Recent developments in setting aside judgments for fraud

by Catherine Gibaud KC and Devon Airey, Three Verulam Buildings

Status: **Published on 29-Apr-2025** | Jurisdiction: **England, Wales**

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In this article, Catherine Gibaud KC and Devon Airey of Three Verulam Buildings consider recent developments in setting aside judgments for fraud and provide practical considerations for litigants.

The principle that fraud vitiates a judgment extends back to the decision of *Lazarus Estates Ltd v Beasley [1956] 1 Q.B. 702*: "*No court in this land will allow a person to keep an advantage which he has obtained by fraud. No judgment of a court... can be allowed to stand if it has been obtained by fraud. Fraud unravels everything.*" (*Denning LJ at paragraph 712*). However, as the Privy Council recently warned in the judgment of the Board handed down by Lord Leggatt in *Finzi v Jamaican Redevelopment [2024] 1 WLR 541*, allegations of fraud are not to be regarded as "*some kind of open sesame which have only to be uttered to enable a party to engage in a new round of litigation of disputes that have been compromised or decided*" (*paragraph 76*). Recent decisions have highlighted the tension between two long-established principles of public policy, namely that fraud unravels all, and that there should be finality in litigation. This article considers recent developments in setting aside judgments for fraud and provides practical considerations for litigants.

When will a judgment be set aside for fraud?

No need for reasonable diligence

One of the most pivotal recent decisions in setting aside judgments for fraud is the Supreme Court's ruling in *Takhar v Gracefield Developments Ltd [2019] UKSC 13*. In a dispute concerning the transfer of land, the defendants at the original trial relied upon an agreement between the parties, which appeared to show the claimant's signature. Although the claimant could not explain how her signature came to be on the agreement, no allegation of fraud or forgery was made at trial. However, after the trial, the claimant obtained expert handwriting evidence showing their signature had been transposed onto the signature page from a different letter. The question was whether the claimant could commence new proceedings, setting aside the earlier judgment, on the basis that the signature relied upon had been forged. The defendants sought to strike out the claim on the basis that the claimant could have discovered this evidence by exercising reasonable diligence and that, therefore, the claim to set aside the original judgment for fraud was an abuse of process.

Newey J held that a party seeking to set aside a judgment for fraud did not have to demonstrate that they could not have discovered the fraud by the exercise of reasonable diligence and held that the claim to set aside was not an abuse of process. The Court of Appeal overturned the decision of Newey J on the grounds that there was a reasonable diligence test and applied the policy considerations embodied in the rule in *Henderson v Henderson*.

The Supreme Court allowed the appeal from the Court of Appeal and found there were no grounds to impose a reasonable diligence requirement in the test for setting aside a judgment for fraud. The leading judgments were given by Lords Kerr and Sumption. Lord Kerr (with whom Lord Hodge, Lord Lloyd-Jones and Lord Kitchen agreed) found that "*where it can be shown that a judgment has been obtained by fraud, and where no allegation of fraud had been raised at trial which led to that judgment, a requirement of reasonable diligence should not be imposed on the party seeking to set aside the judgment*" (*paragraph 54*). Lord Kerr qualified this statement in two respects: in circumstances where fraud had been raised at the original trial and new evidence of the fraud is advanced, or where at the original trial a deliberate decision was made not to investigate suspected fraud. In both cases, he

stated that the court would have a discretion as to how to deal with those situations (*paragraph 55*).

Lord Sumption (with whom Lord Hodge, Lord Lloyd-Jones and Lord Kitchen agreed) opined that setting aside judgments for fraud was not a procedural application but a free-standing cause of action (*paragraph 60*). Lord Sumption continued:

> "The cause of action to set aside a judgment in earlier proceedings for fraud is independent of the cause of action asserted in earlier proceedings. It relates to the conduct of earlier proceedings, and not to the underlying dispute. There can therefore be no question of cause of action estoppel. Nor can there be any question of issue estoppel, because the basis of the action is that the decision of the issue in the earlier proceedings is vitiated by fraud and cannot bind the parties..." (*paragraph 61*).

