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You Swynson, you lose some

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Lowick Rose LLP (in liquidation) v Swynson Limited and Another [2017] UKSC is a decision of the Supreme Court which was handed down on 11 April 2017. It is the latest in a line of so called ‘transferred loss’ cases - where the courts have grappled with the question of when a claimant in an action for breach of contract can recover damages for a loss which has been suffered not by them but by a non-party.

The Supreme Court’s predecessor, the House of Lords, last considered such a case some 17 years ago. That was, of course, Alfred McAlpine Construction Limited v Panatown Limited [2000] UKHL, 43 which features a majority decision, a majority subtly divided in its reasoning, and judgments running to 74 pages. It is (or was), therefore, a case much beloved of academics and the setters of exam papers.

In the Lowick Rose case Lords Sumption and Mance dealt with a transferred loss problem rather more succinctly.

The Albazero

The general rule is that a claimant can only recover loss which he has himself suffered. An exception was recognised in cases concerning the carriage of goods by sea. A shipowner contracts with a shipper to carry goods from one place to another. The shipper sells the goods while they are in transit, whereupon risk and ownership passes to someone else, who may sell them on again to someone else, and so on. The goods are damaged or lost. Whomever owns the goods at that time has no contract with the shipper. The shipper has a contract with the shipper but has suffered no loss, because he no longer owns the goods, and they are no longer at his risk. In such a case, the shipper can sue the shipowner to recover for the loss which has been suffered by the third party consignee, and will be accountable to the consignee for the damages recovered. In Albacruz (Cargo Owners) v Albazero (Owners) [1977] AC 774, 847 Lord Diplock described the exception in these terms:

“in a commercial contract concerning goods where it is in the contemplation of the parties that the proprietary interests in the goods may be transferred from one owner to another after the contract has been entered into and before the breach which causes loss or damage to the goods, an original party to the contract, if such be the intention of them both, is to be treated in law as having entered into the contract for the benefit of all persons who have or may acquire an interest in the goods before they are lost or damaged, and is entitled to recover by way of damages for breach of contract the actual loss sustained by those for whose benefit the contract is entered into.”

St. Martins

Linden Gardens Trust v Lenesta Sludge Disposals Limited and others and St. Martins Property Corporation Limited and others v Sir Robert McAlpine & Sons Limited [1994] 1 AC 85 comprises conjoined appeals, only the second of which is of interest.

St. Martins Property Corporation Limited (the “Corporation”) was a wholly owned subsidiary of St. Martin’s Holdings Limited which was itself wholly owned by the state of Kuwait. Corporation agreed to develop a site owned by a local authority. The local authority contracted to grant Corporation a 150 year lease of the site once the development was completed. Corporation retained Sir Robert McAlpine & Sons Limited (“McAlpine”) to carry out the works. The contract contained a prohibition against assignment.

Before the works were completed “a scheme was implemented for tax reasons” whereby Corporation assigned its rights under the agreement with the local authority, and purported also to assign its rights under the contract with McAlpine, to another wholly owned subsidiary of St. Martins Holdings called St. Martin’s Property Investments Limited (“Investments”).

Practical completion of the works took place in 1980. In 1981 part of the development was found to be defective. Remedial works were carried out at Investments’ cost. Corporation and Investments brought a claim against McAlpine for the cost of the remedial works.

Investments had no rights as against McAlpine, because the assignment to Investments was ineffective, it being prohibited by the building contract. As for Corporation, it had suffered no loss since it had no interest in the affected property, having transferred its interest to Investments before the defective work was ever done.

Their Lordships held that Corporation could, nonetheless, recover substantial damages by analogy with The Albazero. The following is from the judgment of Lord Browne-Wilkinson, with whom all the other judges agreed:

“The contract was for a large development of property which, to the knowledge of both Corporation and McAlpine, was going to be occupied, and possibly purchased, by third parties and not by Corporation itself. Therefore it could be foreseen that damage caused by a breach would cause loss to a later owner and not merely to the original contracting party, Corporation. As in contracts for the carriage of goods by land, there would be no automatic vesting in the occupier or owners of the property for the time being who sustained the loss of any right of suit against McAlpine. On the contrary, McAlpine had specifically contracted that the rights of action under the building contract could not without McAlpine’s con-
sent be transferred to third parties who became owners or occupiers and might suffer loss. In such a case, it seems to me proper, as in the case of the carriage of goods by land, to treat the parties as having entered into the contract on the footing that Corporation would be entitled to enforce contractual rights for the benefit of those who suffered from defective performance but who, under the terms of the contract, could not acquire any right to hold McAlpine liable for breach. It is truly a case in which the rule provides ‘a remedy where no other would be available to a person sustaining loss which under a rational legal system ought to be compensated by the person who has caused it.’

