SECOND DIVISION, INNER HOUSE, COURT OF SESSION

[2018] CSIH 27
P194/16

Lord Justice Clerk
Lord Brodie
Lord Glennie

OPINION OF LADY DORRIAN, the LORD JUSTICE CLERK

in the reclaiming motion

by

CENTENARY 6 LIMITED

Noter and reclaimer

against

ROBERT CAVEN and KEVIN MAWER

Respondents

in the liquidation of Centenary Holdings III Limited (in liquidation)

Noter and reclaimer: Smith QC, Smart; TLT LLP
Respondents: Borland QC; CMS Cameron McKenna Nabarro Olswang LLP

10 April 2018

Introduction

[1] By interlocutor dated 14 December 2016, the reclaimer was ordained by Lord Doherty to find caution for expenses in the sum of £100,000. The proceedings were sisted until caution was found. On 15 February 2017, no caution having been lodged, the matter called before a different Lord Ordinary, when the reclaimer was given 28 days in which to do so. The reclaimer did not do so, resulting in a motion to refuse the prayer of the

note on account of that failure. This motion was heard on 29 March, and continued for further hearing on 5 April. By 29 March, the reclaimer had proffered an After the Event ("ATE") policy, and a motion was made at the bar to allow this to be approved as a method of security alternative to caution, in terms of RCS 33.4(2) and to allow the case to proceed. After hearing the motion, it seems that the Lord Ordinary indicated orally that she did not consider the ATE policy to be satisfactory security. However, she acceded to the reclaimer's motion to be granted a further 28 days to find caution as originally ordered on 14 December 2016. On 5 May 2017, the reclaimer produced a Deed of Indemnity (the "DOI"), proffered as a bond of caution. The Lord Ordinary refused to accept the DOI as caution, and in her interlocutor she formally refused the motion previously made in respect of the ATE policy. She acceded to the respondents' motion to refuse the prayer of the note in terms of RCS 33.10(a).

[2] The focus of this reclaiming motion was that final interlocutor of 5 May 2017. A challenge to the original order for caution was not insisted upon.

Legislation

[3] Section 726(2) of the Companies Act 1985 provides as follows:

> "(2) Where in Scotland a limited company is pursuer in an action or other legal proceeding, the court having jurisdiction in the matter may, if it appears by credible testimony that there is reason to believe that the company will be unable to pay the defender's expenses if successful in his defence, order the company to find caution and sist the proceedings until caution is found."

Rules of Court

[4] The rules relating to caution are to be found in chapter 33, the main provisions of relevance being as follows:

> "33.1 Subject to any other provision in these Rules, this Chapter applies to-

(a) any cause in which the court has power to order a person to find caution or give other security; […]

33.4.-(1) A person ordered-

(a) to find caution, shall do so by obtaining a bond of caution; or

(b) to consign a sum of money into court, shall do so by consignation under the Court of Session Consignations (Scotland) Act 1895 in the name of the Accountant of Court.

(2) The court may approve a method of security other than one mentioned in paragraph (1), including a combination of two or more methods of security.

(3) Subject to paragraph (4), any document by which an order to find caution or give other security is satisfied shall be lodged in process.

(4) Where the court approves a security in the form of a deposit of a sum of money in the joint names of the agents of parties, a copy of the deposit receipt, and not the principal, shall be lodged in process.

(5) A bond of caution or consignation receipt lodged in process shall be accompanied by a copy of it.

[…]

33.6.-(1) A bond of caution shall oblige the cautioner, his heirs and executors to make payment of the sums for which he has become cautioner to the party to whom he is bound, as validly and in the same manner as the party and his heirs and successors, for whom he is cautioner, are obliged.

33.7.-(1) The Deputy Principal Clerk shall satisfy himself that any bond of caution or other document, lodged in process under rule 33.4(3), is in proper form.
(2) A party who is dissatisfied with the sufficiency or form of the caution or other security offered in obedience to an order of the court may apply by motion for an order under rule 33.10 (failure to find caution or give security).

[…]

33.10 Where a party fails to find caution or give other security (such a party being in this rule referred to as 'the party in default'), any other party may apply by motion-

(a) where the party in default is a pursuer, for decree of absolvitor; or

> (b) where the party in default is a defender or a third party, for decree by default or for such other finding or order as the court thinks fit."

Opinion of the Lord Ordinary

The ATE policy

[5] The Lord Ordinary considered that the underlying objective of an order for caution was to secure payment of the judicial expenses of the benefiting party. The liability of the cautioner was contingent only upon the award of expenses against the principal obligant, and the latter's default thereunder (para [46]; RCS 33.6(1)). Section 726(2) envisaged the provision of a "guarantee of the …. judicial expenses, rather than merely a level of comfort" (para [47], citing *Monarch Energy Ltd* v *Powergen Retail Ltd* 2006 SLT 743, Lord Drummond Young at para 11). Consequently, any alternative to caution for the purposes of rule 33.4 "must … fulfil the same purpose as a bond of caution" (*ibid*).

[6] In the present case, there were too many features of the ATE policy that were outwith the respondents' control or within the discretion of the insurers, such that it did not provide sufficient certainty of payment of the respondents' expenses. Four features in particular made the deed unacceptable (para [48] *et seq*):

(i) there was no provision for a claim by or payment to the respondents directly, and endorsement of the respondent's interests on the policy was not possible; to that extent, the respondents would be dependent on the "goodwill" of the reclaimer to claim and pay over any sums due, and there was nothing to prevent any recovered sums from falling into the general pot of unsecured assets in respect of which the respondents would rank as ordinary creditors only;

(ii) the insurers were entitled to treat the policy as void in the event of the reclaimer's insolvency. This was problematic, given that caution had been ordered on the basis

that the court had been satisfied that the reclaimer would be unlikely to be able to pay the respondents' expenses;

(iii) there was a right of immediate cancellation of the policy by the insurers if they or the reclaimer's agents considered that the reclaimer's prospects of success fell to 50:50 or less, in which case the respondents would be deprived of the benefit of the policy at the very point when it was needed; and

(iv) the continuation of cover under the policy was otherwise dependent upon a variety of matters outwith the respondents' control but within the discretion of the insurers, or otherwise dependent upon the reclaimer's conduct, including ongoing reporting, disclosure and cooperation obligations, and the exclusion of cover in the event of proceedings being discontinued due to lack of funds on the part of the reclaimer.

[7] There was no mitigating protocol in respect of the fourth of these features, as had been offered in *Monarch.* The additional concern in that case, namely the potential for avoidance of the policy for fraud, was not an issue in the present case. Nevertheless, the remaining features were "too far removed from the clear, simple and readily prestable obligation in a bond [of caution] to qualify as a suitable alternative for the purposes of rule 33.4" (para [55]).

The Deed of Indemnity ("DOI")

[8] The Lord Ordinary noted that the position of the reclaimer's counsel was "essentially passive" in tendering the deed (para [60]). He had declined to make any submissions as to its import, on the basis that it bore to be governed by English law. The deed bore to be a quadripartite one but had been signed only by the insurers. Senior counsel for the reclaimer had asked for a further continuation of two days to arrange for it to be signed. The Lord

Ordinary concluded that there was no basis for allowing this, standing the history of the case. She accepted the respondents' submissions with regard to the apparent deficiencies of the deed (para [61]). The deed, being unsigned by all parties, was ineffectual and, in any event, insufficient in its terms. Clause 3, which contained the operative undertaking to pay "costs" (*sic)*, was suspended by virtue of clause 2, which provided that the deed only came into effect if the claim was not struck out for reasons related to an order for security for "costs" or the court approved the deed as sufficient security. The jurisdiction of the Scottish courts was excluded by clause 15. Accordingly, the Lord Ordinary concluded that the DOI had not brought into existence any binding undertaking in relation to the respondents' expenses.

[9] The reclaimer had had some 5 months within which to obtemper the order for caution, and had endeavoured to obtain a bond since around mid-March 2017. The continuation of matters on 5 April had been accepted by the reclaimer as the "final indulgence" to be expected from the court (para [62]). Given the stance of the respondents, there was no prospect of the deed being signed, and therefore no utility in granting further time for this purpose. In any event, the non-justiciability of the import of the deed precluded satisfaction of the suspensive condition (cl 2). Accordingly, the respondents were entitled to refusal of the prayer of the reclaimer's note (RCS 33.10).

Answers to grounds of appeal

[10] It is necessary to say something at the outset about the form of the respondents' answers. In response to two substantive grounds of appeal (only one of which is now insisted in), contained in three pages of text, the answers span some 19 full pages set out across five chapters and some 147 paragraphs, including what is properly to be regarded as

argument, with numerous references to authority, and aspects of procedural history. Indeed, the answers are some five pages longer than the respondents' relative note of argument, which is itself around twice the length of the reclaimer's note of argument. (The reclaimer's note of argument does not entirely escape criticism itself. It is, like the respondents' note, unhelpfully set out in single line spacing. More importantly, however, the lack of consistent paragraph numbering makes the note almost impossible to navigate.)

[11] It should be emphasised that such a lengthy and unfocussed document is not helpful to the court; rather, answers should mirror the grounds of appeal insofar as consisting of "brief specific numbered propositions", from which arguments may be developed in the subsequent notes of argument, and further refined in oral submissions (RCS 38.18(1); PN No. 3 of 2011, paras 78 and 86). These documents serve distinct purposes, as part of an iterative process, and it will rarely assist parties to indulge in prolixity in either case. Most importantly, any grounds or answers ought to form the mere framework of the reclaiming motion, with moderately detailed written argument being confined to parties' subsequent notes. As a rule of thumb, the distinction ought to be plain from the appearance and relative substance of each document.

[12] In the interests of fairness, the matter not having been explored in the course of the hearing, I should note that it is not known what role, if any, counsel appearing before this court played in the preparation of the various documents lodged in the present case, and therefore these comments do not direct any criticism to the particular counsel appearing.

Submissions for the reclaimer

[13] Although the Note of Argument seemed to foreshadow an argument that the Lord Ordinary ought, first, to have considered whether proceedings should be brought to an end,

and then to have addressed whether the security was adequate, this was not developed as a submission.

The ATE policy

[14] The reclaimer argued that the Lord Ordinary had erred in refusing to approve the ATE policy as an alternative to caution. The conclusion that there were too many factors outwith the respondents' control failed to take account of the fact that there were significant limitations upon when an insurer could seek to avoid liability to make payment under such a policy (*Quantum Claims Compensation Specialists Ltd* v *Wren Insurance Services Ltd* 2012 SLT 481, and 2011 SLT 1051). It would not be easy to do so on spurious grounds. An ATE policy provider would be unlikely to seek to avoid liability other than for good reason. That an insurer could theoretically avoid the policy was not the point: the point was whether this could and would be done "readily". One had to weigh the escape provisions against the nature of the claim. In *Monarch (supra),* and in *Premier Motorauctions Ltd* v *PricewaterhouseCoopers LLP* [2017] 6 Costs LO 865, where issues of fraud arose, there had been a risk of avoidance for non-disclosure. There was no such risk here.

[15] In *Monarch,* the possibility arose that some of the difficulties in the ATE policy could be overcome by a protocol, monitoring the operation of the policy. No such protocol had been offered to the Lord Ordinary, but she should nevertheless have considered whether this would be an option to address the concerns arising. The reclaimer was prepared, at least now, to offer any acceptable undertakings which would do so: the policy could be assigned in favour of the respondents, and the suggestion that the respondents would be reliant on the goodwill of the reclaimer could be dealt with by endorsement.

[16] In any event, the conclusion that the respondents would be reliant on the reclaimer's goodwill failed to take account of the fact that a party holding an award of expenses had a

number of procedural mechanisms available for enforcement (see, eg, *Martin & Co (UK) Ltd, Petitioners* [2013] CSOH 25; *Tods Murray WS* v *Arakin Ltd* [2013] CSOH 134 and *Kidd* v *Paull & Williamsons LLP* [2017] CSOH 124). Should these enforcement steps result in the reclaimer's insolvency, the Third Parties (Rights against Insurers) Act 2010 would entitle the respondents to take action directly against the insurers for the sum insured, which would not be available for general creditors. The Lord Ordinary's concerns thereanent had, therefore, been misplaced *(Harlequin Property (SVG) Ltd* v *Wilkins Kennedy (A Firm*) [2015] 3 Costs LR 495).