Lord Sumption went on to state (at paragraph 63) that the basis on which the law sets aside transactions (including judgments) for fraud is that a reasonable person is entitled to assume honesty in those with whom they deal. Thus, where the judgment has been obtained by fraud, it is wrong to hold that because a matter could have been raised in earlier proceedings, that it *should* have been so raised, such as to render the raising of the matter in later proceedings necessarily abusive. A person is not expected to conduct their affairs on the basis that other persons are dishonest, unless they know that they are. So, unless a claimant deliberately decided not to investigate a suspected fraud or rely on a known fraud, then it cannot be said that they *should* have raised it in the earlier proceedings, even if they *could* have done.

The Supreme Court in *Takhar* endorsed the stringent conditions set out by Aikens LJ in *Royal Bank of Scotland plc v Highland Financial Partners LP [2013] EWCA Civ 328* (combined with the professional duties of counsel) as a means of keeping the risks of frivolous or extravagant litigation within acceptable limits.

The "materiality" requirement

The questions of establishing whether there was a fraud in the obtaining of a judgment and whether the fraud was sufficiently material for the purposes of setting aside that judgment are often inter-related. However, the requirement of materiality does not extend to the second court having to retry the whole question of the liability of the parties. The correct test for materiality in the context of a cause of action to set aside a judgment for fraud was considered by the Court of Appeal in *Tinkler v Esken [2023] EWCA Civ 655*.

Mr Tinkler was removed from office as a director by his co-directors. He sought to challenge a decision of HHJ Russen QC (sitting as a judge of the High Court) upholding his dismissal by alleging that new evidence that had been deliberately withheld from HHJ Russen, which was highly material to the issues that he had decided and would have changed the court's approach and decision. In considering the action to set aside the judgment for fraud, Leech J found that no such fraud was proved, and he preferred the formulations of the materiality test applied in *Highland*.

The Master of the Rolls, Sir Geoffrey Vos (in a judgment with which Popplewell and Snowden LJJ agreed) found that:

- The resolution of the appeal was assisted by an understanding of the *dicta* of Lord Sumption in *Takhar* to the effect that the cause of action to set aside a judgment for fraud is independent of the cause of action asserted in the earlier proceedings and relates to the conduct of the earlier proceedings and not to the underlying dispute (*paragraph 11*).
- "*...the court... has to be shown to have been deceived, deliberate dishonesty is required, and materiality rather than simple reliance must be shown...*" (*paragraph 12*). It is important to understand what the court is doing in trying a free-standing action to set aside a judgment for fraud, it is to be tried like anything else by evidence properly taken directed to that issue (that is, the issue of whether there was a fraud on the court). It is "*quite different from an application to adduce fresh evidence after judgment*" under principles in *Ladd v Marshall [1954] 1 WLR 1489* (*Tinkler, paragraph 13*).
- The correct test for materiality was that set out in *Highland*, which was supported by the case law and to be preferred (*paragraph 20*). The majority of the Supreme Court in *Takhar* (at paragraphs 56 and 67) expressly referred with approval (albeit *obiter*) to Aikens LJ's formulation in *Highland* (*paragraph 106*) to the effect that:
  - there must be conscious and deliberate dishonesty in relation to the relevant evidence given, or action taken, statement made or matter concealed;
  - the relevant evidence, action, statement or concealment must be "material" in the sense that the fresh evidence that is adduced after the first judgment is such that it demonstrates

that the previous evidence or concealment was "*an operative cause of the court's decision to give judgment in the way it did*" or that the fresh evidence "*would have entirely changed the way in which the first court approached and came to its decision*"; and

– the question of materiality of the fresh evidence was to be assessed by reference to its impact on the evidence supporting the original decision (*paragraphs 35 and 44*).

In practice, the three-part test set out by Aikens LJ can be considered in two parts, namely the "fraud condition" comprising his first criterion and the "materiality condition" comprising his second and third criteria.

