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**SWAP CONTRACTS AND SCOPE OF DUTY : SAAMCO
REVISITED**

**BEN PATTEN QC
FOUR NEW SQUARE**

SWAP CONTRACTS AND SCOPE OF DUTY : SAAMCO REVISITED

The Court of Appeal's decision in *Haugesund Kommune v Depfa ACS Bank*¹, handed down on the 28th January 2011 is the latest striking application of the legal principles often colloquially referred to as *SAAMCO*². The facts in *Haugesund* were as follows. In 2004 and 2005 two Norwegian municipalities, Haugesund Kommune and Narvik Commune entered into swap contracts with Depfa Bank. The effect of these swap contracts was to allow the Kommunes to use substantial funds advanced by the Bank for investment. However, Section 50 of the Norway's Local Government Act 1992 prohibited borrowing by municipalities save in very limited circumstances. Prior to entering into the swap contracts the Bank had sought the advice of Norwegian lawyers, Wikborg Rein & Co. Wikborg Rein had advised that the swap contracts did not contravene Section 50 and the Bank relied upon that advice. In 2008, having made disastrous investments, the Kommunes asserted that the swap contracts were invalid and declined to make any further payment under them. The contracts were governed by English law and later that year the Kommunes commenced proceedings in the Commercial Court seeking declaratory relief as to their invalidity. Depfa counterclaimed on the basis that if the contracts were invalid it was entitled to restitution of the sums which it had advanced. Depfa also commenced proceedings against Wikborg Rein³, alleging that the latter had been negligent and claiming the monies advanced as damages, albeit it would give credit for monies received.

The action came on for trial in April and May 2009⁴ before Tomlinson J. The issues at trial were all issues of liability (both as to the Kommunes' liability and Wikborg Rein's liability). Issues of quantification of loss were put off to be dealt with at a second trial. The Kommunes succeeded in establishing that the swap options were invalid and unenforceable. However, Depfa succeeded in establishing an entitlement to restitution. Wikborg Rein was found to have advised negligently and the Judge further found that if Depfa had been advised that there was even a risk of the swap contracts being invalid, it would never have entered into them. Judgment was entered against Wikborg Rein for damages to be assessed. The Kommunes appealed but in May 2010 the Court of Appeal upheld the Judge. During the course of this litigation it became increasingly clear that not only were the

¹ [2011] PNLR 14

² *South Australia Asset Management Corporation v York Montague Ltd* [1997] AC 191

³ Although the retainer was governed by Norwegian law and only gave rise to rights and obligations in contract, it was agreed that Norwegian law was the same as English law for all practical purposes.

⁴ An order for expedition having been made

Kommunes unwilling to repay the advances, but because of the losses sustained on their investments, they were probably unable to do so.

In January 2010 Tomlinson J heard the assessment of damages to be paid by Wikborg Rein. The case was fought on the issue as to whether Depfa was required to give credit for its rights of recovery against the Kommunes⁵. Depfa relied upon the principle in *The Liverpool*⁶, to the effect that a person who has suffered loss caused by two parties may sue either and is not required to give credit for his rights against the other. Wikborg Rein relied upon the analysis of recoverable loss in *Nykredit Mortgage Bank Plc v Edward Erdman Group*⁷, contending that when valuing the claimant's loss, account must be taken of the value of the rights it retained (in the case of a lender, being the value of the borrower's covenant). Depfa responded that the Nykredit approach was confined to bringing into account the value of contractual rights. The Judge acceded to Depfa's submissions⁸. He rejected the contention that Depfa's restitutionary rights were to be taken into account. These were not contractual rights and the value ascribed to them, for this purpose, was nil.

The only respect in which the Judge touched upon the issue of scope of duty was when he sought to take comfort from lenders cases where solicitors were found liable for the total loss (*Bristol & West Building Society v Fancy & Jackson*⁹ and *Portman Building Society v Bevan Ashford*¹⁰).

“In both cases of course the court had in mind the scope of duty limitation introduced or underscored by Lord Hoffmann's speech in the *South Australia Asset Management* case. However the context was not that of a wrong valuation where, ordinarily, the consequences of a correct decision would be an advance on different terms. The context was rather that of wrong advice or information where correct advice or information would have led to there being no transaction at all. In both situations the enquiry is at bottom what properly are to be regarded as the consequences of the advice or information being wrong. In the present case Depfa advanced money on the strength of what turned out to be a non-existent promise to repay it by an entity which had no capacity to borrow or to promise to repay. It is to my mind consistent with the approach in these cases to regard Wikborg Rein as responsible for the whole loss arising from the advice, save in so far as that loss has been reduced by recoveries made prior to the point at which the court is called upon to assess the loss. A similar approach is to be found in *Aneco Reinsurance Underwriting Ltd (in Liquidation) v Johnson & Higgins*

⁵ Wikborg Rein conceded that, should the Kommunes' appeal on change of position succeed, it would be liable for the entire loss.