[17] The Lord Ordinary had applied too high a test to the requirements of RCS 33.4(2), which required simply that there should be "adequate alternative security". This did not require fulfilment of the "same purpose as a bond of caution".

The Deed of Indemnity ("DOI")

[18] The reclaimer submitted that the DOI constituted a bond of caution. Indeed, it offered "better security" than the usual bond of caution since the respondents would not be required to seek payment from the principal debtor for it to be effective. Accordingly, the DOI ought to have been held to discharge the order to find caution, being "of greater comfort" to the respondents (RCS 33.4(2)).

[19] Whilst the reclaimer acknowledged that the DOI incorrectly identified the respondents as the joint liquidators of the reclaimer, bore to be an agreement amongst four parties, inviting the respondents' signature, and contained several other errors, it was submitted that these "errors" did not render the operative indemnity clause 3, nor the entire deed, ineffectual. The designation of the respondents was plainly a clerical error in the recital, which was not replicated in the body of the deed, and ought to have been ignored

(*Mannai Investment Co Ltd* v *Eagle Star Life Assurance Co Ltd* [1997] AC 749, Lord Hoffmann at 774). The respondents had not required to sign or endorse the deed in order for the cautionary obligation of the insurers to be effective (Gloag & Irvine, *The Law of Rights in Security* (1897), p 693).

[20] Notwithstanding that the submission had not been advanced before the Lord Ordinary, it was submitted that "an effective, unconditional and irrevocable unilateral undertaking" by the insurers to indemnify the respondents up to the sum of £100,000 in respect of "costs" arose from clause 3, as supported by clauses 8 and 9. Clause 3 was severable from the remainder of the deed and constituted a binding, unilateral obligation. It was not "suspensive" or dependent upon "purification": the effect of the prior clause 2 was merely to ensure that the obligation would fall in the event that the reclaimer was deemed not to have found caution. The concept of a "suspensive" clause was more appropriate to mutual obligations (McBryde, *The Law of Contract in Scotland* (3rd edn), para 5-41) and the Lord Ordinary had erred to the extent that she had sought to introduce it in the context of a unilateral guarantee.

[21] Notwithstanding that it appeared in a document bearing to regulate matters amongst four parties, therefore, clause 3 could stand alone. The deed having been signed by the cautioner and effectively delivered to the respondents, as a unilateral obligation, it did not have to be signed by them too. It was wholly unnecessary, for the obligation to be effective as respects the respondents, that they endorsed or signed the deed.

[22] The Lord Ordinary had failed to consider whether clause 3 amounted to a clear and binding obligation to make payment of expenses should the reclaimer fail to do so, irrespective of whether the deed may have appeared to be "slapdash and shoddy". The operative clause was "unaffected" by either the substantive applicable law or prorogation

clause; properly construed, those clauses applied to the mutual obligations between the insurers and reclaimer only, and were irrelevant to the obligation in clause 3 in favour of the respondents. In any event, the governing law was to be presumed to coincide with Scots law, no contrary submission having been advanced by the respondents (Anton, *Private International Law* (3rd edn), para 27.171). Moreover, there would appear to be no material difference between the position of a cautioner according to Scots law, and that of a surety according to English law (see, eg, Gloag & Irvine, *supra*, p 642; cf *Vossloh Aktiengesellschaft* v *Alpha Trains (UK) Ltd* [2010] EWHC 2443 (Ch), Sir William Blackburne at paras 21 – 22).

[23] With regard to the remaining particular clauses of the deed, clause 5 merely reflected the insurers' right to make representations, via the reclaimer, to the auditor in respect of any account of expenses, and did not require the respondents' agreement; clause 6, which provided for the means by which any agreement reached between the reclaimer and respondents would be confirmed to the insurers, was strictly unnecessary, and if anything of benefit to the respondents; clause 8 did not require to define the "principal debtor", which was in common usage and well-understood in the context of cautionary or surety obligations (see, eg, Gloag & Irvine, *supra; Bank of Ireland v Morton* 2003 SC 257); and clause 13 could not affect the rights of the respondents as creditor in respect of what was an unqualified unilateral bond. The Lord Ordinary ought to have striven to give effect to the obligations plainly intended by the parties, and to have asked whether, objectively, the granter of the deed intended to be bound (*Royal Bank of Scotland* v *Carlyle* 2015 SC (UKSC) 93, *per* Lord Hodge at para 29).

Submissions for the respondents

[24] The respondents submitted that section 726(2) of the 1985 Act proceeded on the

hypothesis that the defending party will be successful in its defence of the claim. That provision, as supplemented by RCS 33.6(1), was intended to ensure that limited liability was not used as a means of evading the payment of expenses, and envisaged that the security offered must provide a "full guarantee" of the defending party's expenses, rather than merely a degree of comfort, which could only be achieved if the party providing the security was liable in exactly the same manner as the pursuing party (*Monarch (supra),* Lord Drummond Young at para 31).

The ATE policy

[25] The Lord Ordinary had applied the correct test, namely that any alternative method of security must fulfil the same purpose as a bond of caution. To this end, the ATE policy was to be construed on its own terms, without reference to any general and unvouched assertion as to the position of legal expenses insurers. A number of features of the policy supported the Lord Ordinary's conclusion that it was unsuitable: it could be cancelled immediately and at any time, according to the insurers' view of the reclaimer's prospects of success, irrespective of the view of the reclaimer's legal representatives, in relation to the whole dispute and/or any interim hearings (cl 10.5); it was conditional upon the reclaimer having "greater prospects of being successful rather than unsuccessful" on the legal merits or according to any other factors (cl 3 and 6.1.2), which could conceivably turn on expert reports or witness statements lodged in due course. These features alone rendered the ATE policy insufficient as a "full guarantee" (see, eg, *Michael Phillips Architects Ltd* v *Riklin* [2010] BLR 569, Akenhead J at paras 18(c), 22, 23 and 27 – 30; *Premier Motorauctions*, *supra,* Longmore LJ at para 31).

[26] The additional features of the policy identified by the Lord Ordinary also supported her conclusion in this regard: the extensive notification and cooperation obligations incumbent upon the reclaimer and its legal representatives, non-compliance with which would entitle the insurers to withdraw coverage under the policy (eg cl 3.1 – 3.3, 5.1.18.14, 6.1.3 and 6.1.4), and over which the respondents would have no control; the lack of coverage in respect of the respondents' expenses where the reclaimer's case was "abandoned, lost, withdrawn or discontinued owing to… lack of funds or funding" (cl. 5.1.18.6), a legitimate concern in this case, given the basis upon which the (now unchallenged) order for caution was made; and the exclusion of coverage in respect of appeal proceedings (cl 5.1.9), subject to the insurers' consideration afresh of whether to extend coverage under the existing or a new policy (cl. 7.3), such that it was tolerably clear that the expenses of any reclaiming motion would not be covered under the policy offered presently. Such clauses were capable of enforcement by the insurers, and there was no good reason to consider that they would not be invoked, if appropriate, and quite legitimately, in order to avoid liability under the policy. Indeed, the Lord Ordinary had not suggested that the insurers would seek to do so otherwise than for good reason.

[27] In any event, the policy gave the respondents no direct right of recourse against the insurers, the only party having enforceable rights thereunder being the reclaimer itself. Thus, the policy did not oblige the insurers to meet the respondents' expenses "as validly and in the same manner" as the reclaimer. These features, individually and taken together, indicated that the policy did not amount to a "full guarantee", as section 726(2) and rule 33.6(1) required. The Lord Ordinary's conclusions in this regard could not be said to be plainly wrong or wholly unreasonable, but an exercise of her discretion within reasonable parameters.

The Deed of Indemnity ("DOI")

[28] The principal DOI was not lodged until 5 May 2017, after expiry of the deadline of 3 May, the reclaimer's agents having sought only to lodge a copy on the last day for doing so. Accordingly, on any view, no effective form of caution had been lodged timeously. No draft of the deed had been intimated to the respondents' agents in advance of the lodging deadline. Another version of the deed, signed only by the reclaimer, had not been relied upon during the hearing on 5 May (Opinion, para [35]).

[29] During the hearing on 5 May, the reclaimer's then senior counsel had made no substantive submissions in support of the deed, on the basis that it was governed by English law, and had adopted an "essentially passive" position in relation to its effect. If anything, this fact rather supported the Lord Ordinary's doubts as to the efficacy of the deed. The deed, as a quadripartite agreement, had not been signed by all parties to it. On that basis alone, as a basic principle of contract law, the agreement was of no legal effect (see, eg, *Hoult* v *Turpie* 2004 SLT 308, Lord Drummond Young at paras 10 – 12). Accordingly, it was not capable of constituting a suitable form of caution or security, particularly having regard to the fact that the respondents were unwilling to agree to its terms.

[30] In any event, as at 5 May, the deed was not yet in force, its operation being conditional upon the matters set out in clause 2. Moreover, it required the respondents to assume obligations to provide information to the insurers (cl 4), and it purported to regulate matters as between the insurers and the reclaimer (cl 9 and 10).

[31] All that being so, the Lord Ordinary could have had no real certainty as to the efficacy of the deed as a suitable form of caution or security. Specifically, having regard to the terms of clauses 2 and 3, the Lord Ordinary had had no basis upon which to conclude

otherwise than that there was no prestable obligation contained within the deed. The reclaimer having been given ample opportunity to produce an effective form of caution prior to the hearing on 5 May, the Lord Ordinary had been reasonably entitled, in the exercise of her discretion, not to allow more time to do so. In any event, section 726(2) and RCS 33.4(1) envisaged the reclaimer producing caution, and did not empower the court to compel the respondents to do anything pursuant to that obligation, such as to execute the proposed agreement.

[32] Accordingly, the reclaiming motion ought to be refused.

Analysis and decision

[33] Prior to enactment of the 1985 Act, the Companies Act 1948 contained a single provision applicable to Scotland, and to England and Wales alike: section 447 of the 1948 Act provided that the court may require "sufficient security" for costs and may "stay" proceedings until the security is given. With the enactment of the 1985 Act, however, there was introduced specific provision for Scotland, recognising the particular requirement in this jurisdiction for security in the form of caution, and the corresponding terminology of sisting proceedings until caution is found. The point of such an historical analysis is to emphasise that the statutory requirement applicable to Scotland is addressed to the provision of caution specifically, and not to the provision of 'security' more generally. A cautioner "binds himself as cautioner with the principal, for the greater security of the creditor" or "under a distinct and separate obligation, in which he is himself the principal" (Bell's Dictionary (7th edn), p 151: "Cautionry"), and so the creditor may proceed directly against the cautioner.

[34] Your Lordship, Lord Glennie, raises the possibility (page 7) that when granting a statutory application a Lord Ordinary might see fit to approve an alternative form of security as provided for in RCS 33.4(2). I beg leave to doubt that, although I should not be taken as having reached a concluded view on the matter in the absence of detailed argument on the point. However, it should be noted that where the statutory test is met, and the court is satisfied that security should be ordered, the statute provides that the security which will be ordered will take the form of caution, not some other, perhaps lesser, form of security that may be offered. I would accept that the issue is one of substance not form, so a deed may meet the requirements of a bond of caution without being described as such. However, in that case it will meet the requirement to provide caution: it will not be some alternative form of security. It will fall within RCS 33.4(1), not RCS 33.4(2). The relevant chapter of the Rules of Court is designed to cover awards of caution and provision of other security generally, but despite the generality of RCS 33.4(2) it would seem to me that, in the context of an award under section 726(2) of the 1985 Act, it cannot override the terms of the statute specifying security in the form of caution. Of course, in the event of some other security being offered at the stage of a statutory application, the court will take that into account in determining whether the statutory test has been met; or as a factor mitigating the extent of caution to be found. The relative strengths of the parties cases may entitle the court to decide not to grant the application, even though the test has been met (see *Monarch,* para 10), but if the application is to be granted, the applicant is entitled to an order for caution. Where a party offers an alternative form of caution, which proves acceptable to an applicant, the likely result may be that the statutory application would not be granted, and that the court would simply give effect to the parties' agreement that security should be given in the form agreed.

