IN THE MATTER OF BOSCOLO LIMITED [2025] EWCA Civ 906:

TO WHOM DO INSURANCE PROCEEDS BELONG?

Professional indemnity *insurance* benefits insureds and those who may claim against them.[1] The essential purpose of *compulsion* on professionals to insure is consumer protection (more narrowly, the protection of those who use the services of professionals).[2]

The consumer protection is not absolute. For example, although many regulators require professionals to insure not only to a minimum level but also to a level adequate to the particular practice, a practice may turn out to be under-insured. The Court of Appeal has just handed down a decision which shows another hole in the safety net. It is particularly striking because of the unusual fact that some of the money paid by the indemnity insurer appears to be going to flow through to the individual professional alleged to have been at fault, to the detriment of the claimants who have made the claim.

Because one of the writers of this note is one of the counsel in the case, we identify the legal analysis but do not comment on it.

The background to the claim against the professional – the parties, the professional obligation to insure, and the client contract

The professional, Mr Lakhaney, ran an interior design practice. The practice was conducted by a limited company, Boscolo Limited, which he owned and controlled.

Boscolo was a member of the of the British Institute of Interior Design ("BIID"). The BIID required members to have professional indemnity insurance. It also provided to its members a standard contract template.

Messrs Desai and Shah owned a valuable flat in Hampstead which was Grade II listed. They wished to refurbish it and engaged Boscolo. The contract was in the BIID standard form.

Clause 9 of the contract's terms provided:

9 PROFESSIONAL INDEMNITY INSURANCE

9.1 The Designer shall obtain professional indemnity Insurance in respect of the Services for not less than the amount stated in the Letter/Memorandum.

9.2 The Designer shall maintain such insurance until the expiry of the period stated in the Letter/Memorandum provided such Insurance remains available to the Designer on

[1] An important part of the cover is, of course, the availability of funding to defend unmeritorious claims.

[2] As at 2022, only two states in the USA imposed on lawyers a requirement to have professional indemnity insurance (and that at low coverage levels). See the report of the International Bar Association: https://www.ibanet.org/document?id=IBA-International-Principles-on-Professional-Indemnity-Insurance-for-the-Legal-Profession, at page 9. The trend to compulsion in the United Kingdom was led by compulsion on solicitors to insure, of which the Supreme Court has said that the paramount purpose is the protection of those who use the services of solicitors: *Impact Funding Solutions Impact Finding Solutions Ltd v Barrington Service Ltd* [2017] AC 73 at paragraph 41: "the paramount purpose of The Law Society being given statutory power to require solicitors to maintain insurance cover against professional liability was "the protection of that section of the public that makes use of the services of solicitors" … ."

commercially reasonable rates and terms, failing which the Designer will inform the Client in order that the parties can discuss the best means of protecting their respective positions in the absence of such insurance.

9.3 The Designer shall produce on request, evidence that the insurance required under the Agreement is in place and is being maintained.

The insurance contract

Boscolo had and maintained a professional indemnity insurance policy with Royal & Sun Alliance Insurance Limited (RSA). The Policy had an indemnity limit of £250,000 with a £500 excess per claim. The Policy provided indemnity in respect of claims "in respect of civil liability… incurred in connection with the conduct of Professional Business."

Unknown to Messrs Desai and Shah, the Policy had a clause which provided:

"In connection with any Claim against the Insured the Insurer may at any time pay to the Insured the Limit of Indemnity…and thereupon the Insurer shall relinquish the control of such Claim and be under no further liability in connection therewith…"

In the writers' experience, clauses of that kind are not particularly uncommon. It is, however, difficult to find discussion of them in textbooks (they are referred to, without comment, in Enright's *Professional Indemnity Insurance Law*[3]).

The claim against Boscolo

Messrs Desai and Shah made a claim against Boscolo, which has not been determined.

The essential allegations were as follows. Mr Lakhaney had been asked by the clients whether Listed Building Consent was required for interior design alterations proposed by him. Mr Lakhaney said that it was not. It is alleged that the making of this statement was a breach of the duty owed by Boscolo to Messrs Desai and Shah. Proceeding on the basis that no Listed Building Consent was required, the alterations were then carried out. It turned out that Listed Building Consent had been required, so the alterations were unlawful. That caused financial loss to Messrs Desai and Shah, alleged to be well over £250,000.