⁶ *The Liverpool No.2* [1963] P.64

⁷ [1997] 1 WLR 1627

⁸ [2010] PNLR 21

⁹ [1997] 4 AER 582

¹⁰ [2000] PNLR 354

*Ltd*¹¹ where brokers failed to advise their clients Aneco that the basis upon which they proposed to enter into a reinsurance was not viable since retrocession was unavailable. They were held liable for the whole of the losses suffered by Aneco consequent upon entering into the reinsurance, not simply the losses which they would have suffered in any event had the retrocession in fact obtained not been voidable and in due course avoided.”

Wikborg Rein appealed and the Court of Appeal (Rix and Gross LJ and Peter Smith J) allowed the Appeal. Having noted that the foundation of Tomlinson J’s judgment was reliance upon the principles set out in *The Liverpool* and that his finding that (in *SAAMCO* terms) this was a case where the adviser was responsible for all the consequences of his negligent advice, the Court first considered the principle established by *The Liverpool*, holding that “the principle..... is not in doubt”. However, Rix LJ stated, the principle did not answer the real question raised by Wikborg Rein’s appeal, namely “whether Depfa’s loss has been properly established against it.” The answer to that question was, he held, to be decided according to whether Wikborg Rein’s duty was to take reasonable care to provide information (a *SAAMCO* category 1 case) or take reasonable care to provide advice (a category 2 case). The competing contentions of the parties were summarised in this way: “Mr Pollock submits that this is a category 1 case, and that Wikborg Rein is not responsible for the Kommunes’ loss of money which had been advanced to them in their disastrous investments. The creditworthiness of the borrower is a risk for the banker, not for the lawyer. Mr Railton, however, submits that this is a category 2 case, so that Wikborg Rein is responsible for the foreseeable consequences as a whole.” Having considered *Nykredit* and noted the statement by Lord Nicholls to the effect that it was not always easy to decide whether particular facts fell into a category 1 or category 2 case, Rix LJ considered the facts of *Aneco*, *Fancy & Jackson*, *Portman Building Society* and the submission by Depfa that Lord Lloyd’s speech in *Nykredit* was authority for the proposition that category 1 cases were exceptions to the basic category of category 2. He provided his assessment of the application of the principles in those cases to the facts:

“In my judgmentthis is a category 1 case. For these purposes I am prepared to assume, with Lord Lloyd in *Aneco*, that category 2 reflects the primary category, and category 1 reflects the exceptional case. Nevertheless, it seems to me that it is difficult to see Wikborg Rein’s duty as being that of a general, as distinct from a specific kind. Wikborg Rein was asked to advise about a specific question, the validity of the proposed swap contracts. It did not have a general retainer to report or notify problems about the proposed transactions. It was not concerned with the creditworthiness of the Kommunes. It warned Depfa that it could not execute a summary judgment against the Kommunes, so that in that, different, sense, its contractual rights could not ultimately be vindicated or, one might say, enforced. In such circumstances, Depfa knew that it ultimately relied on the creditworthiness and good faith of

¹¹ [2002] 1 Lloyds Rep 157

the Kommunes: and on those qualities Depfa made up its own mind and was wholly confident.....¹²

I therefore do not consider Wikborg Rein's retainer to have been of a general kind. It was not like the examples of general retainers which have been considered in the authorities discussed above. Wikborg Rein had no general responsibility to advise Depfa on whether to proceed with the transactions or not. It did not share the same markets, in the way insurers and insurance brokers do. It was not acting as lawyers sometimes do, as *hommes des affaires*. It was giving a specific piece of legal advice.....¹³

The next question was the extent of the loss which fell within Wikborg Rein's scope of duty. Unlike the Trial Judge, Rix LJ thought that the real cause of the loss was not the invalidity of the swap contracts, but the impecuniosity of the Kommunes. The Kommunes had not disputed that, if ordered by the Court to make repayment, they would endeavour to do so. The problem was that they had no means to do so. He analysed the problem this way:

“...unless the law must regard Depfa's loss as having been incurred entirely by the time of the initial transfers, irrespective of all questions of the obligation to make restitution on the one hand and of impecuniosity on the other, then it seems to me that it would be wrong simply to assume, on the basis of the transfer of funds, that there was then and there established loss within the scope of Wikborg Rein's duty.

