When Will the Court Force You to Lie in a Crib of Your Own Making?

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PRACTICES International Arbitration

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In *LA Micro Group (UK) Ltd* v *LA Micro Group, Inc* [2021] EWCA Civ 1429, the Court of Appeal reviewed the law relating to 'estoppel by conduct'.

This doctrine prevents a party from adopting inconsistent positions in separate or successive formal proceedings. The Court of Appeal considered the rationale for this doctrine in a case that arose from the breakdown of the relationship between two close friends, involving businesses with very similar names, one operating in the United Kingdom and the other in the United States. In this article, we look at what happened in the case, the raison d'être for the doctrine and the application of it to the facts, before considering its relevance against the background of other wider legal principles, notably *res judicata*.

How the parties fell out

Mr. Frenkel and Mr. Lyampert are two Russian American businessmen. They were friends and business partners for nearly 10 years before falling out in February 2010, when they embarked on hard fought litigation both in the United States and in England. In happier times, Mr. Frenkel and Mr. Lyampert each owned 50% of and ran a business in California, through a company called LA Micro Group Inc ("**LA Inc**"). LA Inc purchased and resold high end computer components. After a few years in business, they wanted to expand across the Atlantic – and it is at this stage that the third protagonist (or antagonist) appears, a Mr. Bell.

LA Inc had already been trading with an English company owned by Mr. Bell. Discussions about a joint venture between Mr. Frenkel / Mr. Lyampert and Mr. Bell commenced. In April 2004, LA Micro Group (UK) Limited ("**LA UK**") was newly incorporated. A single share in LA UK was issued to Mr. Bell. It was not until 2009 that a second share in LA UK was issued, this time to Mr. Lyampert. The legal shareholding did not, however, reflect how the parties wanted to divide beneficial ownership of LA UK. During meetings in 2004, the parties had discussed, and ultimately agreed, how ownership and entitlement to profits made by LA UK were to be split, but nobody had drawn up a contract or (it seems) recorded the terms of the agreement clearly in writing. In the litigation that ensued, it was common ground that 49% of LA UK was beneficially owned by Mr. Bell. However, the ownership of the other 51% of LA UK would prove to be most contentious.

In early 2010, Mr. Frenkel ended his business relationship with Mr. Lyampert. He commenced proceedings in the Californian courts, seeking the dissolution of LA Inc (previously held 50/50 by Mr. Frenkel and Mr. Lyampert), claiming that Mr. Lyampert had breached his fiduciary duties. Mr. Frenkel would go on to be successful in that litigation, at least on paper: in 2017, the Californian courts awarded him restitutionary damages of US$ 4.3 million, but this judgment appears to have gone unpaid.

As regards LA UK, in discussions held in 2010 as part of the break-up, Mr. Frenkel made it known at least twice to Mr. Bell that he wanted nothing more to do with the UK anymore and that the company (LA UK) was Mr. Bell's. Mr. Bell and Mr. Lyampert, still the only two registered shareholders in LA UK, took Mr. Frenkel at his word. They altered the trading relationship between LA UK and LA Inc and agreed that the beneficial interest of the shares in LA UK should now accord with the legal title - so 50% held by Mr. Lyampert and 50% held by Mr. Bell.

As things turned out, following the departure of Mr. Frenkel, the prospects of LA UK improved considerably. By 2015, LA UK recorded a turnover of over £13 million and a trading profit before tax of £856,766. Mr. Frenkel, who had not recovered anything through the US litigation, went after LA UK. He brought a claim in the English Courts – this was the first of two sets of proceedings in England. In the first claim, Mr. Frenkel sought a declaration from the High Court that 25.5% of LA UK were held by each of himself and Mr. Lyampert personally (accepting that Mr. Bell owned the other 49%). He said that notwithstanding the fact that only Mr. Bell and Mr. Lyampert held shares in LA UK, the 25.5% split had been agreed at a meeting in 2004, which Mr. Frenkel had not attended in person. In 2017, Mr, Frenkel's claim came before HHJ Tipples QC. The judge determined that 51% of LA UK was beneficially owned by LA Inc, and 49% by Mr. Bell:

> "*I have reached the clear view that … there were no discussions between Mr Frenkel, Mr Lyampert and Mr Bell in late 2003 or early 2004 pursuant to which it was agreed a company would be established in the UK in which they all would be individually shareholders and directors … Rather, the agreement made between Mr Lyampert, on behalf of* [LA Inc]*, with Mr Bell, was that Inc would own 51% of the UK Company's share capital … [and] that the UK Company's profits would be split equally between Mr Bell and* [LA Inc]*…*"

Mr. Frenkel was thus found not to have acquired any interest in LA UK personally in 2004 when that company was set up. However, it remained at least arguable that Mr. Frenkel had some interest in LA UK as a result of his participation in LA Inc, which (as HHJ Tipples QC found) held 51% of the beneficial interest.