The involvement of insurers

The claim was referred to the insurers. By this time Boscolo was insolvent, and RSA knew that. Before Boscolo became a "relevant person" for the purposes of the Third Parties (Rights Against Insurers) Act 2010 – at which point Boscolo's rights against insurers would have been transferred to Messrs Desai and Shah – RSA exercised the contractual right to pay to Boscolo the limit of indemnity. It did not seek to impose any restriction on the use of the money by Boscolo.

One may surmise that RSA thought that the claim against Boscolo had sufficient substance that RSA was better off paying £250,000 than it would be if it funded defence of the claim.

Boscolo having been paid by RSA, it had no rights left against insurers, and so there were no rights left to be transferred under that Act if Boscolo became a "relevant person".

Boscolo promptly went into creditors' voluntary liquidation (thereby becoming a "relevant person" – when becoming such was irrelevant). Liquidators then had to consider whether the

[3] 3rd edition, at paragraph 4-077.

insurance money was or was not part of the assets of the company – If it was, it ought to be divided pari passu amongst the general body of creditors. The main creditor other than Messrs Desai and Shaw was Mr Lakhaney.

The issues in the Court of Appeal, and the decision

The essential question was whether Messrs Desai and Shah had, by one route or another, acquired a right in the money paid by insurers.

The Court of Appeal (Moylan, Arnold and Zacaroli LJJ) unanimously upheld the decision of HHJ Matthews that the money belonged to the company and ought to be divided pari passu amongst the general body of creditors.

The right was asserted on two bases.

Firstly, that there was an implied term in the contract between Messrs Desai and Shah and Boscolo, the effect of which was that, in the circumstance of Boscolo being insolvent, the money would be held on trust to address the claim.

This contention was rejected because the Court considered:

a) that the suggested term was not necessary;

b) that the detail of the term could not be identified with sufficient precision to meet the "reasonable bystander" test (the problems of formulation of such a term are discussed in detail in the judgment);

c) that a valid trust could not have been created.

Secondly, that there was a constructive trust over the proceeds of the policy.

This contention was rejected on the basis that it was, in the Court's view, "an attempt to resurrect the type of constructive trust recognised in *Neste Oy v Lloyds Bank plc* [1983] 2 Lloyds Rep 658, but rejected by the Supreme Court in *Angove's Pty Ltd v Bailey* [2016] UKSC 47; [2016] 1 WLR 3179 as a species of remedial constructive trust not recognised in English law." (paragraph 84).

Observations

The result is not a happy one[4], except perhaps for Mr Lakhaney. If there was indeed a breach of duty, it was his personal mistake, and the improvement of his lot as a creditor is inconsistent with the moral principle, often relied upon in judicial decisions, that no one should benefit from his or her own wrong.

On the basis of this decision, only some very specific wording in the contract between a professional and a client will confer on the client, under that contract, a proprietary, or equivalent, right in money paid by insurers in similar circumstances.

We say "equivalent" because in a different context the Court has recognised that there may be an enforceable fiduciary obligation on an insured to deal with insurance proceeds in a particular way. In *re E Dibbens & Sons Ltd* [1990] B.C.L.C 577 the company provided furniture storage facilities. Some customers had specifically requested the company to insure their goods; others had not. The warehouse burned down and the insurers paid the company, which went into creditors' voluntary liquidation. Harman J. considered that the better approach was not to start

[4] The Court describes the result as creating a hardship for the appellants: paragraph 90.

off by "characterising the matter as a trust or not a trust"[5] but by examining whether the contracts of those who had stipulated for the insurance gave rise to a fiduciary duty. He concluded that it did, and that a fiduciary duty existed as to the application of insurance monies which (a) could be enforced and (b) protected them from the general body of creditors.[6]

One is inclined to say that at the very least it would seem necessary that the professional be restricted by contract from doing anything with the insurance proceeds pending the resolution of the client's claim (except, possibly, for funding the defence of it). It is possible that that overstates what is necessary, but it seems to the writers appropriately cautious.

Even such a provision might fail to protect a third party claimant (such as a disappointed intended beneficiary under a Will).

Regulators may wish to consider whether they can impose requirements at the level of the insurance contract which would result in segregation, and restriction of use, of the insurance proceeds pending resolution of the claim in respect of which the insurer has elected to pay the insured sum rather than conducting the defence. Such a restriction would enable the money to be used to fund a defence, but would also see that it went to the appropriate hands if the defence failed.

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Disclaimer: this article is not to be relied on as legal advice. The circumstances of each case differ and legal advice specific to the individual case should always be sought

[5] Page 581h

[6] Page 583