In my judgment, however, the question of the existence of a loss must essentially be a question of fact. If the law has a role to play, as setting the boundaries within which fact plays its part, then legal principles must seek realistic and, in a commercial setting, commercial results. It seems to me to be a harsh doctrine to visit a loss in fact due to lack of creditworthiness on a solicitor as being within the scope of his duty to advise as to the validity of a transaction, when that creditworthiness has been entirely within the province of the lender and outside the solicitor's duty.”¹⁴

Although some loss might have occurred at the moment of transfer, that loss might be very small. The matter could be illustrated by an example: if the invalidity of the transaction had been discovered before the monies were invested and the Kommunes had offered to repay them, it would have been absurd for Depfa to have pursued Wikborg Rein on the basis that these sums had been lost. Although Depfa had lost its contractual rights at that moment, the restitutionary rights it acquired were valuable. Rix LJ continued: “Mr Railton submits that a merely restitutionary right should not be taken into account, whatever the circumstances. In my judgment, however, there is no reason in principle why it

¹² Paragraph 74

¹³ Paragraph 76

¹⁴ Paragraphs 79 and 80

should not be. The existence of loss and its allocation as being within the scope of a defendant's duty will always be fact sensitive. The law should not create principles, particularly with regard to remedies, which are so inflexible that they lead to unrealistic and uncommercial results. That to my mind is the principle teaching of *Saamco* and *Nykredit*¹⁵. Everything depended on why the Kommunes had not repaid Depfa. If that reason was impecuniosity or the fact that there was no means of taking action against the Kommunes, then the risk was not within Wikborg Rein's scope of duty. In this case the evidence suggested that this was precisely what had happened.

In his concurring judgment Gross LJ concurred with the result, but did not think himself constrained by the categorisation of Wikborg Rein's advice as being category 1:

“...I am unable to accept that Wikborg Rein could be liable for loss relating to enforcement and credit risks, which, as already emphasised, were never assumed by Wikborg Rein. I do not think it can be right – without more – to suppose that the loss suffered by Depfa was within the scope of Wikborg Rein's duty. Even if the contract was valid, Depfa had been advised that it could not enforce a claim against the Kommunes. So far as concerns the credit risk, that was for the bank (Depfa) not its legal advisers..... For these purposes I do not think that it matters whether this is a “category 1” or “category 2” case, losses attributable to enforcement and credit risks were outside the scope of Wikborg Rein's duty.”¹⁶

Is the application of the SAAMCO principles any easier ?

Haugesund is another demonstration of the difficulties encountered in applying *SAAMCO* principle to facts of particular cases. The Trial Judge was clear in his view that the whole loss was recoverable. On the same facts, the Court of Appeal held that none of it was¹⁷. As Lord Nicholls in *Nykredit* noted, the principle of liability is easier to formulate than to apply¹⁸.

The most striking example of this difficulty is *Aneco* where the issue was whether the defendant insurance brokers should be liable for all the consequences of Aneco entering into reinsurance agreements or only those consequences which would have been avoided if reinsurance had been

¹⁵ Paragraph 86

¹⁶ Paragraph 101

¹⁷ Although it is right to note that Wikborg Rein had previously accepted liability for the legal costs of the claim for declaratory relief.

¹⁸ Paragraph 245

available. Aneco was offered a chance to reinsure certain marine risks (the Bullen Treaty) and the broker suggested that Aneco should purchase a measure of excess of loss protection. The broker acted for Aneco in purchasing that further insurance but in so doing misdescribed the Bullen Treaty. Those excess of loss policies were subsequently avoided. Aneco lost \$35 million by entering into the reinsurance contracts, but only \$11 million of this loss was attributable to avoidance. It contended that the brokers had advised that suitable reinsurance would be available and that had the correct advice been given it would not have entered into the transactions at all. The Court of Appeal held that had the underlying risk been properly described suitable reinsurance would not have been available. By a two to one majority they found that the brokers had assumed a duty to advise Aneco what course to adopt rather than merely to place the reinsurance. Fundamental to the conclusion reached by the majority was the finding that the broker's actions were those of advising as to whether Aneco should enter into the transactions and were not confined to the placing of reinsurance. That finding was itself based upon the finding that the advice given was that reinsurance would be available which constituted "a failure to report correctly the current market assessment of the reinsurance risks which Aneco was proposing to undertake"¹⁹. These were risks which were central to Aneco's decision.