In parallel with the proceedings in England, Mr. Frenkel and Mr. Lyampert had continued to litigate in California. Mr. Bell had become embroiled in the US litigation, too. For present purposes, the material point is that in 2012, Mr. Bell was deposed by US attorneys in California. They asked him who the owners of LA UK were. He said:

> "*The owners, so far as I understand it, are myself, Mr Lyampert and Mr Frenkel.*"

Note the apparent inconsistency: Mr. Bell's answer in the deposition suggests that in 2012, LA UK was owned by the three men personally, rather than LA Inc having a 51% beneficial interest as was contended, and ultimately accepted, in the first English proceedings. Mr. Bell was asked about this statement in the proceedings before HHJ Tipples QC. Under oath, he explained that what he had meant to say was that "*… Mr Frenkel and Mr Lyampert were owners "via Inc"*."

After the judgment of HHJ Tipples QC, Mr Bell and LA UK brought a second claim in the English Courts. That claim was aimed at finally establishing that Mr. Frenkel had no interest in LA UK at all, either personally or indirectly through LA Inc. The claimants sought a declaration that Mr. Frenkel (and also LA Inc) had disclaimed any interest or shareholding in LA UK in 2010 – since Mr. Frenkel (also representing LA Inc at the time) had told Mr. Bell that "… *the company is yours* …". In 2021, HHJ Jarman QC, sitting in the High Court, accepted this. The judge found that Mr. Frenkel's

statements made in 2010 amounted to an irrevocable disclaimer of any interest in LA UK, and also bound LA Inc. Mr Frenkel appealed. That led to the Court of Appeal decision.

Estoppel by 'judicial' conduct

Before the Court of Appeal, the parties raised a range of points. For present purposes, the focus is on an argument made by Mr. Frenkel, that Mr. Bell was estopped from denying that LA Inc (and thus Mr Frenkel indirectly) had any beneficial interest in LA UK through the doctrine of 'estoppel by conduct' (or 'judicial conduct'), based on what Mr. Bell had said in the California deposition and, crucially, in the first English proceedings. Sir Christopher Floyd, sitting in the Court of Appeal, accepted that the doctrine formed part of English law. That much was clear from the decision of the Privy Council in *Kok Hoong* v *Leong Cheong Kweng Mines* [1964] A.C. 993 in which Viscount Radcliffe said that:

> "*A litigant may be shown to have acted positively in the face of the court, making an election and procuring from it an order affecting others apart from himself, in such circumstances that the court has no option but to hold him to his conduct and refuse to start again on the basis that he has abandoned.*"

This suggests that not every instance of a litigant changing its position gives rise to an estoppel: the inconsistency must be a reason for the order in question having been made, and the court must feel compelled to hold the litigant to their original position.

The Court of Appeal further agreed with the authors of *Spencer Bower and Handley: Res Judicata* that, on this particular point, there was no reason to suppose that the law of England is different to that of the United States, as expounded by the United States Supreme Court in *New Hampshire* v *Maine* 532 U. S. 742 (2001). Justice Ginsburg, delivering the unanimous opinion of the US Supreme Court, held that the doctrine could not be reduced to any general formulation of principle, but that there were a number of factors which would inform the court's decision in any particular case. Sir Christopher Floyd found it convenient to adopt these three factors, whilst clarifying that they should not be considered as exhaustive. It will therefore be relevant to ask (i) whether a party's later position was "*clearly inconsistent*" with its earlier position, (ii) whether the party succeeded in persuading the court of the earlier position; and iii) "*whether the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped*".

