The assessment of interest in breach of trust cases (Watson v Kea Investments)

28/10/2019

Dispute Resolution analysis: This case provides useful guidance in respect of the appropriate method in assessing interest payable in respect of breach of trust cases. In particular, it confirms that in appropriate cases where there is sufficient evidence, the rate of interest payable ought to be assessed on the basis of the equivalent rate of interest which could have been obtained if the money had been invested in a proper trustee investment. A fixed rate of interest based upon the level of interest which could have been obtained by borrowing or depositing the money was not appropriate in this instance. Written by Georgia Whiting, barrister at 4 King's Bench Walk.

Watson v Kea Investments Ltd [2019] EWCA Civ 1759, [2019] All ER (D) 147 (Oct)

What are the practical implications of this case?

This decision provides important guidance in respect of the assessment of interest in breach of trust cases. However, it is arguably equally applicable in respect of any case in which a party can demonstrate that money was wrongly taken and subsequently held pursuant to a constructive trust.

The leading judgment of McCombe LJ also provides a helpful review of the relevant authorities in respect of the award of interest in such cases. In appropriate cases, judges are perfectly entitled to make an award of interest by reference to the amount which would have been obtained had the money been invested in 'proper trustee investments'.

In any such case, practitioners need to ensure that clear and cogent evidence of the rate of interest which could have been achieved if the money had been invested in proper trustee investments is put before the trial judge. Arguments in such cases that interest rates should reflect the equivalent borrowing or deposit rates are now unlikely to be successful.

What was the background?

The underlying claim was brought by Kea Investments Ltd and Sir Owen Glenn against several defendants, including Mr Watson and two companies called Novatrust Ltd and Spartan Capital Ltd. Watson and Sir Owen agreed to participate in an investment joint venture, through Spartan as the joint venture vehicle. The relationship eventually deteriorated, and Kea presented a petition for the winding up of Spartan on the 'just and equitable' ground. Sir Owen and Kea issued a claim in the underlying proceedings alleging deceit and a breach of fiduciary duty on the part of Watson and others and seeking the setting aside of various joint venture agreements. The trial judge held that Watson was personally liable to pay equitable compensation to Kea, representing the shortfall between a settlement (mid trial) which had been reached between Spartan and Kea. Therefore, a key question was establishing the amount of interest properly recoverable by Kea from Spartan up until the monies were paid.

The trial judge held that Kea was entitled to equitable compensation from Watson and that interest should continue to accrue at 6.5% per annum (compounded annually). The issue on appeal was whether the interest payable should properly have been fixed at a rate of 6.5% to reflect what the money to be recovered would have produced if invested in 'proper trustee investments'. Watson argued that interest should instead be fixed by reference to borrowing or deposit rates, at a level no higher than 3% above base rate.

The trial judge granted permission to appeal because he considered that there was a compelling reason for the appellate court to give guidance on the exercise of discretion by trial judges in fixing interest rates in cases of this type.

What did the court decide?

For Watson, it was contended that the trial judge was wrong to approach the case on the basis that interest was to be calculated against a defaulting trustee and that, in any event, an appropriate rate of interest representing income yield only should have been fixed.

McCombe LJ, in giving the lead judgment held that the trial judge exercised his discretion to award interest under the equitable jurisdiction of the court entirely in accord with the principles to be found in the decided cases. Accordingly, the decision was upheld. It was objected that an award of interest at the rate of 6.5% was without precedent. However, McCombe LJ considered that the crucial question was whether the award was in accord with equitable principles, rather than whether an award at the specific rate in question had been made before.

In dealing with the question of interest on equitable compensation in trust cases, the courts had consistently tried to make awards that were suited to the investment of trust funds and the economic realities of the times. In each individual case, a suitable proxy rate for the general characteristics of the claimant entitled to the equitable remedy must be found. That was entirely in accord with the approach to the interest award, albeit in different circumstances, in the case of *Carrasco v Johnson* [2018] EWCA Civ 87, cited in the instant case.

A borrowing rate was not appropriate in the instant case as it was unrealistic to assume that the deprived fund would have borrowed to invest. It was similarly unrealistic to assume that the deprived fund, duly replaced, would have been placed on deposit with no regard to capital accretion; it would not have been so placed. Thus, the material before the judge illustrated precisely what a deprived fund of the type in question would have done with the appropriated money. The appeal was accordingly dismissed.

Case details

- Court: Court of Appeal, Civil Division
- Judge: McCombe, Hamblen LJJ and Sir Bernard Rix
- Date of judgment: 23/10/2019

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