The House of Lords agreed with this analysis. It was artificial, said Lord Steyn, to separate out advice as to the risks inherent in reinsurance with the risks inherent in the Bullen Treaty: advising on the former would inevitably have revealed the true position on the latter. However the clearest exposition of the SAAMCO principles is contained in the dissenting speech of Lord Millett²⁰:

- (1) where a plaintiff enters into a loss making transaction in reliance on the defendant's negligent advice, he is not entitled to recover the whole of the loss on the transaction merely because the defendant was aware that he would not have entered into it but for the advice he received. He is liable only for the loss which is due to the advice being wrong.....
- (2) The court does not ask what would have happened if the defendant had performed his duty and stated the true facts (in which case the transaction would not have gone ahead at all). This is not the basis of the defendant's liability.
- (3) The correct measure of damages is not the difference between the loss which has in fact occurred (the loss on the transaction) and the loss which would have occurred if the defendant had performed his duty and stated the facts correctly (which would have been zero since the transaction would not have gone ahead). This would not exclude the loss which ought to be irrecoverable. They are measured by the difference between the loss on

¹⁹ Per Evans LJ at paragraphs 82 to 84

²⁰ A summary subsequently applied by the Court of Appeal in *Andrews v Barnett Waddingham* [2006] PNLR 24

the transaction and the loss which would have been sustained if the facts had been as the defendant represented them to be (when the transaction would still have gone ahead).

- (4) The case is different where the defendant assumed responsibility for advising generally what course of action to take in relation to a particular transaction. But it is necessary to identify the transaction in question, for he is not liable for loss arising from some other transaction even though it may be linked with it, particularly if it called for the exercise of a different professional judgment.
- (5) The defendant's liability is measured by the scope of his duty. Accordingly, where the complaint is that he failed to report or give advice at all on a particular matter, the plaintiff must prove that he was under a legal obligation to do so. It is not enough that he would probably have volunteered the information if asked.²¹

Lord Millett's disagreement with the majority was founded upon both factual and legal divergences. As to the facts, in the course of a close examination of the pleadings and evidence, coupled with concessions made by Aneco, he held that the brokers had neither been asked to advise upon, nor had any duty to advise upon, the merits of the Bullen Treaty. The scope of their duty was confined to advising upon the availability of reinsurance. The legal divergence lay in the last of the principles set out above: it was incorrect, he said, to consider what would have happened if the brokers had advised that the market was hostile towards reinsurance and in particular whether this would have led Aneco to realise that the Bullen Treaty carried unacceptable risks; it was only permissible to look at the advice which the brokers were legally obliged to provide.

Loss or Duty - where does the analysis start ?

There is a degree of "chicken and egg" about whether the Court starts with the scope of duty, or starts with the nature of the loss sustained. Given that the essence of the *SAAMCO* exercise is an analysis of the relationship between the two, it may not matter. As a matter of chronological convenience consideration of the nature of the defendant's duty may precede consideration of the occasioning of loss. Moreover, on one footing analysis of the scope of duty may be dispositive: if the adviser's obligation was to advise generally then, in a proper case, the adviser is liable for all the foreseeable consequences of the advice being negligently wrong, whatever they may be. However, analysis of the scope of duty abstracted from the question of loss is unsatisfactory. It begs the question: "duty to protect the claimant from what?" The underlying question must always be kept in mind: "is this the

²¹ At 223

kind of loss in respect of which a duty is owed?" Both duty and loss need to be considered together and separating them out can give rise to a degree of artificiality. Examination of the authorities reveals that more satisfactory results appear to be produced where the analysis starts with the loss and then moves to a consideration of the scope of duty, rather than vice versa.

Identifying the Cause of the Loss

As Lord Millett said in *Aneco* "there must be a sufficient causal connection between the particular feature of the transaction which occasioned the loss and the subject matter of the defendant's duty of care."

What counts as "a sufficient causal connection" ? *Andrews v Barnett Waddingham*²² illustrate the importance not merely of correctly identifying the cause of the loss, but also of inquiring into whether loss *caused in that way* was within the risk carried by the adviser. Mr Andrews sought the advice of consulting actuaries about transferring his pension to a different scheme. He was particularly concerned about security and asked for written advice that he would receive protection under the Policyholders Protection Act 1975 in the event that any such provider went into liquidation. The defendants obtained a number of quotations, one of which was from Equitable Life. Mr Andrews decided to put his pension into a scheme operated by that company, subject to confirmation of statutory protection. The defendants gave negligent advice as to the level of protection afforded by the Act in relation to the Equitable Life scheme. Had proper advice been given, Mr Andrews would not have invested his pension monies in the scheme. Equitable Life subsequently got into financial difficulties and this had a deleterious effect upon the value of Mr Andrews' pension. Relying on *Fancy & Jackson* the Judge held that the defendants' negligence had deprived Mr Andrews of the opportunity of making a properly informed choice as to the identity of a new pension provider. The Court of Appeal allowed the defendant's appeal. Equitable Life did not go into liquidation and no loss was caused by shortcomings in the protection afforded by the Act. Equitable Life's financial difficulties were the cause of his loss. Richards LJ applied the measure of loss identified by Lord Millett in *Aneco*:

"the correct measure of damages is the difference between the loss sustained by acquiring the Equitable Life with-profits annuity and the loss which would have been sustained if the 1975 Act applied to the annuity as Mr Andrews was advised that it did. That difference, however, is

²² [2006] PNLR 24

nil, since the loss sustained by acquiring the annuity would be unaffected even if the 1975 Act applied in full.

In reaching a different conclusion Cox J reasoned that Mr Andrews should have been told that the 1975 Act did not apply to with-profit annuities in the same way as other annuities because of the fact that in relation to future benefits the protection of the Act is in respect only of the reversionary bonus guaranteed, once declared. If that correct explanation had been given, as it should have been, Mr Andrews would not have purchased the Equitable Life with-profits annuity. The loss was recoverable because it was “inextricably linked to the negligently given information”.....she said that the loss was “caused by Mr Waddingham’s mis-information, because Mr Andrews would never have purchased the policy if he had been correctly informed, and his loss is therefore intimately connected with that feature of the policy, which would have made him decide, had he been properly advised, not to purchase it.”

It seems to me that that line of reasoning amounts to saying that because Mr Andrews would not have entered into the transaction if he had been properly advised about the 1975 Act, he is entitled to recover the loss he has sustained in consequence of entering into the transaction. But that runs directly contrary to *SAAMCO* and *Aneco*. The fact that Mr Andrews would not have entered the loss-making transaction but for the negligent advice is a necessary but not a sufficient condition of liability.

....the judge, in distinguishing the factual situation in *SAAMCO*, stated that “the kind of loss” which had occurred was the same as that against which Mr Andrews wanted protection. In my view that is too broad an approach. It is true that Mr Andrews wanted protection against anything that would threaten the long-term security of his pension. But the negligent advice related to protection conferred by the 1975 Act against the insolvency of the insurance company. The loss that occurred was not that loss.”²³

As demonstrated by *Haugesund* the identification of loss is a matter of commercial reality rather than legal theory. The same loss can often be described in different ways, sometimes depending upon an assessment of when it occurred and sometimes depending upon an assessment of the causal chain necessary to bring it about. As is set out below, some of the lender claims have contributed to the creation of a confusion between the consequences of entering into the transaction and the consequences of the information being wrong. Misdescription of the kind of loss feeds back into the question of whether that loss was within the adviser’s scope of duty and invariably leads to the wrong result. A careful and commercial analysis of the kind of loss, uncontaminated by the need to fit it into a particular legal category is the surest way to avoid this happening.

²³ Paragraphs 43 to 45

Identifying the Scope of Duty

In *SAAMCO* Lord Hoffman approached scope of duty at a high level of abstraction:

“How is the scope of duty determined ? In the case of a statutory duty, the question is answered by deducing the purpose of the duty from the language and context of the statute: *Gorris v Scott*²⁴ In the case of tort, it will similarly depend upon the purpose of the rule imposing the duty. Most of the judgments in the *Caparo* case are occupied in examining the Companies Act 1985 to ascertain the purpose of the auditors’ duty to take care that the statutory accounts comply with the Act. In the case of an implied contractual duty, the nature and extent of liability is defined by the term which the law implies. As in the case of any implied term, the process is one of construction of the agreement as a whole in its commercial setting. The contractual duty to provide a valuation and the known purpose of that valuation compel the conclusion that the contract includes a duty of care. The scope of the duty, in the sense of the consequences for which the valuer is responsible, is that which the law regards as best giving effect to the express obligations assumed by the valuer: neither cutting them down so that the lender obtains less than he was reasonably entitled to expect, nor extending them so as to impose on the valuer a liability greater than he could reasonably have thought he was undertaking.”²⁵