A closer look at the rationale for the doctrine

Equity generally steps in where there is unconscionability, and retains flexibility as to when that is deemed to be the case. With that in mind, three main rationales for the doctrine can be discerned from the cases cited in Sir Christopher Floyd's judgment and the wider jurisprudence. The first is, perhaps self-evidently, the importance of promoting proper and truthful conduct in judicial proceedings. In *New Hampshire* v *Maine*, Justice Ginsburg supported the idea that the doctrine is meant to prevent parties to litigation from playing 'fast and loose' with the courts. Litigants should think carefully about what they say to the courts. They will be under oath. If they set out their stall in a particular manner, or worse, fail to tell the truth, they should be held to this (leaving to one side potential sanctions for contempt of court). As the Tennessee Supreme Court put it in *Hamilton* v *Zimmerman* 37 Tenn. (5 Sneed) 39 (1857), the doctrine is rooted in the desire to uphold "*the proper reverence for the sanctity of [the judicial] oath*". In that case, Hamilton claimed that there was a secret agreement with Zimmerman, that they were to operate the pharmacy they both worked at as a partnership. The Tennessee Supreme Court held that Hamilton was estopped from asserting that

he was a partner by his representing in a previous case with Zimmerman that he was employed as a clerk. This rationale alone would not, however, require that the previous court was *persuaded* of the position taken in the first proceedings, or that this was a reason for the judgment or order having been made. If the principle is designed to deter lies, then it should not matter whether the lie was believed in the initial proceedings. After all, a deterrent that only bites when you have already made a gain (and which does not undo that gain) does not deter much.

Looking beyond merely protecting the judicial oath or promoting truthful conduct in litigation, the Court of Appeal in *LA Micro* also referred to the earlier English decision in *Gandy* v *Gandy* (1884) 30 Ch 57. In that case, Bowen LJ refused to permit an argument that was inconsistent with a prior one, at least partially, on the basis that "… *there would be monstrous injustice*" if the claimant was allowed to win one case on one footing and then "… *turn round and win the new suit upon a diametrically opposite construction*". This suggests that the doctrine is, in reality, about bringing justice to the parties to the case – with a focus on the consequences. This justification for the doctrine, which is further supported by Justice Ginsburg's final factor (that the party seeking to advance the inconsistent argument would derive an unfair advantage or push an unfair disadvantage on the other party), is broadly similar to that for equitable estoppel in general, which will refuse to allow a representor to resile from their representation when, broadly speaking, it would be unconscionable for them to do so. But if doing justice between the parties is the rationale, then estoppel by judicial conduct would require there to be the same litigants in the separate proceedings for it to apply – thus essentially making it a species of 'normal' equitable estoppel which only operates as between the (same) parties.

Finally, Justice Ginsburg in *New Hampshire* v *Maine* (as approved in *LA Micro*) also seemed to justify the doctrine on the basis that it was needed to "… *protect the integrity of the judicial process*", a concern that is reflected in numerous other US decisions. On this understanding, the doctrine is designed to prevent a court from rendering inconsistent judgements, something that would undermine the credibility and authority of the court. The risk of inconsistent judgments is not a danger that other doctrines, such as estoppel by representation, are well placed to address.

The Court of Appeal's formulation of the test

Having reviewed the authorities, Sir Christopher Floyd noted that "… *this form of estoppel by [judicial] conduct is one which is approached by means of a broad, merits-based assessment*" and that the doctrine should not be constrained by strict rules. Justice Ginsburg's three factors – in short, (i) was the position clearly inconsistent, (ii) was the earlier court persuaded, and (iii) was an unfair advantage gained – were certainly matters to consider. However, the most material question to ask was:

> "*… whether it is apparent that the earlier decision was obtained on the footing of, or because of, the stance taken by the party in the earlier proceedings. Absent that factor, whilst the change of position may affect the credibility of the party or the witness concerned, there will not be an impression that one or other court was misled into giving its decision, so that the administration of justice risks being brought into disrepute*."

English law thus focuses on the outcome or result brought about by the inconsistency. So, if the change of position has in fact led to an earlier decision (one which likely benefits the party in question), then they may very well be estopped in the later proceedings. If that is not the outcome, then the inconsistency will be relevant when it comes to assessing the credibility of the party in the subsequent proceeding. That could still be determinative: inconsistent evidence given by a witness under oath can be very damaging, and can lead to the evidence being thrown out.

