

Solicitors' Professional Indemnity Insurance – When does one partner 'condone' the dishonest conduct of another partner?

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Professional indemnity insurers who provide the first layer of insurance to solicitors must issue policies which comply with the SRA's Minimum Terms and Conditions of Professional Indemnity Insurance. Cl.6.8 of the Minimum Terms permits insurers to decline to cover claims which arise from dishonesty, or a fraudulent act or omission, which was either (a) committed or (b) "condoned" by a person.

How does this apply in practice? Take the case of a solicitors' firm with two partners, A and B. A claim is made against the firm and it arises out of the fraudulent act of A. If the insurers can prove not only (i) that A committed the fraudulent act but also (ii) that B condoned that fraudulent act, then they need not cover the claim. But what do insurers have to prove in order to show that B "condoned" A's fraudulent act?

The Commercial Court is the specialist court dealing with insurance law. The question of what 'condone' means in this context reached the Commercial Court for the first time in *Discovery Land Company LLC v AXIS Speciality Europe SE* [2023] EWHC 779 (Comm) (3 April 2023). Jirehouse was both a company and a solicitors' practice. The two directors were Mr Jones and Mr Prentice. Discovery Land and linked companies made claims against Jirehouse which arose out of the fraudulent acts of Mr Jones, and obtained judgments against Jirehouse. The question was whether Mr Prentice had condoned those fraudulent acts, so that the insurers of Jirehouse, AXIS, did not have to provide cover for the claims.

Mr Jones had been retained by Discovery Land in connection with its intended purchase of Taymouth Castle in Scotland. Discovery Land had sent US\$14m to Jirehouse to use as the purchase money for the castle. Mr Jones dishonestly took the \$14m for himself. By a series of lies, he then persuaded Discovery Land to send additional money to buy the castle, and Discovery Land did buy the castle. Mr Jones then arranged for the castle to be mortgaged. The sum raised by the mortgage was nearly £5m. Mr Jones proceeded to take that money for himself as well.

The question was whether Mr Prentice, the other director, had condoned those two acts of dishonesty. The judge, Mr Justice Robin Knowles, held that

- 'condone' should be given its meaning in ordinary language;
- in ordinary language, to condone an act "conveys acceptance or approval" of the act, although "in some situations it does not require an overt act" (of approval);
- in order to prove that a person, B, has condoned the fraudulent act of another, A, it is not necessary to show that B knew of the fraudulent act before, or at the time when, it was committed. Instead, "it is enough [for B] to know and condone a pattern of dishonest behaviour of which the particular fraudulent act forms part."
- In deciding what B knows, the court should take account of 'blind eye knowledge', in the sense of a suspicion "firmly grounded and targeted on specific facts" and a deliberate decision by B to "avoid obtaining confirmation of facts in whose existence [B] has good reason to believe" (*Group Seven v Nasir* [2020] Ch 129).
- In this context it is necessary to decide "what it was that was condoned." That requires close attention to the facts.

The judge therefore engaged in a detailed analysis of the facts. What he found was that, although Mr Prentice's behaviour was open to considerable and justifiable criticism, the evidence did not show that Mr Prentice had realised that Mr Jones was involved in a multi-million pound fraud; Mr Prentice did not realise that, and he did not condone it. As a result, Mr Prentice did not condone the two relevant fraudulent acts of Mr Jones. The insurers therefore had to provide cover in respect of the claims which were based on those two fraudulent acts.

Of course, each case turns on its own facts. The case confirms that, before an insurer concludes, for the purposes of the Minimum Terms, that B has condoned A's fraudulent acts or omissions, the insurer must undertake a detailed factual enquiry. But it also suggests that, even if the evidence shows that B has condoned some dishonest or fraudulent conduct of A's, the insurer must ask what it is that B condoned: can it fairly be said that B has condoned the fraudulent acts or omissions out of which the claims arise? If not, the claim must be covered.

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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.