In the now iconic passage which considers the formulation of the *SAAMCO* principle Lord Hoffmann enunciated what has become known as the distinction between category 1 and category 2 advice. However, as is shown by *Haugesund*, that classification is more of a guideline than a complete code. Even where general advice is being provided it is still necessary to inquire whether the loss sustained is a loss for which the adviser is responsible. Moreover, within the same retainer an adviser can provide general and specific advice. A practical example of how the Court approaches the scope of duty is *Johnson v Gore Wood (No.2)*²⁶. In this case the Court of Appeal considered Mr Johnson’s appeal from the decision of Hart J who had decided that certain losses suffered by him were outside of the defendant solicitors’ scope of duty. The solicitors had given negligent advice to Mr Johnson and his company concerning a property development transaction. They then continued to act for him in his efforts to ameliorate his position, negligently advising him that he was in a strong position. He contended that their negligence had caused him to lose certain investments and take on certain extra liabilities, albeit that no advice was given as to particular transactions. The Judge found, although these losses were foreseeable consequences of the solicitors’ breach of duty, some of them were not within the scope of that duty. The Court of Appeal allowed the appeal. Lady Justice Arden commenced her analysis of scope of duty by emphasising its factual sensitivity:

²⁴ [1874] LR 9 Ex.125

²⁵ At 212

²⁶ [2003] EWCA Civ 1728

“To determine the scope of duty the court must examine carefully the purpose for which advice was being given and generally the surrounding circumstances. The determination of the scope of duty thus involves an intensely fact-sensitive exercise. The final result turns on the facts, and it is likely to be only the general principles rather than the final solution in any individual case that are of assistance in later cases.”²⁷

In four respects Lady Justice Arden provided guidance as to those principles. First, as with remoteness, it is the kind of loss and not its size that matters²⁸. Second, the purpose for which the advice is sought may, in an appropriate case, be a general purpose: “if the advice which a solicitor gives is for the general purpose of making investments, it cannot matter that the solicitor does not know what those investments are or the scale of the proposed investment. The court has to ask simply whether the loss that occurred was “the kind of loss in respect of which the duty was owed.... The Court must, therefore, ask for what purpose the advice was given. In some cases it will be sufficient that the purpose can be generally described.” Third, the more emphatic the advice and less it is hedged with qualification and reservations, the more likely it is that a court will be justified in considering that the scope of duty was a broad one²⁹. Fourth, all the circumstances may include consideration of other advice and the role taken by the adviser (the solicitor had given advice on a number of business matters)³⁰. On the facts the Court came to the conclusion that the Judge had been wrong to try to draw a dividing line between certain losses.

Occasionally the authorities suggest the possibility of more rigid guidelines. The distinction between information and advice did cause difficulty until clarified in *Nykredit*. Although Lord Lloyd in *Aneco* appears to have regarded the application of *SAAMCO* as being a narrowly confined to exceptional cases, no subsequent authority has suggested the existence of some presumption against exclusion of loss on a *SAAMCO* footing. Lastly whilst there is support in *SAAMCO*, *Nykredit* and *Aneco* for the proposition that different types of advisers may, by reason of their profession, more readily fall into the respective categories of advisers providing information and advisers providing advice, no case appears to have been decided on this basis. Such overarching guidelines may be of little value in the fact sensitive analysis identified in *Johnson*. Although a solicitor may be instructed on narrow points he may decide to give general commercial advice, if asked to advise generally he may hedge or qualify his advice to indicate a restriction upon his responsibility. An accountant asked to give advice on one aspect of a particular transaction may be expected to advise on other aspects by reason of an

²⁷ Paragraph 91

²⁸ Paragraph 93

²⁹ Paragraph 96

³⁰ Paragraph 96

assumption of a broader responsibility over a long course of dealing. In any particular case, even though the adviser has a general remit, the kind of loss suffered may require a very specific duty to advise. The better view (particularly in the context of a contractual relationship) is that the Court makes a judgment as to the allocation of risk which the parties would reasonably have considered the adviser was undertaking at the time when the advice was given³¹.

Problem Cases

In one of the *Fancy v Jackson* cases (*Steggles Palmer*) a solicitor failed to inform a lender (amongst other things) that the transaction was proceeding by way of sub-sale. The borrower defaulted and Chadwick J found that the solicitors were liable for the whole of the loss. He held that had the lender known the true facts it would not have been willing to lend to this borrower at all and “in those circumstances it seems to me fair and in accordance with Lord Hoffmann’s test, that the defendants should be responsible for the consequences of the society not being in the position to take the decision which it would have taken if the defendants had done what they should have done.” In *Portman Building Society* the borrowers applied for a loan of £168,700 to enable them to purchase a property for £225,000. They said that the balance of the purchase price was coming from their own resources. Unbeknown to the lender, the borrowers proposed to enter into a second charge in favour of the vendor securing £50,000, of the purchase monies. The borrowers made a false declaration, certifying that no further loan was in contemplation. The defendant solicitors failed to advise the lender of these matters. The lenders surveyor valued the property at £225,000. Some two years later the borrowers defaulted. The lender sought to realise its loan and suffered a shortfall (the property being sold for £110,000). The solicitors admitted negligence, but contended (amongst other things) that the only loss within their scope of duty was nominal loss. They argued that the effect of the second charge was merely to ensure that the vendor suffered loss which otherwise would have been carried by the borrowers. It did not affect the lender’s recovery. Had the assertion that there was no further borrowing been true, the lender’s loss would have been exactly the same. The Judge rejected these contentions and the Appeal failed.