The decision in *LA Micro*

In the second High Court proceedings in *LA Micro*, HHJ Jarman QC granted declarations that, following Mr. Frenkel's disclaimer in 2010, Mr. Lyampert and Mr. Bell were the only shareholders, they were entitled to the profits of LA UK, and that LA Inc did not beneficially own any of the shares, and was not entitled to any of the profits, of LA UK. The judge also found that Mr. Bell was not estopped from asking for these declarations. He concluded that there was no estoppel because Mr. Bell had not taken a "*clear and consistent position*" in previous proceedings, essentially finding that Mr. Bell had been confused. That reduced the weight that the court would attach to Mr. Bell's evidence:

> "*Before me Mr Bell sought to explain his earlier evidence by saying he was confused during that cross examination and that he was referring to the pre 2010 position. He sought to explain the deposition by saying that its focus was upon the incorporation of UK in 2004 and was taken in stressful conditions in California in a room full of lawyers as well as Mr Frenkel and Mr Lyampert.*
>
> *I accept that the main (but not sole) focus of his 2012 deposition was the formation of UK and that the main (but not sole) focus in the 2017 hearing was the 2004 agreement and that some of his answers in both were in such contexts.*
>
> *In my judgment there is no sufficient justification to infer that he was deliberately setting out to mislead the court, then or now. Even on the basis of confusion, however, that is sufficient for me to adopt the cautious approach to Mr Bell's evidence ...*"

As the judge noted, Mr. Bell had given a similar explanation during the 2017 proceedings, where he had also been cross-examined about what he had said in the deposition. At that stage, he explained that he had meant to say that Mr. Frenkel had been an owner 'via [LA Inc]'. That still leaves the issue of why Mr. Frenkel should have had an indirect interest in the company via the US entity, as of 2012, when Mr. Bell was now saying in court that there had been a disclaimer in 2010.

In the Court of Appeal, Sir Christopher Floyd nonetheless refused to accept LA Inc and Mr. Frenkel's estoppel argument. He held that "*it is not possible to say with anything approaching confidence that he [Mr. Bell] won before…* [HHJ Tipples QC in the first proceedings] *on the footing of or because of the position he took in relation to continued ownership by Inc*". All that Mr. Bell had needed to show in first set proceedings was that LA Inc held 51% of the beneficial interest in LA UK in 2004. The events of 2010 surrounding Mr. Frenkel's alleged disclaimer had not been in issue, and Sir Christopher Floyd found that Mr. Bell had made no sufficiently clear representation as to them. He noted that it would be far-fetched to suggest that the first judgment, which determined who the shareholders of LA UK were in 2004, was the result of Mr. Bell's representations as to what the position had been after 2010.

Instead, as the Court of Appeal noted, HHJ Tipples QC had assessed the evidence of all the witnesses, attaching due weight to the fact that Mr. Frenkel had not been present at the meeting where the 2004 agreement was reached. The judge found that the reason for his absence was that Mr. Lyampert was attending on behalf of LA Inc. He was representing the company's interests, and implicitly also those of its shareholders, including Mr. Frenkel. There were only two parties to the 2004 agreement: LA Inc and Mr. Bell, and both were found to have become shareholders. Mr. Frenkel's case in the 2017 proceedings depended on hearsay evidence of what he was later told had been decided at the meeting (on his case, that he was to have a personal 25.5% interest,

which the judge rejected). In all the circumstances, the Court of Appeal found that Mr. Bell's change of position was not "… *an affront to the administration of justice*."

Discussion: looking at estoppel by 'judicial' conduct in context

There was no estoppel by conduct in *LA Micro* because no court ever based a decision on a statement by Mr. Bell from which he then sought to resile in subsequent proceedings. HHJ Tipples QC did not reach her decision on the ground of Mr. Bell's evidence that LA Inc was the only other beneficial owner in 2004, and also still in 2012. When Mr. Bell made the infelicitous statement in 2012 that "*The owners, so far as I understand it, are myself, Mr Lyampert and Mr Frenkel*", the first set of proceedings had not been commenced. When he was cross-examined in the first set of proceedings about this statement, he explained that he had meant to refer to LA Inc as being the vehicle through which Mr. Frenkel was an 'owner' in 2012. While even that explanation was inconsistent with the declaratory relief sought in the second proceedings, the previous judgment was not based on Mr. Bell's inconsistency, and there was no risk to the integrity of the judicial process.

Sir Christopher Floyd's judgment is a relatively rare example of the English Courts reviewing the doctrine of estoppel by judicial conduct at the appellate level. The requirement that the previous and new positions should be inconsistent is crucial, but - as *LA Micro* illustrates – apparently inconsistent utterances may yet be capable of explanation or justification once the judge has had the chance to hear the witness in person. It is also plainly necessary that the previous position has been accepted by a court. If a court refused to accept the argument the party previously made then there is no risk of harming the integrity of the judicial system if a subsequent decision also impliedly rejects it, by accepting an alternative account (indeed, the integrity would, in fact, be bolstered).