[35] Thus, with the benefit of further reflection, I also doubt the validity of part of the basis upon which the submissions proceeded, namely the assumption that when Lady Wolffe was considering the motion to refuse the prayer of the note, it would have been open to her to approve some different form of security rather than caution as ordered by Lord Doherty. The court would not be entitled to approve some other security in substitution, if it would not have had the power to do so upon determination of the original application. In any event, a party ordered to lodge caution in terms of section 726(2) may ask for the order to be varied, for example as to amount, or recalled. It may have obtained an alternative form of security such that it could be argued that the statutory test is no longer met, and that the order should be recalled. But it is not obvious that, caution having been ordered under section 726(2), a party, instead of seeking recall, may subsequently rely on RCS 33.4(2) to seek approval of the provision of any security which falls short of meeting the requirements of caution. Where caution has been ordered under section 726(2) and not found, the offer of another method of security would be relevant only to the extent of excusing the defaulting party from the full consequences that may otherwise flow from the default. On the basis of the authorities (see, for example, *Monarch,* para 11), where the court is satisfied that the suggested alternative provided a security as good as that of caution, the court might exercise its common law discretion to allow proceedings to continue, notwithstanding the failure to find caution, due to some satisfactory method of security having been offered.

[36] In the present case, a statutory order for caution was granted and is not challenged before this court. Nor was any motion for variation or recall of that order made before the Lord Ordinary. Moreover, the reclaimer concedes that there has been default in terms of the original order for caution, which accords with the analysis outlined above, that approval of

any other security would not avoid default in terms of the original order for caution. Thus, it was only the consequences that should follow upon such a default, taking account of any other security offered subsequently, which arose as a discretionary matter for the court at first instance. There again, however, any such exercise of discretion ought not to function as a method by which to circumvent the original order in circumstances where its variation or recall is not sought. That is certainly the case here, where the original order for caution is not reclaimed. The narrow issue for this court is whether there are any grounds upon which it might legitimately interfere with the Lord Ordinary's exercise of discretion in that context.

[37] Whether to take action because of a failure to lodge caution, or because of an insufficiency in the form of caution offered, is for the party in whose interest the security has been ordered to decide (RCS 33.7; RCS 33.10): in the absence of a motion for absolvitor, or other decree by default, the court would be entitled to assume that that party does not insist upon the benefit of caution, whether by reason of some other security having been offered or otherwise. In practical terms, the nature of such a default, considered in isolation, is that it has consequences only for the applicant party, rather than wider consequences for the court in the administration of proceedings. Thus, as a generality, the sufficiency or form of caution will be the subject of interrogation by the court only to the extent that it does not appear to satisfy the applicant party. Where a motion is made under RCS 33.10, the applicant must recognise that the court will be entitled to have regard, in the granting of any discretionary remedy, to the terms and effect of any other method of security offered meantime by the defaulting party, and the extent to which there remains substantial default. The court may be unlikely in modern times to grant decree of absolvitor, or its equivalent, on the basis of a technical default, considered in isolation, if other factors such as the availability of some lesser form of security, perhaps in combination with other awards of

expenses as conditions precedent, may be sufficient to justify allowing proceedings to continue or to be dismissed and potentially re-raised in the interests of fairness and justice. That is not to say that the defaulting party should not expect to be held to the original requirement to find caution if proceedings are to continue: that requirement will not simply "fly off" at his option. The default may yet require to be remedied, notwithstanding any other procedures designed to address the prejudice arising to the applicant party. Ultimately, the defaulting party will be at real risk of the primary remedy of absolvitor, or other decree by default, passing against him where his default is founded upon and remains unaddressed. Indeed, the court may be expected to look severely upon any party who seeks to rely on the exercise of discretion merely to flout the requirements of earlier orders.

[38] In sum, therefore, it is important to recognise that in this reclaiming motion we are not dealing with a challenge to the original decision of the Lord Ordinary ordaining the reclaimer to find caution in terms of an application under section 726 of the Companies Act 1985. Had an appropriately worded ATE policy been in place at that time, it is no doubt a factor that would have been taken into account in determining whether the test in section 726 was satisfied, but no such policy was (or indeed, is) in place, and no such argument could have been advanced. Equally, in such an application the court will bear in mind that the effect of granting it may be to terminate the claim. The court may ask the question whether "... it might amount to a denial of justice if the case were not allowed to proceed on other terms" (*Morrison* v *Morrison's Exrx* 1912 SC 892, Lord President (Dunedin) at 895). In certain circumstances, it might be oppressive or disproportionate in all the circumstances, having regard to the nature of the claim and the defence, to grant the motion. For example, where there is a very strong claim, and a very weak, irrelevant or formal defence; where there is a question over a defender's good faith in either the defence or in

making the application for caution: these may be considerations which weigh against the granting of the motion. The conduct of the parties in the litigation to date may also be relevant. However, without a factor indicating some sort of imbalance or unfairness in the situation, the fact that the order for caution may make it possible or probable that the pursuer company will be unable to pursue the claim is not in itself a reason to refuse the motion.

[39] In *Monarch Energy Ltd* v *Powergen Retail Ltd* 2006 SLT 743, Lord Drummond Young referred (at para 10) to the words of Lord Maxwell in *Dean Warwick Ltd* v *Borthwick* 1981 SLT (Notes) 18 (at 19) that:

> "… if the requirement to find caution will in fact make it impractical for the pursuer to proceed, that merely goes to demonstrate that the conditions justifying the requirement of caution are fulfilled."

[40] In dealing with an application under section 726, the court must balance the prejudice to the pursuer in being unable to pursue a possibly meritorious claim against the prejudice to a successful defender in being unable to recover the expense of his successful defence, but must do so in the context that, for reasons to prevent abuse of the status of limited liability, impecuniosity alone may be a sufficient basis for granting the motion. In the present case, the original Lord Ordinary weighed, as far as was reasonably possible at that stage, the strengths and weaknesses of each party's case and concluded that each was arguable. As Lord Drummond Young noted in *Monarch (supra,* at para 17):

> "In such a case the normal rule, that caution will be ordered if it appears that a company pursuer will be unlikely to pay the defender's expenses if the latter is successful, must be applied."

[41] In the present case, the Lord Ordinary was satisfied on credible testimony that there was reason to believe that the reclaimer would be unable to pay the respondents' expenses if successful in their defence. Senior counsel for the reclaimer did not challenge that decision

before this court and restricted himself to arguing (a) that the ATE policy was a suitable alternative security, which should have been approved in terms of RCS 33.4(2); (b) that clause 3 in the DOI was a unilateral undertaking, amounting to a bond of caution, providing at least an equivalent level of security, and should have been accepted as such in terms of RCS 33.4(1)(a) (although no such argument had been advanced to the Lord Ordinary); (c) that, in any event, together they provided sufficient security in terms of RCS 33.4(2) (although no such argument had been advanced to the Lord Ordinary); and (d) that being so, the Lord Ordinary had erred in refusing the prayer of the note.

[42] I have already stated my views as to the arguments based on RCS 33.4(2). Whether the Lord Ordinary was correct to entertain that argument or not, the first issue to be determined was whether the ATE policy amounted to an offer of caution. The Lord Ordinary concluded that what was required was either a bond of caution or a deed which fulfilled the same purpose. I do not consider that she made any error in this respect, or in concluding that the ATE policy did not do so.

[43] In my opinion, largely for the reasons given by the Lord Ordinary (see para 6 above) and contained in the submissions for the respondents (see paras 25 – 27 above), the Lord Ordinary was entitled to conclude that the ATE policy did not provide an acceptable level of security. Having regard to the particular terms highlighted, the cover provided to the reclaimer under and in terms of that policy is simply too precarious to provide a meaningful safeguard to the respondents on the matter of expenses, such as would be expected in the case of a cautionary obligation, which the respondents are entitled to expect.

[44] In addition, whilst the respondents may avail themselves of rights under the policy by virtue of the Third Parties (Rights against Insurers) Act 2010, their entitlement to do so would be predicated upon the reclaimer's insolvency (2010 Act, s 6; *Monarch, supra,* at

para 23). It is no answer to this significant disadvantage, relative to a cautionary obligation, that the respondents may be able to bring about the necessary insolvency situation in reliance upon the awards of expenses that may be made in their favour in due course. That such steps may be necessary merely emphasises the unsatisfactory nature of the ATE policy, for present purposes, by comparison with a directly enforceable cautionary obligation.

[45] As to the sort of protocol which was offered alongside the ATE policy in *Monarch,* and designed to address the defects which, on the face of it, made that policy unsuitable, it was not suggested in argument to the Lord Ordinary that any such protocol, or any other mitigating step might operate to render the policy acceptable, or put it on the footing of a cautionary obligation. The respondents are given no directly enforceable claim against the insurers, that right being confined to the reclaimer. It does not offer a guarantee "as validly and in the same manner" as the claim against the reclaimer. In the reclaiming motion, it was suggested that such steps might be available, by means of a protocol, endorsement or assignation. However, these were merely speculative suggestions: in my view, there was absolutely no basis upon which the court could consider that the very many deficiencies in the ATE policy might be overcome, even if it were willing to engage in such an exercise when the Lord Ordinary had not been asked to do so. In fact, I note that one of the "solutions" posed to us was endorsement of the policy, to reflect the respondents' interests, yet in the Outer House it was specifically submitted, in answer to a question from the Lord Ordinary, that there was no prospect of this being achieved (Opinion, para [18]).

[46] An argument that the Lord Ordinary had erred in concluding that it was "too late" to consider whether the ATE policy amounted to sufficient security for the purposes of RCS 33.4(2) (Opinion, para [58]) was based on a misconception and essentially conceded as such by the reclaimer. The Lord Ordinary did not indicate that the nature of the policy

could only be considered at the stage of asking whether caution should be ordered. She clearly considered it relevant to the exercise of her discretion, and examined it carefully to determine whether it constituted a form of security equiparable to cautionary, and whether its existence would justify refusing the respondents' motion. This point needs no further consideration.

[47] Turning to the DOI, the Lord Ordinary was presented with a document riddled with drafting errors; containing English terminology; which bore to be a multi-party deed, signed only by the insurers; appearing to impose obligations on parties other than the insurers; to be construed according to English law; subject to the exclusive jurisdiction of the English courts; and produced only on the morning of the hearing. There may, as was submitted to this court, be little difference in substance between the law regarding cautionary obligations and the law of guarantee or surety, but that is not to say that there is no difference between how those obligations may properly be created, particularly in respect of the creation of an obligation by unilateral undertaking or promise. The whole argument for the reclaimer, however, depends upon this court being able to say that clause 3 of the deed can safely be construed as containing a binding, unequivocal, unilateral undertaking, enforceable against the insurers. The presumption that foreign law is the same as Scots law is of no assistance to a party in the position of the reclaimer, who, ordered to lodge a bond of caution, produces a different type of document and merely asserts that it has exactly the same effect and import as a bond of caution would have done. In those circumstances, and where the court's jurisdiction to construe the document is arguably excluded, it is incumbent upon the reclaimer to satisfy the court that the document does, as a matter of fact and law, have that effect.

[48] Whilst I might not agree with every aspect of the Lord Ordinary's reasoning (for example, her conclusion as to the suspensive effect of clause 2), I find it impossible to say that she erred in concluding that the document, as presented, did not fulfil the requirements of a bond of caution. The fundamental difficulty for the reclaimer is that its position is periled upon severance of a single clause, from a multi-party deed, which includes multi-lateral obligations. Against the terms of the document as a whole, in the context of which it appears and must necessarily be construed, it is not in my view possible to characterise clause 3, in isolation, as a "unilateral and unconditional" obligation of the kind to be found in a bond of caution. The deed contains a bundle of interdependent rights and obligations: they cannot be "unpicked" so that reliance can be placed solely on an obligation contained in a single clause. Clause 4 sought to place an obligation on the respondents to provide certain information to the insurers; clause 5 sought to give the insurers the opportunity to be represented at any taxation; and clause 7 expressly limited the extent of the obligation undertaken in clause 3. There is no basis for saying that the clauses regarding prorogation and choice of law are irrelevant to clause 3. It is impossible to say that clause 3 contains a free-standing obligation to be construed regardless of the other terms of the deed. To use the language of the respondents, it is impossible for the court to say that the insurers intended to create such an obligation irrespective of the remaining clauses of the deed.