Lord Griffiths, however, suggested that the same result could also be justified on what has become known as the “broader ground”. This was that the developer had himself suffered the loss because he had his own interest in being able to give the third party the benefit that the third party was intended to have. He could recover the cost of rectifying the defects because it represented what the developer would have to spend to give the third party that benefit, even though he had no legal liability to spend it. On the broader ground, the principle would not be confined to cases where the loss related to transferred property.

### Darlington v Wiltshier

In Darlington Borough Council v Wiltshier Northern Ltd. [1994] EWCA Civ 6 a local authority had entered into an agreement with a finance company under which the finance company was to have a building constructed on a site owned by the local authority. Pursuant to the agreement the finance company engaged a contractor to construct the building. The contractor was aware that, although its contract to build the building was with the local authority, the building was actually being constructed for the local authority. The building was defective. The finance company assigned to the local authority all rights and causes of action which the finance company had against the contractor. The Court of Appeal found that the local authority was able, as assignee, to recover substantial damages from the contractor under the Albazero principle, notwithstanding that the property had not been “transferred from one owner to another after the contract has been entered into and before the breach which causes loss or damage”.

### The Harmon case

Harmon CFEM Facades (UK) Ltd v The Corporate Officer of the House of Commons [1999] EWHC Technology 199 is a first instance decision which provides a useful illustration of a common transferred loss-type problem. The case concerns the construction of Portcullis House, a government office building which, at the time was one of the most expensive buildings ever to be built in London. The new building was to have a bombproof façade, (according to the judgment) meant that it would be “the most expensive fenestration system ever built”. A picture of portcullis house, showing its distinctive windows, is below.

The corporate officer of the House of Common (“H of C”) awarded the fenestration contract for Portcullis House to a company called Seele Alvis Fenestration Ltd. A company called Harmon CFEM Facades (UK) Ltd. (“Harmon”) had tendered for the same contract and complained that H of C was not entitled to award the contract to Seele Alvis, but should instead have awarded the contract to Harmon, under the law relating to public procurement contracts. Harmon succeeded in this argument, and so the question arose as to what damages Harmon should be awarded. If Harmon had been awarded the contract, it would have subcontracted much of the work to other companies within the same company group. Much of the profit from the contract would have been earned by those other group companies, not by Harmon. It is not really clear from the judgment, but such arrangements often reflect some kind of transfer pricing - where profits are pushed into those group companies in which the profits will attract the least tax liability.

Could Harmon claim for a loss of profit which had been suffered not by Harmon but by its associate companies? HHJ Lloyd referred to St. Martin and Darlington v Wiltshier and held that Harmon could recover for this “intra group margin”. Despite it being only a first instance decision, the case is a useful one, and is frequently cited in arbitrations as an authority in support of claims to recover such intra group profits.

### The Panatown case


Historically, the UK had applied a zero rate of VAT to the construction of such buildings. In 1988, however, the European Court of Justice held this was in breach of the UK’s obligations with respect to the harmonisation of such taxes (Commission of the EC v UK Case 416/85 [1988] ECR 3127). As a result the UK enacted legislation which meant that, from 1 April 1989, the zero rating was only
to apply to the construction of dwellings. The effect would be to increase very considerably the cost of contracts for other construction work which were entered into after that date.

UIPL was not going to be able to appoint a contractor before the 1 April 1989 deadline. HMRC agreed, however, that any payment which Unex made to a company outside the Unex VAT Group in connection with the construction project before the 1 April 1989 deadline would be zero rated.

Panatown was outside the Unex VAT group. So Unex borrowed £7.5 million from Barclays Bank, with the stated purpose of the loan being to assist with prepayment of a building contract, and paid the money over to Panatown before the 1 April 1989 deadline. At the time the relevant VAT rate was 17.5%, so this move presumably will have allowed Unex to avoid £1,312,500 of VAT.

Deals within the Unex Group were rather informal, and so it was far from clear what obligations Panatown had undertaken in return for the receipt of this money. It would later be determined that Panatown’s obligation was only to procure construction of the development - i.e. an obligation just sufficient to pass the threshold required to secure the VAT saving (that the payment be for the purpose of the construction project). Panatown did not owe the other Unex group companies any detailed obligations, though, as to (say) the form which the development was to take or the time for completion.