English litigation is adversarial by nature, and judges and arbitrators decide on the evidence presented to them and the arguments made before them. A situation could therefore arise where a party adopts an inconsistent position, but for whatever reason – perhaps by oversight – the other party does not raise the estoppel. If the court or tribunal were to accept the inconsistent position, it might make an inconsistent judgment or award. Should it therefore be open to judges or arbitrators to find an estoppel by conduct of their own volition, always provided that they have sufficient information to spot the issue? That appears anathema to English practitioners and decision-makers. However, at the very least, judges or arbitrators could put the argument to the parties, which generally ensures that submissions are made, and the point can then be decided.

Estoppel by conduct exists alongside other legal principles that govern the conduct of litigation, in particular those that control successive or parallel proceedings that touch on the same issues. The main such principle is that of *res judicata*, which holds that the finality of litigation is in the public interest, and that defendants should not be put to the trouble of dealing with claims arising out of the same set of circumstances twice. *Res judicata* has two main branches – cause of action estoppel and issue estoppel. A cause of action estoppel arises where, as the House Lords held in *Arnold* v *National Westminster Bank* [1991] 2 AC 93:

> "*… a cause of action in a second action is identical to a cause of action in the first, the latter having been between the same parties or their privies and having involved the same subject matter. In such a case, the bar is absolute in relation to all points decided, unless fraud or collusion is alleged, such as to justify setting aside the earlier judgment. The discovery of new factual matter which could not have been found out by reasonable diligence for use in earlier proceedings does not permit the matter to be re-opened.*"

This is a defendant's first port of call when faced with a second or subsequent similar claim: if it can be shown that the cause of action in the second claim is identical to one that has either been found to exist, or not exist, the second claim must be struck out. A party cannot seek to have a second bite at the cherry, or even recover more damages for losses it could not have claimed for in the first claim. A defendant who cannot establish cause of action estoppel may seek to rely on issue estoppel. In *Arnold* v *Westminster*, Lord Keith said:

> "*Issue estoppel may arise when a particular issue forming a necessary ingredient in a cause of action has been litigated and decided and in subsequent proceedings between the same parties involving a different cause of action to which the same issue is relevant, one of the parties seeks to reopen that issue.*"

Issue estoppel prevents a party from reopening or revisiting a matter that has already been decided in a claim between the same parties. Assume a party adopts a position on an issue that is accepted in the earlier proceedings. If that party were then to bring a subsequent claim for a different cause of action against the same defendant (avoiding *res judicata*), but in doing so had to advance a different (now more advantageous) position on the same issue that has already been decided, then it might yet be estopped from pursuing the fresh cause of action. This is because the original finding on the issue would then appear as adverse, and, as Snowden J said in *Taylor Goodchild Ltd* v *Taylor* [2020] EWHC 2000 (Ch):

> "*The policy underlying issue estoppel is that a party against whom adverse findings were made in one case should not be able to challenge them in subsequent proceedings between the same parties.*"

Res judicata has many facets, and there are exceptions to issue estoppel (notably the availability of fresh evidence, or the discovery of fraud) which are beyond the scope of this article. In addition, English law also recognises that the judicial process should be final, and should not be abused or prolonged by successive claims. This is called the rule in *Henderson* v *Henderson* [1853]. More recently, in *Barrow* v *Bankside Members Agency Limited* [1996] 1 All ER 981, the late Bingham LJ (as he then was) explained this was a rule of public policy that:

> "*... requires the parties, when a matter becomes the subject of litigation between them in a court of competent jurisdiction, to bring their whole case before the courts so that all aspects of it may be finally decided ... once and for all. In the absence of special circumstances the parties cannot return to the court to advance arguments, claims or defences which they could have put forward for decision on the first occasion, but failed to raise.*"

If neither cause of action estoppel, issue estoppel or the rule in *Henderson* v *Henderson* applies, a party may still seek to raise estoppel by conduct, which does not require proof of identity of the cause of action or the issue in question, or persuading the court that the point should have been made in the earlier proceedings. These points are always worth reviewing when faced with several sets of litigation arising out of the same facts.