

# *A new scope/purpose of duty test in professional negligence cases*



## **A summary of the Supreme Court judgment in Manchester Building Society v Grant Thornton UK LLP**

On 18 June 2021, the Supreme Court handed down a landmark judgment in the case of *Manchester Building Society (MBS) v Grant Thornton UK LLP [2021] UKSC 20* in which it has provided further guidance in relation to the application of the SAAMCO principle and established a six-part test for assessing the extent of a professional's liability for negligence.

### **Legal background – the SAAMCO principle (until now)**

The SAAMCO principle, as established in the judgment of the House of Lords (as it was then) in *South Australia Asset Management Corp v York Montague Ltd [1997] AC 191*, provides that a claimant must establish not only that the loss for which damages are claimed was caused by the professional's breach of duty but also that that loss fell within the scope of the duty owed by the professional. In giving the leading judgment, Lord Hoffman drew a distinction between a duty to provide *information* for the purpose of enabling someone else to decide upon a course of action and a duty to *advise* someone as to the course of action that they should take. Where the professional only gives information then they are only liable for the consequences of the information being wrong. However, where a professional gives a client advice, for example, whether to enter into a particular transaction at all, then, if the advice is negligent, the professional will be responsible for all of the consequences of the advice being wrong.

### **Factual Background**

By way of a high-level summary, MBS provided lifetime mortgages to customers incorporating a fixed rate of interest, which it funded by borrowing at variable rates of interest. To manage the interest rate risk on the transactions, MBS purchased interest rate swaps. In 2006, Grant Thornton ("GT") advised MBS that its accounts could be prepared using the practice known as 'hedge accounting', which would assist in minimising the volatility in MBS' balance sheet and the capital reserve requirements caused by the swaps.

In 2013, it was discovered that GT's advice as to the use of hedge accounting was wrong. MBS had to restate its accounts, which then showed insufficient capital reserves. Therefore, MBS had to sell the swaps early at a cost of £32.7 million. MBS also sold its book of mortgages at a profit of £5.96 million, providing a net loss to MBS of £26.7 million.

MBS claimed damages from GT for the losses suffered as a result of GT's negligent advice. GT admitted negligence and it was accepted that but for the negligent advice MBS would not have

suffered the loss. However, in accordance with the SAAMCO principle, GT denied that the loss was within the scope of its duty of care.

### Lower courts' decisions

The High Court concluded that, but for the negligent advice, MBS would not have bought the swaps and, therefore, it would not have needed to break the swaps in 2013. However, GT escaped liability (other than for certain penalty costs associated with terminating the swaps and some professional fees) because Teare J held that the loss resulted from a business decision by MBS to enter into the swaps, for which GT had not assumed responsibility. The losses crystallised at the time the swaps were closed out but the losses were caused by market forces and not by the act of closing out the swaps.

The Court of Appeal came to the same outcome as the trial judge but on different grounds. The Court of Appeal rejected Teare J's approach and found that the case should be determined by considering whether GT gave 'advice' or only 'information' to MBS in line with the SAAMCO principles set out above. The Court of Appeal held that this was an information case, such that GT was only responsible for the foreseeable consequences of the information it gave being wrong. The losses sustained by MBS were found not to be within the full scope of GT's duty of care.

### Supreme Court decision

The Supreme Court ruled unanimously in favour of MBS (although it produced three differing judgments). Lord Hodge and Lord Sales gave a joint leading judgment for the majority of five. They set out six questions, which should be asked in all professional negligence claims in order to assess liability. These are as follows:

1. The actionability question - Is the harm which is the subject matter of the claim actionable in negligence?
2. The scope of duty question - What are the risks of harm to the claimant against which the law imposes a duty on the defendant to take care?
3. The breach question - Did the defendant breach the duty by an act or omission?
4. The factual causation question - Is the loss for which the claimant seeks damages the consequence of the defendant's act or omission?
5. The duty nexus question - Is there sufficient nexus between a particular element of the harm for which the claimant seeks damages and the subject matter of the defendant's duty of care?
6. The legal responsibility question - Is a particular element of the harm for which damages are sought irrecoverable because it is too remote or because there is a different effective cause or because the claimant has mitigated his or her loss or failed to avoid loss they could have been expected to avoid?

They held that the scope of the duty of care assumed by a professional adviser, which was the central issue in this appeal, is governed by the purpose of the duty. This should be judged on an objective basis by reference to the purpose for which the advice is given. As such, in order to determine the scope of the professional adviser's duty, you must consider the risk the duty was supposed to guard against and then assess whether the claimant's loss was the result of that risk coming to fruition.

Further, they found that the distinction drawn between 'information' and 'advice' by Lord Hoffman in SAAMCO should be dispensed with. It followed that the counterfactual analysis as to whether the loss would have been suffered if the information provided by the defendant had been correct was no longer the core question, although it may still be utilised as a useful cross-check in simple factual circumstances.

Lord Leggatt and Lord Burrows gave separate but concurring judgments, while differing on certain aspects of the relevant test. Lord Leggatt considered that the central question is whether there is a sufficient causal relationship between what made the information or advice wrong and the loss. Lord Burrows placed greater emphasis on the policy considerations of achieving a fair and reasonable allocation of risk between the advisor and client than on the conceptual framework.

Applying the above to the circumstances of the case, the majority held that the purpose of GT's advice was specifically to assess whether MBS could use hedge accounting in light of its business model and the regulatory capital requirements. GT negligently advised that it could. As a result, MBS entered into the swap transactions and, when it was realised that hedge accounting could not be used, MBS was exposed to regulatory capital demands which the use of hedge accounting was supposed to avoid. Accordingly, the Supreme Court considered that MBS was entitled to recover the loss of £26.7 million from GT (subject to a deduction of 50% due to the trial judge's finding (which had not been appealed) that MBS had been contributorily negligent).

### **CPB Comment**

Many practitioners have welcomed the removal of the arbitrary distinction between 'advice' and 'information' cases, and the focus on the counterfactual analysis in the latter. However, professionals and their insurers will not welcome the anticipated rise in professional negligence claims, in terms of volume and quantum, as claimants may now pursue losses which had previously been considered to be beyond the duty owed by the professional.

Each case will continue to be judged on its own facts and circumstances. When contemplating or receiving a professional negligence claim, the importance of early advice cannot be overstated. It is also now more important than ever that professionals clearly define the scope and purpose of their advice within letters of engagement and terms of business and that this is kept under review.

### **Any questions**

If you have any questions regarding the insurance-related issues highlighted in this article, please get in touch with Simon or Dean.

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