[49] In all the circumstances, therefore, the reclaimer having failed to obtemper the order to find caution, and no other factors justifying the exercise of discretion to the contrary being commended to her or otherwise apparent, the Lord Ordinary was in my view entitled to refuse the prayer of the note. Accordingly, I suggest to your Lordships that the reclaiming motion ought to be refused.

Postscript

[50] Before this court, the reclaimer produced a further deed described as a "copy bond of caution" and bearing to be a DOI granted by the insurers in favour of the reclaimer and signed by them on 22 and 14 June 2017 respectively (Appendix, no 69). It appears, effectively, to be a version of the DOI referred to above, but "tidied up" to be a unilateral deed, subject to Scots law and the jurisdiction of the Scottish courts, and imposing no obligations on the respondents. Senior counsel for the reclaimer submitted that, if we accepted his primary argument that the original DOI could be read as a unilateral deed, then this revised deed should be accepted in substitution, for the sake of clarity and convenience. The new deed was said to contain the same obligation as the original, only in clearer terms.

[51] For the reasons noted above, in my view the reclaimer's primary argument falls to be rejected. It follows that the document now tendered is not, in my view, one which contains the same obligation as contained in the original: it is an entirely new document, and a new form of undertaking. The deed has been entirely redrafted.

[52] Senior counsel relied on this deed only if his primary argument succeeded. We were not asked to allow this deed, at this late stage, to be accepted as caution. There is no indication of any grounds upon which it would be appropriate for the court to entertain such a prospect at this late stage, apparently without notice in the grounds of appeal or relative (original or revised) note of argument, and notably following the numerous opportunities to do so permitted at first instance, which culminated in the reclaimer's then senior counsel accepting that the Lord Ordinary's interlocutor of 5 April 2017 would be the last continuation for this purpose, the Lord Ordinary having "stressed that this was the last indulgence to be afforded" in this regard (Opinion, para [32]).

[53] That was some 11 months ago, following which significant (likely irrecoverable) additional expense will have been incurred by the respondents in connection with the present reclaiming motion, which will not be covered by any caution that may now be approved. In those circumstances, and in the absence of any explanation whatsoever for the failure to obtain caution since around mid-March (Opinion, para [62]), the court would not be minded to grant any further indulgence. It is particularly noteworthy that the Lord Ordinary was not asked for any further indulgence for the purposes of rectifying or otherwise altering any matters of drafting in connection with the deed: only to allow its signature by the respondents. That being so, the Lord Ordinary cannot be criticised for failing to allow yet further opportunities to resolve matters, where the reclaimer was not offering to do so. It carries little (if any) weight to produce a substitute deed before this court in order to demonstrate what could have been done, or might have been found acceptable to the respondents, at a much earlier stage of proceedings.

[54] It must also be borne in mind that the issue determined by the Lord Ordinary on 5 May 2017 was not whether caution should be ordered, at which juncture the Lord Ordinary would consider the evidence of impecuniosity; the availability of other means of payment; the effect caution might have in stifling a claim; the proportionality of making such an order, and so on: all as referred to in para [38] above. Where the issue before the court is compliance with an order for caution already granted, the purpose is dictated by the formal requirement for caution as construed above, rather than the more amorphous concept of whether a company is likely to meet its expenses.

[55] At the stage of applying RCS 33.10, the failure to find caution or give other security is presupposed. In other words, the reclaimer must satisfy the court that there has, in fact, been no such failure; or that, notwithstanding such failure, mitigating factors would justify

the court in exercising its discretion to allow proceedings to continue. The reclaimer challenged the Lord Ordinary's findings in the former respect only, no broader considerations having been relied upon before her, or before this court. Whilst the court is aware of the substantial nature of the claim before it in the present case, the reclaimer must accept responsibility for the proper conduct of that claim, and if necessary draw to the court's attention any matters upon which it may wish to rely in order to argue, for example, that it would amount to a denial of justice if the case were not allowed to proceed. No such matters were advanced, by way of general appeal to the equities of the situation in which the reclaimer now finds itself. The reclaimer found solely upon the nature and effect of the "security" now offered. In those circumstances, notwithstanding any concerns that the court may have with regard to the conduct of matters to date, the court cannot be expected to take it upon itself either to speculate as to where the justice may lie between the parties, without having been addressed on such matters, or somehow to rescue the reclaimer from its current predicament, where to do so would inevitably involve further speculation as to the other remedies, if any, that may be open to it.

[56] The scope of a reclaiming motion is generally confined by the terms of the issues raised in the grounds of appeal. In the present case, those grounds, and hence the arguments advanced, were in relatively narrow compass. The approach suggested by your Lordship, Lord Glennie, that the reclaiming motion should be allowed on the basis of some uncertain prospect of agreement between the parties as to the adequacy of the revised deed, which failing a repeat of the procedure under rules 33.7(2) and 33.10 would be anticipated, was not one advanced by senior counsel for the reclaimer. Indeed, he effectively renounced such an approach, accepting that the revised deed would only be of relevance if his primary arguments succeeded. He did not argue that, notwithstanding the various failures to date,

there were explanations or other equitable considerations that should have caused the Lord Ordinary, or at least should cause this court, to decide in the reclaimer's favour. Had he advanced such arguments, the respondents would have been entitled to counter them, and this court would have had to take those arguments into account. We cannot do so, and the candid response of the respondents' senior counsel, that he did not have instructions in relation to the revised deed in the absence of any application for its approval having been placed before the court, emphasises the point that such a disposal would stray beyond anything contemplated by the parties themselves. In effect, such a disposal would require us to disregard the substance of the reclaiming motion, drawing a line through the procedural history following upon the original order for caution to date, and to treat the revised deed as if it had been placed before the court at a much earlier stage, prior to the making of any motion by the respondents under rule 33.10, notwithstanding that no justification whatsoever has been placed before us to suggest that such a radical course would be appropriate. The revised deed may, or may not be in terms which effectively constitute a bond of caution: it may be observed, at least, that it is not presented in conventional form. It seems possible, if not likely, that the respondents would seek to argue that it did not constitute such a bond. No argument on any of these matters was advanced before us, and there is no basis upon which this court could be satisfied that yet further opportunity to explore these matters ought now to be permitted, far less imposed upon the parties. In the absence of any relevant error, it is not the function of this court to take the presentation of a reclaiming motion as an opportunity to substitute its own decision making.

SECOND DIVISION, INNER HOUSE, COURT OF SESSION

[2018] CSIH 27
P194/16

Lord Justice Clerk
Lord Brodie
Lord Glennie

OPINION OF LORD BRODIE

in the reclaiming motion

by

CENTENARY 6 LIMITED

Noter and Reclaimer

against

ROBERT CAVEN and KEVIN MAWER

Respondents

in the liquidation of Centenary Holdings III Limited (in liquidation)

Noter and Reclaimer: Smith QC, Smart; TLT LLP
Respondents: Borland QC; CMS Cameron McKenna Nabarro Olswang LLP

10 April 2018

[57] I have had the very considerable advantage of seeing the opinions of your Ladyship in the chair and your Lordship in draft. Beyond indicating what I see to be the appropriate disposal, I have very little to add.

[58] The noter and reclaimer has departed from the contention that the Lord Ordinary (Lord Doherty) erred in ordaining the noter to find caution in terms of his interlocutor of 14 December 2016. What remains in the Grounds of Appeal are the propositions that in granting the interlocutor of 5 May 2017 the Lord Ordinary (Lady Wolffe) erred: (1) in law, by

concluding that the ATE policy was insufficient to provide an adequate alternative to a bond of caution in terms of RCS 33.4(2); (2) in law, and separately in an exercise of her discretion, in holding that the deed of indemnity (no 48. of process) was insufficient to constitute a bond of caution and therefore to comply with Lord Doherty's interlocutor of 14 December 2016; and (3) by dismissing (*sic*) the claim.

[59] The noter having been ordained "to find caution", the framework for Lady Wolffe's decision-making was provided by RCS 33. By interlocutors of 15 February 2017 and 5 April 2017 and in exercise of her powers under RCS 33.2 and 33.3, she specified the period within which caution was to be found and then varied that period. As varied, the period came to an end on 3 May 2017. RCS 33.4(1)(a) provides that a person ordered to find caution shall do so by obtaining a bond of caution. For this purpose a bond of caution is defined by RCS 33.6 as an obligation on the cautioner, his heirs and executors, to make payment of the sums for which he has become cautioner to the party to whom he is bound, as validly and in the same manner as the party and his heirs and successors. However, RCS 33.4(2) provides that the court may approve a method of security other than a bond of caution or consignation. Equally, in terms of RCS 33.7(2), a party who is dissatisfied with the sufficiency or form of the caution or other security offered in obedience to an order of the court may apply by motion for an order under RCS 33.10. In terms of RCS 33.10 where a pursuer fails to find caution or give other security (thereby becoming the "party in default") the other party may apply by motion for decree of absolvitor.

[60] On 5 May 2017 Lady Wolffe had before her applications in terms of RCS 33.4(2) to approve a method of security other than a bond of caution, and an application for absolvitor because the noter was in default by reason of its failure to provide a bond of caution within the specified time.

[61] I agree with your Ladyship in the chair that when exercising the RCS 33.4(2) jurisdiction it is only logical for the court to require that any proffered alternative provides at least the same degree of security as a bond of caution. I take your Lordship to share that view. As I would see it, an aspect of that conclusion is that where a deed constituting an obligation is offered as an alternative to a bond of caution it must be in clear and unequivocal terms; its effectiveness as security must be beyond any reasonable argument. I further agree with your Ladyship and your Lordship that the ATE policy did not provide that. Your Lordship is more forgiving of the deficiencies in the deed of indemnity than is your Ladyship but your Ladyship and your Lordship are at one in considering that Lady Wolffe was correct in rejecting the deed as an acceptable equivalent of or alternative to a bond of caution. Again, sharing the opinion of your Ladyship on the various defects of the deed, I respectfully agree.

[62] Lady Wolffe was accordingly right to conclude that as at 5 May 2017 the noter had not lodged a bond of caution or any acceptable alternative despite her having initially ordered on 15 February 2017 that a bond be lodged by 15 March 2017. That latter date had been extended to 3 May 2017 after Lady Wolffe had indicated, at the continued hearing on 5 April 2017, that she did not consider the proffered ATE policy to meet the requirements of RCS 33.4. On that occasion she stressed that this was "the last indulgence to be afforded to the noter".

[63] That Lady Wolffe did not err in her assessment of the ATE policy or in her assessment of the deed of indemnity disposes of grounds of appeal (1) and (2). That leaves ground of appeal (3), that she erred by "dismissing the claim", but the way in which ground of appeal (3) is framed makes it clear that it is dependent on the success of one or other or both of grounds (1) and (2). Mr Smith did not suggest otherwise. Moreover, as Lady Wolffe

records at para [62] of her Note, counsel for the respondents had observed that a failure to obtain caution entitled the counterparty to decree of absolvitor in ordinary proceedings or, as here, to refusal of the prayer: RCS 33.10. Counsel for the noter (Mr McIlvride QC) had not contradicted the correctness of that proposition. Accordingly, whether or not Lady Wolffe was indeed bound by the terms of RCS 33.10 to grant absolvitor on finding the noter to be in default, as opposed to having a discretion in the matter, she can hardly be criticised for having proceeded as she did, given the position taken by the noter's counsel. Thus, on none of the matters which are directly challenged in the Grounds of Appeal do I see Lady Wolffe to have been in error.

[64] A decision made by Lady Wolffe on 5 May 2017 was to refuse Mr McIlvride's request for further time. She explains her reasoning for so deciding at paragraph [62] of her Note:

> "In the course of the hearing on 5 May 2017, Mr McIlvride made a motion at the bar for further time. His stated intention was to have the Deed of Indemnity signed. In the exercise of my discretion, and having regard to the procedure since the December interlocutor, I refused that motion. The noter and its agents had had a total of some 5 months within which to comply with the December interlocutor. They had been endeavouring to obtain a bond of caution since about mid-March. As the stated purpose of being granted further time was to have the proffered Deed of Indemnity signed, and given the stance of the respondents as stated to the court through their Senior Counsel, there was no prospect that the Deed could be signed by all parties. Even if it were, the non-justiciability in this court of its import precluded satisfaction of the suspensive condition in clause 2. There would be no utility in granting further time for the purpose Mr McIlvride identified. At the hearing on 5 April, having secured on that occasion a further four weeks, Mr McIlvride had accepted that that would be the final indulgence the noter could expect from the court."