- Aikens LJ in *Highland* was not requiring that it be shown that, but for the fraud, the first judgment would not (on a balance of probabilities) have been given, but rather that the fraud was an operative cause of the judgment or would have entirely changed the first court's approach (*paragraphs 51 to 56*).
- The judge's task is to see whether the new evidence impugns the original judgment (*paragraph 44*). The judge must look at the new evidence alongside the old to establish if, considered together, the trial judge had been materially misled (*paragraphs 41, 42, 44, 45 and 48*).
- The requirement of materiality does not extend to the second court having to retry the question of the liability of the parties or to see whether the fresh evidence or new facts are material to the final result. The purpose of a second action is to take the parties back to the position as it was before the trial so that a new trial on honest evidence can then take place (*paragraph 38,* citing Grant and Mumford, Civil Fraud (1st ed, 2018), paragraph 38-017).

The Court of Appeal concluded that the judge below had approached his consideration of the evidence correctly and had applied the correct test for materiality. The court unanimously dismissed Mr Tinkler's appeal, and upheld Leech J's decision.

Abuse of process: the test for "new" evidence on the application to set aside for fraud

In *Finzi*, the Privy Council examined whether a claim to set aside various judgments and consequential settlements based on fraud could be dismissed as an abuse of process when the fraud alleged had been known to the claimant at the time of the original settlement agreement but not raised in those earlier proceedings and where the claimant had offered no explanation as to why they had not deployed the information at the earlier stage.

The Privy Council noted the tension between the "*strong public interest of achieving finality in litigation*" and the principle that "*fraud unravels all*". Lord Leggatt, handing down the judgment of the Board, held that the principle of finality is protected by means of the court's procedural power to prevent abuse of its process and that the Board saw "*no justification for exempting actions alleging that a settlement or judgment was obtained by fraud from the scope of that protection in cases where the evidence relied on was already known to the claimant at the time of the settlement or judgment*" (*paragraph 65*).

The Board clarified that, where a claimant relies on evidence not adduced in the original proceedings to allege that a judgment in those proceedings was obtained by fraud, the burden is on the claimant to establish either that the evidence is new, in the sense that it has been obtained since the judgment or settlement, or if the evidence is not new in this sense, any matters relied on to explain why the evidence was not deployed in the original action. Where the evidence is shown not to be new in this sense, the claim is likely to be regarded as abusive unless the claimant is able to show a good reason, which prevented or significantly impeded the use of the evidence in the original action (*paragraph 72*).

Conclusion

Accordingly, while *Takhar* clarified that a party seeking to set aside a judgment for fraud does not have to demonstrate that they could not have discovered the fraud by the exercise of reasonable diligence, cases such as *Tinkler* and *Finzi* show that the bar required to set aside the judgment remains high. *Tinkler* establishes that the test of materiality in *Highland* is the correct test to be applied and that this was a completely different test from the *Ladd v Marshall* test on an application to adduce new evidence. *Finzi* makes clear that if the claimant had all the material on which they now rely to allege fraud, which could have been deployed in earlier proceedings, the action to set aside the original judgment or settlement on fraud grounds is unlikely to succeed unless the claimant has a good explanation as to why that material was not deployed at the earlier stage.

Taking Stock: practical tips for setting aside judgments for fraud

The above recent developments give rise to the following considerations for litigants:

- **Clear and "new" evidence of fraud is essential.** Courts demand compelling proof of conscious and deliberate dishonesty in obtaining the original judgment (now impugned). Evidence must be "new" (that is, obtained post the judgment), or (if not) there must be a very good reason why the fraud was not raised in the original proceedings. Failure to meet the *Finzi* test will mean that the application to set aside for fraud is likely to be dismissed as an abuse of process.
- **"Materiality" is key.** The *Highland* test for materiality must be satisfied and is critical to the cause of action to set aside for fraud. The fraud must be shown to have been an "*operative cause*" on the original judgment. The judge will look at the new evidence alongside the old to determine whether the court was materially misled.
- **There is no requirement to show reasonable diligence.** If it is shown that a judgment has been obtained by fraud, it is not a reason to allow that judgment to stand that the victim of the deceit was negligent in failing to recognise or allege fraud in the earlier proceedings: "*a knave does not escape liability because he is dealing with a fool*" (*Finzi, paragraph 67, citing Gould v Vaggelas (1985) 157 CLR 215*).