would need to depart from principles laid down for centuries in *Keech v Sandford [1726] EWHC Ch J76*, and at the highest level in *Regal (Hastings) Ltd v Gulliver (1942) Note [1967] 2 A.C. 134* and *Boardman v Phipps [1967] 2 A.C. 46*. These authorities hold that a fiduciary must not without the principal's consent retain any



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profit derived from the fiduciary position. There is a related rule that a fiduciary must avoid placing themself in a position where interest and duty conflict (paragraph 16).

The defendants also had to face a further difficulty that courts have long resisted any attempt to water down these principles by a "but for" test which might allow a fiduciary to keep what they would have acquired, had they committed no breach of duty (paragraphs 38 to 39). The only mitigation of this principle (developed in *Regal* and in *Boardman*) was that, as a matter of discretion, the court may award fiduciaries an allowance as a reward for work and skill they have devoted, or for having put their own capital at risk (paragraph 57).

The defendants' justifications for seeking to change the law are summarised at paragraph 45. These principally were that:

- The present position is draconian because it does not take adequate account of honest fiduciaries who have devoted themselves to a post termination business.
- A discretionary equitable allowance is an inadequate amelioration.
- The hesitancy of courts of equity in constructing counterfactuals in claims for accounts of profits by fiduciaries is outdated, given that claims for equitable compensation to make up for losses to beneficiaries are now well established.
- The remedy of equitable compensation has been improved by the adoption of this technique.

Central to the defendants' case was the proposition that a fiduciary's liability arises because of a breach of a fiduciary duty and that, as with any case of breach of duty, it is proper for the court to consider whether there is a causal link between an alleged breach of fiduciary duty and the fiduciary's receipt of the profits for which an account is sought. If the fiduciary would have received the profits even if there had been no breach, it follows that there is no causal link and therefore no liability. Here the approaches of the judges diverged.

According to the majority (Lords Briggs, Reed, Hodge and Richards) a fundamental difficulty for the defendants is that a principal's entitlement is not confined to the right to a remedy for a wrong. Instead, the profits connected to the fiduciary role are to be treated as belonging to the principals from the moment they are made (paragraph 47) and that this simple proprietary right is not to be watered down into a duty only to avoid making and keeping profits which one cannot show that one would have been able to make anyway. A duty to account, moreover, can arise where there is no breach in the fiduciaries' performance of their duties, as in the three cases cited above, and even where the performance is praiseworthy, as in the last two of these cases. No breach being needed, there is accordingly no need to seek any causal link to one, and accordingly, "the appellants' submissions calling for the application of a 'but for' test of causation would never get off the ground" (Lord Burrows at paragraph 260).

The majority also found it unhelpful to follow the approach of the equitable compensation cases because compensation is about restoring losses, whereas the law regarding fiduciaries is not about restoring losses but enforcing property rights (paragraph 56).

The majority held further that a causal "but for" test is no substitute for the existing regime of recognition of proprietary rights, mitigated only by a discretion to reward conscientious fiduciaries where appropriate. This is because it would work injustice against the principal as adequate protection is achievable only by a strong general rule which removes any temptation for wrongdoing, and because it could work injustice against a conscientious fiduciary because it might sometimes provide an inadequate reward, given the infinite variety of possible cases that there can be (paragraph 58).

The analysis of the majority encounters difficulty, however, with the question of how one is to link a benefit with a defendant's position as a fiduciary. No-one would suggest, after all, that a fiduciary would have to disgorge profits which had nothing to do with the position as fiduciary (see the majority at paragraph 25 and Lord Burrows at paragraph 270).

The main difference between the approaches is this. The majority accepted that the fiduciary position and the receipt of profits need to be linked, but not necessarily causally, to a defendant's fiduciary position. The link derives not necessarily from any breach of duty, but from the fact that the fiduciary is enjoying a profit or gain which has accrued as a result of the fiduciary position (see paragraphs 34 to 36).

Lord Leggatt (with whom Lord Burrows largely agreed) criticised this view, however, both theoretically and practically. Lord Leggatt observed that it made no sense to speak of a connection which was not a causal connection (paragraphs 154 to 159) and that the need for such a connection therefore opens up the possible need to investigate counterfactuals after all (paragraph 162).

Thus, if the principal's entitlement is the result of a breach of duty out of which the right to a remedy arises, as opposed to it being something which arises automatically whenever a fiduciary earns a profit or receives property derived from the position as fiduciary, it follows that it is open to the court to enquire whether there has in fact been no breach which would render it unlawful for the fiduciary to keep all or some of the property so obtained.

In Lord Leggatt's view, no right arises automatically when a fiduciary acquires property because of the fiduciary relationship. Instead, it is the application of the property to the fiduciary's own use which can be actionable, and when that happens, the principal is entitled to seek a remedy which can, but need not, include an account and an order to pay what is found to be owing. No useful purpose would be served by imposing yet another duty (paragraphs 215 and 229).

He also noted the difficulties in imposing a duty before the court has decided to what it extends and how it is to be quantified (paragraph 216). He also saw no justification for adopting different principles to identify and quantify profits from those adopted to identify and quantify losses (paragraphs 149 and 170).

In any investigation into causation, it is necessary first to identify the specific duty of which the defendant was in breach. According to Lord Leggatt, the relevant breach is not generally the receipt of an asset, nor is it necessarily anything done while the fiduciary relationship was in being. The earning of a profit or its receipt are not breaches unless they are followed by a retention of the property adverse to the principal or an application of it for the fiduciary's own use. Only then is there a breach (paragraph 95).

In *Rukhadze*, the failure to seek the claimant's permission to retain the profit was not a breach of duty, as there was no duty to seek such permission (paragraphs 178 and 201). It was not legitimate therefore to pose as a counterfactual what would have happened if the negotiations for a profit-sharing agreement had continued. Any likelihood that permission would have been given for the defendants to retain a part of the profit so as to remove any culpability for the defendants' retention of these was, for that reason, irrelevant. It was therefore right for the appeal to fail, even without the reasoning of the majority.

On the other hand, if contrary to the facts, the fiduciaries had acted honestly throughout, and had benefited the principals by their conduct or by their investment of money which the principals could not raise, an argument for changing the law so as to favour such fiduciaries would be worthy of serious consideration (Lord Leggatt at paragraphs 139 and 142).

So where would we be if a more sympathetic case came before the court? It seems that the court would be bound to find that the profit automatically belongs to the principal when it is received, and that no further investigation is needed, save as to whether there should be a discretionary allowance. Nonetheless, it could be argued that the majority view is not essential to the actual decision in *Rukhadze* and that it can be otherwise supported.

Because the majority so clearly based its decision upon this view, however, it would difficult be to contend that it was mere obiter dicta. Difficult, but not necessarily impossible. See *R. (on the application of Youngsam) v Parole Board [2019] EWCA Civ 229* at paragraphs 58 to 59 for its discussion on identifying a ratio decidendi.

Perhaps the best way through may be found in Lord Burrows' judgment at paragraph 295:

> "My own inclination is to think that, even in the context of breach of fiduciary duty, an equitable allowance should be readily allowed because, like disbursement, making that allowance goes to the correct calculation of the net profit made by the defendant."

For now, though, the law is that the fiduciary's duty inevitably arises when the property is received: "Duty is loot, loot duty."

Whether that is all we know or all we need to know remains to be seen.