[65] I did not understand Mr Smith directly to attack the decision to refuse further time. Indeed, he was critical of Mr McIlvride for asking for further time rather than presenting an argument in support of the sufficiency of the deed of indemnity. Your Lordship, on the

other hand, while expressing sympathy with the position in which Lady Wolffe found herself, considers her to have been wrong to have refused the noter "a further opportunity to deal with the problem". Your Lordship sets out reasons why he considers that Lady Wolffe was led into error: she mistakenly accepted the submission that clause 2 of the deed of indemnity suspended the effect of clause 3; she mistakenly thought the deed of indemnity was beyond repair, it did not occur to her to allow time either for the respondents to consider whether they would sign the deed of indemnity or, if they would not, for the noter to have the deed redrafted and thereby obviate the apparent need for signature; she was frustrated by the time that the noter had taken to get even to the stage of producing the deed in the (very imperfect) form in which it was produced; a month before she had allowed the noter "the last indulgence to be afforded", by 5 May 2017 her patience had run out.

[66] I shall have to return to your Lordship's conclusion that Lady Wolffe can be regarded as having fallen into error but first I note the points made by your Lordship under the heading "General considerations": (1) the provisions in the Rules of Court for caution or other security are designed to ensure that a successful party will recover his taxed judicial expenses from an opponent of doubtful solvency; (2) an order for caution is not designed to stifle litigation although it can have that effect; (3) the role of the court is not to punish a party in default where there is delay in finding caution; (4) the court must act proportionately and therefore should be slow to take a step which results in decree of absolvitor simply because of a failure to provide security; (5) on available information it may be supposed that finding security for £100,000 cannot be easy; (6) there had been delay in the present case but nevertheless it was to be borne in mind that what was in issue was a period of no more than five months; (7) inadequate as the deed of indemnity may have been, it was apparent from its appearance that Elite were willing to provide security; (8) there was no

indication of prejudice to the respondents whereas with absolvitor the noter would irredeemably lose what might be a substantial claim.

[67] Your Lordship makes a strong argument. It becomes the more attractive once Mr Smith is able to hold out the prospect of a new deed of indemnity signed on 14 and 22 June 2017 and free from the defects of its predecessor. But your Lordship's argument was not made to Lady Wolffe. Moreover, she was not presented with the new deed of indemnity or even with the prospect of a new deed of indemnity. Rather, what she had before her was a document which fully deserved her description of it as "ineptly drafted …slapdash and shoddy" (Note, para [41]). The only purpose put forward by Mr McIlvride for a further period of time being allowed was to have that document signed. Critical as I am of the original deed of indemnity being governed by English law and subject to the jurisdiction of the English courts, Lady Wolffe may have gone too far in considering that "the non-justiciability in this court of its import precluded satisfaction of the suspensive condition in clause 2". However I do not see that that matters. The deed was on any view ineptly drafted. It was not a bond of caution. It was not the equivalent of a bond of caution. As the matter was presented to her, Lady Wolffe was simply correct when she said that there was no utility in granting further time for the purpose Mr McIlvride identified. I do not consider her to have made any material error.

[68] It follows that I do not see how this reclaiming motion can properly be allowed.

SECOND DIVISION, INNER HOUSE, COURT OF SESSION

[2018] CSIH 27
P194/16

Lord Justice Clerk
Lord Brodie
Lord Glennie

OPINION OF LORD GLENNIE

in the reclaiming motion

by

CENTENARY 6 LIMITED

Noter and Reclaimer

against

ROBERT CAVEN and KEVIN MAWER

Respondents

in the liquidation of Centenary Holdings III Limited (in liquidation)

Noter and Reclaimer: Smith QC; Smart, TLT LLP
Respondents: Borland QC; CMS Cameron McKenna Nabarro Olswang LLP

10 April 2018

Introduction – the underlying litigation

[69] The following summary of the claim in this litigation is taken from the Note by Centenary 6 Limited ("the Noter") in the liquidation of Centenary Holdings III Limited ("the Company"). It should not be assumed that it is uncontentious.

[70] The Company was originally incorporated under the name Seagram Distillers plc. In 2002 it became part of the Vivendi group of companies. By about 2003 it had ceased trading.

A petition was presented for its winding up by its sole director. At that time, so it is alleged, the Company had significant assets (in excess of £1 billion) as well as significant liabilities in the form of various leases.

[71] On 9 June 2005 an order was made for the appointment of a provisional liquidator. On 28 August 2005, at a meeting of creditors, Robert Caven and Kevin Mawer ("the respondents") were appointed joint liquidators. (In September 2008 Mr Mawer obtained his release as liquidator and was replaced in that role by another insolvency practitioner, but that is not material for present purposes since it occurred after the events with which this action is concerned.)

[72] The Noter is the sole shareholder in and contributory of the Company. By its Note in the liquidation the Noter seeks an order against the respondents, jointly and severally, in terms of section 212(3) of the Insolvency Act 1986, for payment of the sum of £22,324,980.56 with interest thereon as a contribution to the assets of the Company in liquidation.

[73] In support of that claim, the Noter avers that at the time the winding up commenced the Company was the tenant under two leases of the heritable property in Talgarth Road, Hammersmith, London, known as "The Ark". The leases were dated December 1995 and February 1996 and each was for a term of 25 years. In both cases, the landlord's interest was vested in Deka Immobilien Investment GmbH ("Deka"). The leases contained break clauses providing for an option to break the lease after 15 years in one case and 20 years in the other. The Company was potentially liable for rent under the leases in the sum of £4,550,000 per annum from the date of the appointment of the respondents as joint liquidators in 2005 until the earliest dates on which the Company could exercise the break options under the leases. In addition, the Company was potentially liable to Deka until those dates in respect of matters such as service charges and other payments due under the leases.

[74] Deka submitted a claim in the liquidation of the Company in the sum of approximately £38 million, comprising: (i) arrears of rent and service charges together with interest (£3,116,511.57); (ii) dilapidations (£1,407,845.23); and (iii) future rent, service charges and interest for the periods until the break options could be exercised (£33,761,914.00).

[75] In about November 2005 the respondents entered into an arrangement with Deka whereby, in consideration of Deka accepting a renunciation of the leases by the Company, Deka would be entitled to rank in the liquidation on the basis of its claim against the Company being valued in an amount of no less than £28 million (the precise figure depending on a number of details to be worked out in due course).

[76] It is argued by the Noter that, in compromising Deka's claim in the sum of around £28 million, the respondents acted in breach of their duties to the Company and failed to exercise the skill and care reasonably to be expected of ordinarily competent liquidators. The argument is advanced on two separate grounds. First, it is said that at the time the leases were terminated the sums due to Deka, including advance rent then due, only amounted to around £4,500,000. Having given up possession of the Ark, no ordinarily competent liquidator exercising reasonable skill and care would have entered into a compromise agreement with Deka in terms of which Deka's claim in the liquidation would be valued at around £25 million more than the sums actually due to them at that time, irrespective of whether or not Deka was able to sell the Ark or find a replacement tenant in the period of five years or more until the break options could have been exercised. Second, the Noter argues that no ordinarily competent liquidator exercising reasonable skill and care would have entered into a compromise agreement on those terms without insisting that the agreement included an "anti-embarrassment" clause, in terms of which Deka's claim in the liquidation would be reduced if the potential losses under the two leases were to be

extinguished or mitigated, for example if (in consequence of the surrender of the leases) Deka was to sell the Ark with vacant possession. In the event, so it is said, in March 2006, shortly after they agreed the surrender of the two leases, Deka did sell the Ark with vacant possession for around £47 million, securing for itself what the Noter describes as "a sizeable windfall".

[77] In 2009 the then liquidators of the Company commenced an action in the High Court in England against a number of defendants including Vivendi SA. That action was settled in September 2010 by the defendants making payment to the Company of around £47 million. As a result, in or around December 2010 creditors of the Company whose claims in the liquidation had been accepted by the respondents were paid in full. The dividend paid to Deka amounted to £28,995,293.03. The Noter contends that, but for the agreement reached by the respondents with Deka in December 2005, the dividend due to Deka would have amounted to a much smaller sum, in the region of £6,670,312.47 plus interest. On that basis the Noter contends that, but for the failures of the respondents, the assets of the Company would have been increased to the extent of something over £22 million; and funds would have been available in the liquidation for distribution to the contributories of the Company, including the Noter.

[78] There are, perhaps, two points of importance to make about this claim at this stage. The first is that, having regard to the Noter's averments and to the terms of an expert report (albeit provisional) lodged by the Noter in support, the Noter appears to have a clearly arguable case on the merits. This was the view expressed by Lord Doherty in his Note explaining why he ordered the Noter to find caution. Before Lord Doherty it was not argued on behalf of the respondents that the Noter's claim was bound to fail. Nor was any such argument advanced before us. Having said that, there is also, as Lord Doherty

observed, a clearly arguable defence. The important point for present purposes is that this is not a case where, for aught known at present, the Noter's claim can be treated as anything other than genuine and clearly arguable. It is a substantial claim which merits a decision by the court unless it is resolved in some other way. The second point, and the relevance of this will appear below, is that the dispute will be resolved largely on evidence from the respondents together with expert evidence on both sides. It is unlikely to be a case in which any officer of the Noter will give much (if any) evidence, and it does not appear likely that the case will turn on issues of credibility relating to any such witnesses.

The order for caution

[79] On 14 December 2016, on the motion of the respondents made under section 726(2) of the Companies Act 1985 ("the 1985 Act"), Lord Doherty ordered the Noter to find caution (security) for the respondents' expenses (costs) in the sum of £100,000, and sisted (stayed) the proceedings until caution was found. He was satisfied, in terms of that section, by "credible testimony" that there was reason to believe that the Noter would be unable to pay the respondents' expenses if they were successful in their defence. Lord Doherty did not fix a date by which the caution was to be found. There is now no appeal against that order.

Orders for caution (generally)

[80] !t is often overlooked that the rules of court are prescriptive as to what should happen when a person is ordered to find caution. Rule 33.4(1)(a) provides that a person ordered to find caution "shall do so by obtaining a bond of caution". Such a bond must be lodged in process accompanied by a copy thereof: rule 33.4(3) and (5). Provision is made in rules 33.5 – 33.7 as to the requirements in relation to such a bond. Rule 33.6(1) provides that:

> "A bond of caution shall oblige the cautioner, his heirs and executors to make payment of the sums for which he has become cautioner to the party to whom he is bound, as validly and in the same manner as the party and his heirs and successors, for whom he is cautioner, are obliged."

In terms of rule 33.5, "a bond of caution … shall be given only by a person authorised to carry on a regulated activity under section 31 of the Financial Services and Markets Act 2000". Rule 33.7(1) requires the Deputy Principal Clerk to satisfy himself that any bond of caution lodged in process under rule 33.4(3) is in proper form.

[81] Rule 33.7(2) provides for what may happen in the event that caution is not put up in the required amount or in the proper form. A party who is dissatisfied with the sufficiency or form of the caution or other security offered in obedience to an order of the court may apply by motion for an order under rule 33.10 for decree of absolvitor (where the party in default is a pursuer) or decree by default or such other order as the court thinks fit (where the party in default is a defender or a third party). The fact that the appropriate disposal is one of absolvitor where the pursuer is the party in default is of some importance. Had the appropriate disposal been one of dismissal of the action, a pursuer whose action had been dismissed for failure to find caution within the time stipulated in the order could in principal (subject to any relevant time bar) start a new action, though no doubt constrained by an order in that new action to provide caution and, possibly, constrained also by an order requiring him to pay the expenses of the first action as a precondition for continuing with the second. By contrast, decree of absolvitor is *res judicata* between the parties. Where the decree is one of absolvitor, the pursuer has no further rights in respect of the relevant claim. He cannot bring a new action or, if he does, that new action will be met conclusively by a plea of *res judicata* based upon the decree of absolvitor. In the present case the Noter is in the

position of a pursuer, and the equivalent of decree of absolvitor is refusal of the prayer of the Note.