Otton LJ held that the consequence of the solicitor’s failure to advise as to the proposed second charge was greater than that contended for by the solicitors. Because of that failure the lender advanced sums

³¹ See Lord Hoffmann’s speech in *Transfield Shipping v Mercator* [2009] 1 AC 61 at paragraph 17.

in the mistaken belief that the borrowers (a) could afford the repayments and (b) were providing honest covenants (as opposed to the covenants of people guilty of fraud). In particular, Otton LJ held:

“Longmore J was correct to follow the reasoning of Chadwick in the application of the *SAAMCO* principle and has the effect that where a negligent solicitor fails to provide information which shows fraud on the part of the borrowers, the lender is entitled to recover the whole of its loss. In other words the whole of the loss suffered by the lender is within the scope of the solicitor’s duty and is properly recoverable.

I am also satisfied that far from being an incorrect application of the *SAAMCO* principle, the decision of Chadwick J. is a proper application of the principle. If the whole of the loss suffered by the lender is within the scope of the relevant duty, he should be entitled to recover the whole of the loss.”³²

In *Haugesund Rix* LJ remarked that little assistance could be derived from *Fancy v Jackson* because each solicitor’s retainer was general rather than specific and each case turned on its own facts. He distinguished *Portman* on the basis that: “It seems to me that it is one thing to fail to advise a lender, where it is within the solicitor’s duty to do so, that a borrower is lying about the equity which he is apparently putting into his purchase and thus his means to support his borrowing, and on the other hand for a solicitor to err as to an honest broker’s capacity to enter into a transaction where the borrower’s ability to repay is entirely a matter for the lender and not the solicitor.” However, neither *Fancy v Jackson* nor *Portman* are easy to reconcile with *SAAMCO*, as understood after *Aneco*. In both cases an important part of the ratio was a finding that, properly advised, the transaction would not have occurred at all, something which is merely a threshold condition rather than a defining quality. In both cases substantial elements of the loss were caused by the diminution in the value of the security – something that neither solicitor could have had within its scope of duty. In neither case is there a very clear analysis of why the solicitor’s scope of duty extends to the entire loss, as opposed to that part of the loss referable to the inadequacy of the borrower’s covenant. Both cases treat reporting as to the borrower’s honesty as if it were tantamount to advising on the merits of the transaction. However, in neither case was the solicitor asked, whether expressly or inferentially, to advise whether the transaction should proceed: the height of its duty was to advise of facts and matters which might lead the lender to take the view that the borrowers were untrustworthy. Whilst it is true that in *Steggles Palmer* the default occurred almost right away, in *Portman* the borrowers met their obligations for two years. They only defaulted when their business failed, the risk of which occurrence was plainly not a risk allocated to the solicitors.

³² Page 356

It is right to note that Otton LJ stated at the start of his judgment in *Portman* that he considered that the answer to the scope of duty point “is to be found in the particular facts of this case”³³. On those facts the solicitors were contending that they were not liable for *any* loss, a contention which was bound to fail. No secondary argument appears to have been advanced concerning loss limited to the value of the borrower’s covenant. On that basis the decision cannot be impugned. However, insofar as the case adopts the more extensive principle found by Chadwick J that “where a negligent solicitor fails to provide information which shows fraud on the part of the borrowers, the lender is entitled to recover the whole of its loss. In other words the whole of the loss suffered by the lender is within the scope of the solicitor’s duty and is properly recoverable” the application of that principle should be very carefully applied. On a true construction of his retainer a solicitor (or other adviser) may agree to bear this element of risk, but evidence of specific allocation of risk should generally be required³⁴.

Looking Ahead

The *SAAMCO* principles are still new (in legal terms) and it would be surprising if their application was not further refined by the Courts.