[82] The court has power under rule 33.4(2) to approve a method of security other than by finding caution. Such alternative methods of security may include a combination of two or more methods. It is not uncommon for security to be put up in some other form, such as a solicitor's undertaking, a parent company guarantee or a bond from some third-party guarantor such as an insurance company. But the availability of alternative security in any particular form will seldom be known at the time the initial order for caution is granted, since the party against whom caution is sought will often not know whether he will be ordered to find it; and he will often not have explored the different ways in which he might be able to comply if his opposition to the motion is unsuccessful. To cater for that situation, and to avoid the need for subsequent court appearances seeking approval of one or other alternative method of providing security, the court exercising its powers to order caution under section 726(2) or at common law will sometimes order a defender to provide security in whatever sum is fixed "in a manner to the reasonable satisfaction of the pursuer", with liberty to apply to the court in the event of a dispute as to the acceptability of the security offered. This is both practical and expedient. But it is important to note that, in the unlikely event of the initial order for security specifically approving a particular method of alternative security in terms of rule 33.4(2), then, unless an order is made in some such form as that indicated above, the party ordered to find caution will be required to obtain a bond of caution, have it approved by the Deputy Principal Clerk and lodge it in process, all by the time specified in the order.

[83] I should make one further point. As noted above, rule 33.6(1) provides that a bond of caution shall oblige the cautioner to make payment of the sums for which he has become

cautioner "as validly and in the same manner" as the party for whom he is cautioner. In *Monarch Energy Ltd* v *Powergen Retail Ltd* 2006 SLT 743 at para [11], Lord Drummond Young treated this as an indication, consistent with his analysis of caution involving a secondary obligation coextensive with the primary obligation of the principal debtor, that any bond of caution or other security permitted under rule 33.4(2) "must provide the defender with a guarantee of its expenses, rather than merely a degree of comfort": see also at para [31]. I agree with that sentiment. That does not mean that the alternative security must be in the form of a guarantee or some precise equivalent. In the *Monarch Energy* case Lord Drummond Young at para [25] explained how a number of restrictions and qualifications on an insurer's liability under an After the Event ("ATE") insurance policy could be overcome, and the policy treated as an acceptable security, by means of a protocol which depended for its effectiveness on adequate communication from the pursuer's agents to the defender about matters which might give rise to the possibility of insurers avoiding liability – in fact for other reasons, discussed at para [26] onwards, the ATE policy was not acceptable, but this does not affect this particular point. Nonetheless, the security offered must in practical terms be such as to satisfy the defender or, in the absence of agreement, the court that an order for expenses in favour of the defender <u>will</u> be met. This point is of importance in the context of various attempts to provide security in the present case.

Subsequent hearings and orders in this case

[84] The original order in this case was an order for caution. In terms of rule 33.4(1)(a), that required the Noter to obtain and lodge a bond of caution. The order did not in terms allow for security to be provided otherwise than by obtaining a bond of caution, though that did not preclude an application being made subsequently by the Noter under rule 33.4(2) for

the court to approve some other method of security. Nor did it specify a time within which the caution was to be provided.

Initial failure to find caution

[85] On 11 January 2016, four weeks after the order requiring the Noter to find caution, agents for the respondents wrote to agents for the Noter asking them to confirm, by return, whether the Noter intended to lodge caution and, if so, when. They said they were taking instructions on whether to move for decree of absolvitor. The response from the Noter's agents the next day was to the effect that they would liaise with the Noter (who was based in Australia) "and come back to you with the estimated delivery date of the caution to be lodged". On 23 January 2016 agents for the respondents wrote to say that they had not heard anything further. The following day, 24 January 2017, agents for the Noter responded and advised that "the Noter is in the process of securing the full amount of caution required". They said that discussions were ongoing with third-party legal insurers to that end and they expected such discussions to conclude shortly, "resulting in the lodging of the required amount". On 25 January 2017 agents for the respondents pointed out that the Noter had already had six weeks to lodge caution in accordance with the order of the court and stated that "if caution is not lodged in seven working days (by 3 February 2017) we will advise our clients to enrol for decree of absolvitor". On 2 February 2017, the day before expiry of that deadline, agents for the Noter sent an email to agents for the respondents, the relevant part of which reads as follows:

> "As previously advised, we have been liaising with a major third party legal insurer since the caution order was granted. That has been a fairly lengthy and detailed ongoing process of due diligence by the prospective insurer, in conjunction with and involving back and forward with their Senior Barristers. We expect the matter to conclude and for a decision to be issued within 14 to 28 days. Beyond that, what we can say is that having gone through the process to date, the insurer is perfectly

> happy with the merits of the case, including the prescriptive element involved and have no issue in providing the insurance for the caution in regard to those aspects.
>
> We will of course update you as soon as the process has ended, but at this stage we are hopeful of concluding the matter within the timescale suggested and with a positive outcome for our client. It is of course the case that the amount of caution being a six figure sum is not a figure which can be readily sourced and correspondingly, the legal insurer requires to be sure of its ground before committing to its position as third party insurer."

Quite apart from the question of timing, which was the main focus of the correspondence, there was no suggestion at all by the Noter that it proposed to comply with the order other than by lodging a bond of caution in accordance with rule 33.4(1)(a). It is possible that the Noter was unaware of what the rules required.

Date fixed for finding caution

[86] In February 2017 the respondents enrolled a motion seeking, so far as is relevant, the setting of a date by which caution was to be lodged. That motion came before Lady Wolffe on 15 February 2017. She appointed the Noter to find caution as previously ordered by the court within 28 days from that date, i.e. by 15 March 2017. Nothing was said about any alternative form of security since no question about that had been raised by the Noter.

ATE insurance policy

[87] The Noter did not lodge caution within that time. However, on 14 March 2017 agents for the Noter provided the respondents with a copy of an ATE insurance agreement between the Noter and Elite Insurance Company Limited ("Elite"), with a commencement date of 27 February 2017. At the same time they stated that the ATE policy had been lodged with the court in satisfaction of the order for caution.

Motion for decree of absolvitor – hearings on 29 March and 5 April 2017

[88] On 17 March 2017 the respondents enrolled a motion seeking decree of absolvitor in

terms of rule 33.10(a). In the reasons for the motion, they pointed out that the ATE insurance, which was an agreement between the Noter and its insurer, could be cancelled for any number of reasons without further liability on behalf of the insurer and did not provide sufficient security. That motion came before Lady Wolffe on 29 March 2017. She heard argument as to whether the ATE insurance satisfied the requirements for caution. In addition, representations were made by counsel for the Noter that a bond of caution could be produced within a further 4 or 5 weeks if the ATE insurance was not satisfactory. Lady Wolffe expressed doubts as to the acceptability of the ATE insurance. The hearing was continued until 5 April 2017 and again, to allow the Noter one last opportunity to produce a bond of caution in accordance with rule 33.4, until 5 May 2017.

Deed of Indemnity

[89] On 3 May 2017, only two days before the resumed hearing fixed for 5 May 2017, the Noter's agents produced additional documents, including a copy Deed of Indemnity, bearing to be a Deed between four parties, namely Elite, the Noter, and the respondents (Mr Caven and Mr Mawer) but signed only on behalf of Elite. Another copy had apparently been signed, but in that case only by the Noter. The Deed of Indemnity had not been checked by the Deputy Principal Clerk in terms of rule 33.7(1) since it was unsigned (or at least not signed by all parties to it) and, at that stage, only a copy had been tendered. The Deed gave rise to a number of arguments which are referred to below. One problem, though only one amongst many, was that the Deed bore to be governed by English law, as a result of which senior counsel for the Noter declined to make any submissions as to its import. Instead he relied upon advice in the form of a two-page opinion from a solicitor advocate which, while conceding that the Deed was not in the normal form for a deed of caution, expressed the view that the Deed would suffice and that "the court will in all

likelihood be satisfied that it does constitute adequate security and will not grant Decree of Absolvitor".

Hearing of 5 May 2017 – order refusing the prayer of the Note

[90] After hearing argument both in relation to the ATE policy and the Deed of Indemnity, on 5 May 2017 Lady Wolffe pronounced an interlocutor in which she refused to accept the ATE policy as an alternative form of caution under rule 33.4(2); refused to accept the "bond" (i.e. the Deed of Indemnity) as a suitable form of caution; and, on the basis that the Noter had failed to lodge suitable caution in terms of the court's interlocutors, refused the prayer of the Note in terms of rule 33.10(a) (the equivalent, as noted above, of granting decree of absolvitor).

Reclaiming motion

[91] By this reclaiming motion (appeal) the Noter appeals the decision of Lady Wolffe on 5 May 2017. As originally drafted the Grounds of Appeal included an appeal against Lord Doherty's order for caution made on 14 December 2016. Having seen a note prepared by Lord Doherty explaining the basis of his decision, the Noter intimated that it did not insist on that aspect of the appeal. The Noter does, however, maintain its challenge to the order made by Lady Wolffe on 5 May 2017 refusing the prayer of the Note. In summary it contends that Lady Wolffe ought to have approved the ATE insurance policy as an alternative method of security in terms of rule 33.4(2); which failing, she ought to have accepted the Deed of Indemnity as a bond of caution and/or as an alternative method of security in terms of that same rule.

[92] The respondents contend that both aspects of the interlocutor of 5 May 2017 were correct and that Lady Wolffe was perfectly entitled to refuse the prayer of the Note in the absence of security being put up in any suitable form.

Discussion

[93] I propose to consider the arguments relating to the ATE policy and to the Deed of Indemnity separately before setting out my views as to the proper disposal of this appeal.

The ATE insurance policy

[94] As Lord Drummond Young observed in *Monarch Energy* at para [21], After the Event ("ATE") insurance in respect of the insured's potential liability for the legal costs of the other party to the litigation has become a feature of litigation in this century, particularly south of the border as a result of the effective abolition there of civil legal aid. The extent to which such insurance is used in Scotland is less clear. Certainly there is less guidance to be obtained from the decided cases in Scotland – *Monarch Energy* is the only such case to date – so it is appropriate to look to the English cases for guidance, not on the proper interpretation of our domestic rules relating to caution (or security) for expenses, but on the satisfactory nature or otherwise of ATE insurance as a method of providing security.

[95] In a number of cases in England the question has been considered as to whether an ATE policy of such a kind can be used by a claimant as a means of providing security for the costs of the defendant in compliance with a court order that such security be given: see, for example, *Nasser* v *United Bank of Kuwait* [2001] EWCA Civ at 556 per Mance LJ at para 60, *Al-Koronky and another* v *Time-Life Entertainment Group Limited* [2006] EWCA Civ 1123 per Sedley LJ at paras 35-36, *Belco Trading Co* v *Kondo* [2008] EWCA Civ 205 per Longmore LJ at Paras 3-9, *Michael Phillips Architects Ltd* v *Riklin and another* [2010] BLR 569, *Geophysical*

Service Centre Co v *Dowell Schlumberger (ME) Inc* [2013] EWHC 147 (TCC), 147 Construction LR 240, *Premier Motorauctions Limited* v *PricewaterhouseCoopers LLP* [2017] EWCA Civ 1872 and *Recovery Partners GB Ltd* v *Rukhadze and others* [2018] EWHC 95 (Comm). That has involved a discussion of the terms of such policies and the extent to which they can be said to provide sufficient security. They are entirely consistent with the approach of Lord Drummond Young in *Monarch Energy*. From those cases (transposed to the Scottish context) and from the opinion of Lord Drummond Young in *Monarch Energy* I would extract three pointers to the use which can appropriately be made of ATE policies in this field.

[96] First, there is no reason in principle why the court should not approve ATE insurance as an alternative method of security in terms of rule 33.4(2). This was not in dispute, and all the cases make this clear.

[97] Second, whether a particular policy can be treated as a satisfactory alternative method of security will depend upon the sufficiency of the protection it gives to the defender (or other person entitled to security for his expenses). It must in practical terms be in a form which ensures that the defender will be paid his expenses if he is successful in the litigation. Apart from any question as to the financial standing of the insurer, which is unlikely to be an issue, the terms of the insurance combined with such collateral undertakings as may be given must provide an assurance that the insurers cannot repudiate liability or decline cover in the event that the pursuer fails for whatever reason to make good his claim. It will be necessary in each case to look carefully at the policy terms. The test is a high one – it will be necessary to show that the policy amounts, in practical terms at least, to a guarantee of the defender's expenses. It was noteworthy that Mr Smith QC was unable to point to any case in which an ATE policy had in fact been accepted as a means of providing security for costs/expenses.

[98] Third, quite apart from the question whether the policy can be used as a means of providing alternative security under rule 33.4(2), the existence of an ATE policy may be of relevance at the prior stage, namely when the court is considering the threshold jurisdictional question which, in the case of an application under section 726(2) of the Companies Act 1985, is whether "it appears by credible testimony that there is reason to believe that the company will be unable to pay the defender's expenses if successful in his defence". As is made clear in *Premier Motorauctions*, the ATE insurance is an asset of the pursuer, albeit a contingent one, and may be taken into account in deciding whether the jurisdictional threshold is met. In the present case Lady Wolffe was quite correct to accept, at para [59], that a suitably worded ATE policy might be relevant to the "anterior question" whether the threshold test under section 726(2) of the 1985 Act had been met, but she said that that was "not the question here". No doubt she was correct in saying that, because no one had sought to argue the point. However it should be noted that, as in the case of any interlocutory order, a party may apply to vary or recall an order for caution where there has been a change of circumstances; and there is no reason in principle why, in an appropriate case, having obtained ATE cover in the appropriate terms, a pursuer should not be entitled to make an application under rule 33.4(2) to recall the order for caution in light of that change of circumstances. The success or otherwise of such an application would depend in large part upon the terms of the particular ATE policy. The question at that stage, however, would not be whether the policy satisfied the test for approval as an alternative method of security but whether, notwithstanding the existence of the ATE policy, it still appeared by credible testimony that there was reason to believe that the company would be unable to pay the defender's expenses if successful in his defence (to paraphrase section 726(2) of the 1985 Act).

[99] It is unnecessary to set out the terms of the ATE policy in the present case. It is a lengthy document running to over 20 pages. As Mr Borland QC pointed out, it contains a large number of exclusions and other provisions entitling the insurers to cancel the policy and in some cases to treat it as void *ab initio*. Thus, to identify a few such provisions:

(a) Clause 9 entitles the insurers to treat the policy as void "and as if it never commenced" in the event of the Noter becoming insolvent;

(b) Clause 10 sets out the insurers' rights to cancel the policy "immediately without any further liability for your own disbursements and/or opponent's costs". The circumstances in which this right to cancel arises include: (10.5.1 and 10.5.3) if the insurers' legal representative considers that the claim does not have "prospects of success", an expression which is defined as meaning that the prospects of success are better than even, even if the Noter and/or its legal representatives disagree; and (10.5.2) if the Noter does not follow the advice of its legal representative or the insurers about making or accepting a reasonable offer of settlement.

(c) Clause 5.1.18 lists the circumstances in which the insurance does not cover the opponent's costs. They include costs incurred by the opponent: (5.1.18.2) when, in the opinion of the insurers, the Noter's claim does not have "prospects of success", defined as noted above; (5.1.18.6) where the claim is abandoned or lost or discontinued owing to the Noter's lack of funds; and (5.1.18.14) arising from the Noter's failure and/or delay in providing instructions or failing to cooperate with the insurers, a reference to the various obligations imposed on the Noter under the policy (see in particular section 3 "Keeping us informed during your legal dispute").

It can be seen that these provisions, whether taken separately or together, give the insurers the opportunity in a wide range of circumstances of avoiding liability for some or all of the respondents' expenses. In some cases it might be possible to devise a protocol, such as that discussed in *Monarch Energy* at para [25], which might not prevent the policy being cancelled but would, at least, put the respondents on notice of any risk of that happening. No such protocol was offered in this case. In any event, the right to avoid the policy *ab initio* in the event of the Noter's insolvency must be seen as a real risk in circumstances where the court has already been persuaded that the jurisdictional hurdle for an order for caution has been satisfied.

[100] Lady Wolffe held that the ATE policy was not an adequate alternative method of security. She went into the matter in more detail than I have done. I can find no fault with her review of the ATE policy or her conclusions as to its inadequacy as an alternative method of security.

The Deed of Indemnity

[101] The Deed of Indemnity in the form in which it appeared at the hearing before Lady Wolffe on 5 May 2017 was undated. It bore to be between (1) Elite, (2) the first respondent, Robert Caven, (3) the second respondent, Kevin Mawer and (4) the Noter. In the first paragraph of the preamble it wrongly described the respondents as joint liquidators of the Noter, whereas in fact they were joint liquidators of the Company. It referred to the fact that Elite had issued the ATE insurance policy in respect of the Noter's potential liability for adverse costs arising out of the claim made by the Noter against the respondents, stated that the Noter had been ordered by the court to provide "security for costs" to the respondents in the sum of £100,000 and stated, further, that, in order to meet that liability, "Elite has agreed to indemnify [the respondents] in accordance with the terms of this Deed".

[102] The main (operative) part of the Deed of Indemnity appeared under the heading "Indemnity". I shall set out the relevant parts:

> "2. This Deed shall come into effect provided that: (i) the Claim is not struck out, disallowed or otherwise impeded for any reason related to the Court making an order for security for costs; and (ii) the Court approves this Deed as sufficient security for costs.
>
> 3. Elite hereby unconditionally and irrevocably undertakes to pay to [the respondents] any sum or sums which [the Noter] is held liable to pay in respect of their Costs following Taxation or agreement.
>
> 4. [The respondents] will inform Elite immediately if the Claim is resolved (whether by agreement, judgment, Court order or otherwise) in their favour such that [the Noter] incurs an adverse costs liability.
>
> 5. Elite shall be given opportunity to ensure representations are made on behalf of [the Noter] in respect of Costs including during any Taxation.
>
> 6. Payment will be made by Elite within 10 Business days of receipt by Elite documentary evidence of the outcome of any Taxation or agreement which means Taxation is not required.
>
> 7. Elite's total liability under this Deed shall not exceed £100,000.
>
> 8. Elite shall be deemed to be a Principle Debtor and not merely a surety and, accordingly, Elite shall not be discharged nor shall its liability be affected by any act or thing or means whatsoever (including, without limitation, any defences to payment asserted by, insolvency of, or unenforceability as against [the Noter]).
>
> 9. For the avoidance of doubt and without prejudice to the foregoing, Elite's liability under this Deed shall not be subject to avoidance on the grounds of fraud or misrepresentation by [the Noter], nor shall it be affected by any lack of substance in the Claim.
>
> 10. Upon payment by Elite of any sum under this Deed, [the Noter] shall be liable for an equivalent sum to Elite. This sum shall be payable at the conclusion of the Claim."

There then followed a number of administrative provisions concerning notices, followed by some "General" clauses which need not be set out here. Finally, clause 15 provided as follows:

> "15. This Deed shall be governed by and construed in accordance with English Law and shall be subject to the exclusive jurisdiction of the English Courts."

The Deed went on to state that "IN WITNESS WHEREOF this Deed has been executed as a Deed on the Date set out above" (though no date had been set out above), which wording was followed by spaces for signature by each of the four parties to the Deed. It was in fact signed only by or on behalf of Elite.

[103] Before Lady Wolffe, Mr Borland QC made a number of submissions as to the inadequacy of the Deed of Indemnity. Some of his submissions referred to examples of inept drafting, such as the reference to the respondents as being liquidators of the Noter, and the use of English legal terminology such as "costs". Others bore to be more substantial. For example, he noted that the Deed purported to be a four-party document in which the respondents were required to undertake obligations to Elite and to sign the document. It had not been signed by the respondents and the respondents had no intention of signing it or of undertaking any obligations under it. Further, so he submitted, the conditionality of clause 2 meant that there was no immediately enforceable obligation or undertaking owed by Elite to the respondents; and for this reason the Deed was incapable of satisfying the requirements of a bond of caution. The unconditional undertaking in clause 3 appeared to conflict with the suspensive character of clause 2. He complained about clause 5 which, he argued, required the respondents to grant certain entitlements to Elite about taxation. He submitted that the payment provision in clause 6 was inept in that it contained no specification of what would constitute documentary evidence of the outcome of any taxation or agreement. The term "Principal Debtor" in clause 8 was not defined. Clause 10, which contained a counter indemnity by the Noter to Elite, was of no concern to the respondents. Finally, under reference to clause 15, which conferred exclusive jurisdiction on the English

Courts, he submitted that the English courts had no power to rule on what was the subject matter at hand, namely the sufficiency of the Deed of Indemnity as a bond of caution.

[104] Some of these points were more important than others. The misdescription of the respondents as joint liquidators of the Noter could not have affected the validity of the Deed, particularly since the identity of the parties and the circumstances in which the Deed was given were fully explained in the remainder of the recitals. The submission about the suspensive effect of clause 2 entirely missed the point – that clause simply made it clear that unless and until the Deed of Indemnity was accepted by the court, and the Noter's claim was allowed to continue with that security in place, then the obligations of Elite under the Deed would not come into force. That is entirely natural and what one would expect. Clause 5 did not impose any obligation on the respondents; rather it provided a qualification on the obligation to pay out under the Deed. There could be no genuine uncertainty about the meaning of the words "evidence of the outcome" in clause 6, nor about the expression "Principal Debtor" in clause 8. Further, the effect of clause 15 was simply to make the Deed itself subject to English law and jurisdiction; it clearly did not purport to confer on the English court any jurisdiction to rule on the question as to whether the Deed of Indemnity was adequate to meet the requirements of an order for caution pronounced by the Scottish court.

[105] The point of substance, and the only real point of substance in my view, concerned the fact that the Deed purported to be between four parties, namely Elite, the Noter and the two respondents. Further, it appeared to require the signatures of all four parties. I agree with Mr Borland that this was both unnecessary and inept. In making an order for a pursuer (or in this case the Noter) to find caution under section 726(2) of the Companies Act 1985, the court cannot compel any other party to the litigation to enter into commitments of

its own. A Deed of Indemnity offered as an alternative form of security in terms of rule 33.4(2) should not be in a form which requires the signature of the other parties to the litigation. To that extent, as I have said, the Deed of Indemnity proffered in this case was inept.

[106] In the course of the reclaiming motion Mr Smith QC, who did not appear in the courts below, sought to persuade us that the Deed of Indemnity, in the form in which it was presented to the court for the hearing of 5 May 2017, was valid and effective and took effect as an undertaking by Elite in terms of clause 3. His submission was that that clause, under which Elite unconditionally and irrevocably undertook to pay the respondents any sum or sums for which the Noter was held liable in respect of their costs, could be plucked out from the body of the document and given effect regardless of the enforceability or otherwise of the other provisions. I do not accept this submission. Clause 3 is part of a package of provisions which have to be read as a whole. It is qualified by reference to Elite's total liability not to exceed £100,000 (clause 7). It is qualified by the obligation on the Noter, in clause 10, to reimburse Elite for any sums payable under the Deed. Other provisions similarly impinge on or affect Elite's obligations under the Deed. It is, in my opinion, clear that the Deed has to be read as a whole. It is not possible to say that it can take effect as a unilateral obligation by Elite in terms of clause 3 only.

[107] However, it is important to look at substance as well as form and, ultimately, to ask whether a defect of this sort justified decree of absolvitor or, as in this case, refusal of the prayer of the Note.

[108] One question to ask is whether as a matter of substance the Deed of Indemnity did seek to impose any obligations on the respondents. In my view it did not. Clause 4 simply required them to inform Elite immediately if the claim was resolved in their favour in such a

way that the Noter incurred an adverse costs liability. But that is what they would do anyway, since the obligation of Elite under the Deed to pay an adverse costs award would have to be triggered by a demand in some form or other by the respondents. In so far as there was some concern that they would have to inform Elite “immediately” on the Noter incurring an adverse costs liability, at worst this might operate as a brake on Elite’s liability (on the reasonableness of which the court might be asked to adjudicate); but it certainly did not impose any obligation on the respondents. The same point could be made about clause 5 – it imposed no substantive obligations on the respondents.