One area of potential development is the distinction between providing information and providing advice. The allocation of advice (or failures to advise) into boxes marked category 1 and category 2 has proved a blunt tool, as has the distinction between an adviser and a person providing information upon which the client will take a decision whether or not to proceed. The better analysis, it is respectfully suggested, is one which concentrates upon the fair allocation of risk. An analysis which asks, of any specific loss, whether the adviser can fairly be said to have taken legal responsibility for that loss gains in accuracy what it may lose in utility. One advantage of this form of analysis is that it assists in overcoming difficulties which the current guidelines can create. An accountant is asked to advise generally in relation to a particular financial transaction intended to minimise tax. The advice is that the transaction is sound as a tax planning measure, but one potential consequence is that the investment may produce a loss. In fact the scheme has adverse tax consequences as well as producing a loss on the investment. If, as seems likely, the accountant is giving category 2 advice (that is, acting as a general adviser) he bears the consequence of both losses, even though he advised as to the risk of the second. Another example is that of a solicitor tasked with advising the lender, amongst other things, whether the borrower is contributing the deposit from his own resources. Advice is negligently

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³⁴ There is nothing to stop Lenders placing such responsibilities in contract in their instructions to solicitors, or achieving the same result by the imposition of express trusts of the advance monies.

given and the borrower defaults. The lender finds that the security has declined in value and it recovers half of the anticipated value. On one application of the *SAAMCO* principles, the solicitor might be responsible for the whole loss, either on the basis that he is treated as a general advise or, the Court having asked “what is the consequence of the information being wrong?”, because no loss would have been incurred if the borrower had been creditworthy. Neither result seems consonant with the philosophy behind *SAAMCO*.

A second area of potential development concerns the nature of the causal connection between a breach within and the scope of duty and the loss. In *Haugesund* the Court of Appeal refused to admit late evidence which might have demonstrated that some part of the Kommunes’ unwillingness to pay was attributable to the invalidity of the credit swap agreements. It is unclear what would have happened if that evidence had been admitted and accepted. Is a sufficient causal connection established if the breach of duty is only a minor contributory cause? Is the analysis one of the application of classic causation principles (where the answer may be different in contract to that in tort) or is some other analysis appropriate?

The problem can be illustrated by Lord Hoffman’s example of the mountaineer. It is fairly easy to see why the doctor who negligently advised the mountaineer about his knee should be not be liable for an injury which has nothing at all to do with his knee (for example a car crash on the way to the mountain). Similarly if the injury to the knee has a substantial involvement in the accident (giving way at a critical moment when, through an unfortunate chain of errors, the mountaineer was not secured by safety ropes) it is relatively easy to see that the loss is within the scope of duty. However, what of situations where the knee injury plays an unexpected or incidental role in the causation of the loss? Thus, suppose the group of climbers decide to take different routes. The mountaineer, complaining of pain in his knee, leaves the others to take what he thinks to be the more difficult route. On his own he gets into difficulties (he is unable to hold a particular rope for long enough whilst he reaches for a hold) and with no one to help him, falls. Is that loss within the scope of the doctor’s duty? Take another example. Towards the end of the day the mountaineer finds his knee is troubling him and as a result he lags behind the others a little. An avalanche occurs. It misses the others but strikes the mountaineer who is injured. Is that loss within the scope of duty? If there is a different result between the two examples, on what basis is the demarcation to be made?

It may be that in looking for a sufficient degree of causal connection it is necessary to revert to the question of precisely what advice was given and (more particularly) what risk did the adviser adopt.

This can be tested by asking whether it would matter in either of the above examples if the doctor had been asked to advise generally as to whether the mountaineer was sufficiently fit to climb. Suppose that whilst negligently advising that there was no problem with the knee, he had correctly advised that the mountaineer was not physically fit and might have difficulty with his grip or with keeping up. If the advice was of that nature it is difficult to see how the consequences of the accident could properly be attributed to the doctor's error. More importantly if the advice is described in terms of the harm which was foreseen, the analysis becomes easier. Advice that the knee should be strong enough to enable the mountaineer to climb safely excludes responsibility for the risk of harm caused when the mountaineer is not climbing (or, at least, harm directly caused by the knee failing in the process of mountaineering). Advice that the knee should not cause any trouble at all and that there is no risk of the mountaineer being impeded would, on its face, be an acceptance of the risk of the kinds of harm set out in the examples. Of course in real life the advice given may not be specific to that degree: the Court may have to interpret the advice in its context to ascertain the extent to which it was advice which accepted the risk of the harm suffered. In that analysis, particularly in a commercial context, Lord Millet's fifth proposition in *Aneco* may be apposite: "where the complaint is that he failed to report or give advice at all on a particular matter, the plaintiff must prove that he was under a legal obligation to do so. It is not enough that he would probably have volunteered the information if asked."

Conclusions

Haugesund marks a small step in the development of the law on *SAAMCO*. It emphasises the importance of comparing the way in which the loss was caused with what it was that the adviser was asked to do and it underlines a gradual development away from a rigid application of guidelines based on categories of adviser, towards a more subtle examination of the role of particular advice.

Ben Patten QC

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Four New Square
Lincoln's Inn