[109] It follows, in my opinion, that the Deed of Indemnity, though appearing to require signatures from the respondents, did not impose on them any substantive obligations capable of affecting their right to claim under the Deed in the event of an award of expenses in their favour. Although the Deed should not have required their signatures, it would not have prejudiced them to sign. In those circumstances, the proper response on being presented with a Deed of this sort would have been either to agree to sign it, knowing that signing it did not hurt them, or to require that it be redrafted so as to take effect without their signatures. Simply to state that they had no intention of counter-signing the Deed or undertaking any obligations to the Noter was, in my view, obstructive and something to which the court should not have given weight. If it was only a matter of form, there was no good reason not to sign. If it was perceived to be a matter of substance, the Deed could readily have been redrafted to avoid this problem.

[110] As I have already noted, Lady Wolffe was not favoured with any submissions from senior counsel for the Noter as to the effect of the Deed. This was, apparently, because it was stated to be governed by English law. That was unfortunate. It would have been helpful to the court if he had provided some assistance. As it was, Lady Wolffe was

presented with submissions only from the respondents, and those submissions were not contradicted at all on behalf of the Noter. In the circumstances it is not surprising that she accepted all those submissions, good, bad and indifferent (see para [60]). Absent any contradictor, she cannot be criticised for reaching this view. Nonetheless, in many respects she was wrong. In particular, she was wrong to regard clause 2 as in some way making the whole Deed unacceptably conditional or suspensive; and she was wrong to accept the submission that clause 15, stipulating that the Deed of Indemnity was governed by English law and subject to the jurisdiction of the English courts, was "inimical to resolution of the very issue the Noter was asking this court to consider [namely] whether the Deed of Indemnity was sufficient for the purpose of rule 33.4".

[111] In dealing with the submission that the Deed of Indemnity was ineffectual so long as it remained unsigned by all four parties, a position which she noted "will not change, given the respondents' stance" (see para [61]), Lady Wolffe refused a motion made by counsel for the Noter at the bar during the course of the hearing for further time within which to have the Deed of Indemnity signed. She took the view that the Noter had had a total of some five months within which to comply with the order for caution made in December 2016 and had been endeavouring to obtain a bond of caution since about mid-March. Since there was no prospect that the Deed would be signed by all four parties, it would have been pointless to give further time within which to try to make this happen. But she added, presumably under reference to the English law provision in clause 15, that even if there were a prospect of it being signed by all parties, "the non-justiciability in this court of its import precluded satisfaction of the suspensive condition in clause 2". There would therefore have been no utility in granting further time for the purpose identified.

[112] I have great sympathy with the position in which the Lord Ordinary found herself, but I consider that she was wrong to have refused to grant the Noter a further opportunity to deal with the problem. In so far as she thought that the problem stemmed, at least in part, from the terms of clause 2, I have already explained why I consider that she was in error. In so far as she was influenced by the fact that the respondents were refusing to sign the Deed, she should have allowed an opportunity for them to reconsider their position or, if they did not, for the Noter to have the Deed redrafted so that it did not require their signatures. I appreciate that she was not asked to do this in terms – it was not suggested that the Deed should be re-drafted so that the respondents did not need to sign – but nonetheless in my view this is what she ought to have done. Reading the relevant passages in her Note setting out the sequence of events, the arguments and her decision, it is impossible not to form the view that she was influenced by the very many points of attack on the Deed made by Mr Borland QC, all of which she accepted in their entirety. She appears to have considered that the Deed was beyond repair. She was also clearly frustrated by the time which the Noter had taken to get even to the stage of producing the Deed in the form in which it was produced. She had already on 5 April 2017 given the Noter what she described in para [32] as "the last indulgence to be afforded [it]"; and by the time of the hearing of 5 May 2017 her patience had clearly run out. This was understandable but, in my opinion, led her into error.

General considerations

[113] It is often observed that rules of court are designed to regulate litigation, to assist both parties and the court in arriving at a just conclusion in accordance with the law and as expeditiously as is reasonable in all the circumstances: see, for example, *Semple Cochrane plc* v *Hughes* 2001 SLT 1121 per Lord Carloway at para 10, *Barry and Susan Peart* v *Promontoria*

(Henrico) Limited [2018] CSIH 1 at para [13]. They are designed to facilitate the resolution of disputes, not to prevent such a resolution. Putting the matter very broadly, the provisions for caution and/or security both in section 726(2) of the Companies Act 1985 and in Chapter 33 of the Rules of Court are designed to ensure that a person in the position of a defender should not be exposed to the expenses of litigation without some confidence that his legal expenses will be met by the opposite party in the event that he is successful. An order for caution is not designed to stifle litigation, though in some circumstances where security cannot be given it may have this effect. Where there has been delay in finding caution, it is not the role of the court to mete out punishment to the party in default. Delay may, of course, cause prejudice to the other party; but subject to any such prejudice to the other party that may be caused by delay, the court should be slow to dismiss a claim simply because the pursuer has delayed in providing security when ordered to do so – and it must be borne in mind, as noted above, that the relevant sanction here is not dismissal but absolvitor. The court must act proportionately.

[114] In the present case the Noter has a claim for a sum in excess of £20 million which is accepted to be arguable. It has been ordered to provide caution for the respondents' expenses of the litigation and has been slow in doing so. But there is nothing to suggest that that delay has been deliberate. Finding security for £100,000 cannot be easy (as is noted in the email exchanges quoted above). There has been considerable delay, and more than one failed attempt. But by the time the Lord Ordinary ran out of patience and refused the prayer of the Note on 5 May 2017, the delay measured only some five months from the date of the original order. Further, by that time it was clear that Elite, who had provided the ATE policy, was prepared to go further and provide a Deed of Indemnity which amounted to an unconditional obligation to pay expenses awarded to the respondents in the litigation. The

Deed as tendered was inadequate in its drafting, but the willingness of Elite to provide a suitable Deed was by then clear and obvious. There has been no suggestion of any particular prejudice to the respondents caused by that delay of five months. If one sets against that the prejudice to the Noter in losing the opportunity of pursuing a very substantial claim, it is clear, in my opinion, that the Lord Ordinary should not there and then have pronounced an order refusing the prayer of the Note, but should have allowed the Noter a further opportunity of getting the drafting right and providing security in a manner acceptable to the court, thereby enabling the Noter to pursue its claim.

[115] In the course of the hearing our attention was drawn to a further version of the Deed of Indemnity redrafted as a Deed between Elite and the Noter and signed on behalf of both parties in June 2017, some six weeks after the hearing before Lady Wolffe. This Deed did not require any signature by the respondents and the drafting was considerably improved. It was governed by Scots law and subject to the exclusive jurisdiction of the Scottish Courts. Mr Smith QC did not ask the court to approve this version of the Deed under rule 33.4(2). His position was that it was only relevant if he could persuade the court that the Deed considered by Lady Wolffe was valid and enforceable – in which case the new version of the Deed, which was clearly better, could be given instead. I am not sure that that is the right approach. The new version of the Deed can serve as an illustration of what might have been achieved had the Lord Ordinary allowed the Noter further time.

[116] In the course of his argument I asked Mr Borland QC whether he had any observations as to the terms of this new version of the Deed and, in particular, whether there was anything in it which might render it unsuitable as a means of providing security. He responded, understandably, that he had not taken instructions on it since there was no application for that version of the Deed to be considered by this court, but he himself saw

nothing which rendered it unsuitable. I would not wish to hold him to that answer. However, having looked at the Deed myself, and in light of Mr Borland's candid response, it seems to me that that Deed would in fact probably provide adequate security in a form which could be approved by the court in terms of rule 33.4(2).

Disposal

[117] I would move your Ladyship and your Lordship to allow this reclaiming motion and set aside the interlocutor of the Lord Ordinary dated 5 May 2017. It would then be open to the parties to agree, if they can, that the new version of the Deed be accepted as satisfying the interlocutor requiring the Noter to find caution; or, if they cannot reach agreement on this matter, it would be open to either party to make the appropriate motion to the court in terms of Chapter 33 of the Rules of Court. However, I would only proceed in this way on the basis that the Noter pays the respondents' expenses of process for the period from 29 March until today on an agent and client, client paying basis; and I would make payment by the Noter of such expenses as taxed or otherwise agreed a condition of further progress in the action after the date of taxation or agreement.

Postcript

[118] Since writing this Opinion I have had the opportunity of reading in draft the Opinions to be issued by your Ladyship in the chair and by your Lordship, Lord Brodie. I note that both your Ladyship and your Lordship take a different view to that which I propose, and the reclaiming motion must therefore be refused.

[119] However, I cannot leave the matter without commenting briefly upon a point made (albeit tentatively) in paragraphs 33-35 of Your Ladyship's Opinion, to the effect that the terms of section 726(2) of the 1985 Act are "addressed to the provision of caution specifically,

and not to the provision of 'security' more generally"; so that "where the statutory test is met, and the court is satisfied that security should be ordered, the statute provides that the security which will be ordered will take the form of caution, not some other, perhaps lesser, form of security that may be offered"; and, in such a case, it may not be open for the court to approve some alternative form of security under rule 33.4(2).

[120] Your Ladyship's analysis depends on reading the terms of section 726(2) of the 1985 Act as limiting the manner in which security for costs or expenses, if ordered against a company on the grounds set out in the sub-section, may be provided. But I wonder whether this is reading too much into the use of the expression "find caution" in that sub-section. As your Ladyship notes, until 1985 the companies legislation for the United Kingdom (viz. section 447 of the Companies Act 1948 and, before that, section 278 of the Companies (Consolidation) Act 1908) contained a single provision applicable both to England and Wales and to Scotland to the effect that:

> "Where a limited company is plaintiff or pursuer in any action or other legal proceeding, any judge having jurisdiction in the matter may, if it appears by credible testimony that there is reason to believe that the company will be unable to pay the costs of the defendant if successful in his defence, require sufficient security to be given for those costs, and may stay all proceedings until the security is given."

Apart from mention of the company being "plaintiff or pursuer", the language of the section was entirely English ("costs", "defendant", "sufficient security … for those costs", "may stay all proceedings"). The effect of section 726(2) of the 1985 Act was, on one view, simply to translate the provision into Scots legal terminology ("defender", "expenses", "caution", "sist") insofar as the provision applied to Scotland, without making any substantive changes to the requirements imposed by the provision. After all, although the term "caution" usually bears the more precise meaning explained in Bell (*Dictionary* (7th edn), p 151 and

Principles, para 245), it is sometimes used in this context simply as the Scots word for security, being derived from the expression "cautio" in Roman law: see per Lord Hope in *Anderson* v *Shetland Islands Council* [2012] UKSC 7 at para 11. In support of the notion that the change as regards Scotland was intended only as a change in terminology, it is difficult, to my mind, to conceive of why Parliament in 1985 should have intended a substantive change in the law, restricting the way in which a company in Scottish proceedings could give security for costs (as it had been called in the legislation up to that point) and requiring it to find caution in the sense described by Bell. In particular, if a substantive change was intended, this would preclude consignation which, although now little used, surely provides even greater security for a defender than a bond of caution. If, as I am presently inclined to think is the case, the change was simply one of terminology, then there would be no impediment to a company ordered to find caution under section 726(2), and therefore prima facie being required to obtain a bond of caution under rule 33.4(1)(a), asking the court to approve some other method of security under rule 33.4(2). However, like your Ladyship, I have not formed a concluded view on the matter; the point was not argued before us and does not affect the outcome of this appeal; and, in a case where it is or might be of critical importance, the point might benefit from further research.

[121] Having said that, I suspect that, even if the effect of an order under section 726(2) of the 1985 Act is to preclude any form of security other than caution in terms of which the cautioner binds himself as surety for the pursuer, that will not cause great inconvenience. On that hypothesis, caution would have to be provided by obtaining and lodging a bond of caution. However, subject to the requirements of rule 33.6, which follows a well-established definition of caution, and to certain requirements in the case of the cautioner being an insurance company, there are no prescribed forms of such a bond. Though it is difficult to

see how an ATE insurance policy would work in this context, there is no reason to think that a properly drafted Deed of Indemnity of the type attempted in the present case would not suffice.