In November 1989 Panatown retained Alfred McAlpine Construction Limited (‘McAlpine’) to build the offices, for a contract price of just under £10.5 million with a Completion Date of 24 July 1991.

At the same time, McAlpine executed a “duty of care deed” (‘DCD’) in favour of UIPL, which was to own the building. The DCD was a short document, in which McAlpine warranted that it had and would continue to exercise reasonable skill and care, and acknowledged that it owed UIPL a duty of care. The DCD was thus markedly different from the building contract, which imposed much stricter and more detailed obligations on McAlpine.

The construction work overran. Over a year after the contractual completion date had passed, on 4 September 1992, Panatown purported to terminate the construction contract and took possession of the site. Panatown claimed that such work as McAlpine had done were so defective that they largely needed to be demolished and rebuilt. The cost of repair was initially estimated at £7 million. But, by the time that the case reached the House of Lords, Panatown was estimating the total cost of rebuilding plus losses due to the consequential delay at £40 million. Here is a picture of (we believe) the office building which was eventually constructed on the site.

On 8 July 1992 Panatown began an arbitration claim. McAlpine argued that Panatown’s claims were doomed to fail because Panatown had suffered no loss. Panatown did not own the property which was said to be defective, and McAlpine’s breaches had not placed Panatown in breach of any obligations it owed the other Unex group companies.

The question of whether Panatown’s claims failed because Panatown was not the owner of the property was heard as a preliminary issue. The arbitrator determined that issue in Panatown’s favour. The arbitration agreement allowed appeals on the merits, though, and so in 2000, eight years after the arbitration began, the case worked its way through the appellate courts and eventually came before the House of Lords, where their Lordships found in favour of McAlpine by a majority.

The Albazer exception was based upon an assumed intention that the contracting party was to be treated in law as having contracted for the benefit of the third party. In Panatown, no such intention could be inferred because in their contractual scheme the parties had instead provided for the third party (UIPL) to have rights directly against McAlpine under the duty of care deed. Lord Griffiths’ ‘broader ground’ did not apply for the same reason. Panatown could not be said to have suffered anything more than nominal damages.

There was majority support (Lords Goff, Millet and Browne-Wilkinson) for the view that Lord Griffiths’ wider principle is correct.

Note, incidentally, the following passage from the judgment of Lord Clyde (in the majority) which seems to support the use of the transferred loss exceptions in cases like Harmon:

“The problem which has arisen in the present case is one which is most likely to arise in the context of ... the commercial affairs of a group of companies. How the members of such a group choose to arrange their own affairs among themselves should not be a matter of necessary concern to a third party who has undertaken to one of their number to perform services in which they all have some interest. It should not be a ground of escaping liability that the party who instructed the work should not be the one who sustained the loss or all of the loss which in whole or part has fallen on another member or members of the group. But the resolution of the problem in any particular case has to be reached in light of its own circumstances. In the present case the deci-
sion that Panatown should be the employer under the building contract although another company in the group owned the land was made in order to minimise charges of VAT. No doubt thought was given as to the mechanics to be adopted for the building project in order to achieve the course most advantageous to the group. Where for its own purposes a group of companies decides which of its members is to be the contracting party in a project which is of concern and interest to the whole group I should be reluctant to refuse an entitlement to sue on the contract on the ground simply that the member who entered the contract was not the party who suffered the loss on a breach of the contract. But whether such an entitlement is to be admitted must depend upon the arrangements which the group and its members have decided to make both among themselves and with the other party to the contract. In the present case there was a plain and deliberate course adopted whereby the company with the potential risk of loss was given a distinct entitlement directly to sue the contractor and the professional advisers. In the light of such a clear and deliberate course I do not consider that an exception can be admitted to the general rule that substantial damages can only be claimed by a party who has suffered substantial loss.”

A post-mortem of Panatown


“What conclusions can we draw from this survey of some of the issues raised by the litigation between Panatown and McAlpine? The first is that it is much simpler, if not so intellectually stimulating, to pay your taxes as and when they fall due.”

Mirant

Mirant Asia Pacific Construction (Hong Kong) Limited v Ove Arup and Partners International Limited [2007] EWHC 918 (TCC) concerned a complex set of contracts for the engineering and construction of a coal fired power station in the Philippines. During construction certain foundations failed and remedial works had to be carried out. The engineers who had designed the foundations were the subject of a claim. The court held that Arup had breached a duty owed to a party called CEPAS which had employed Arup, but owed no duty to CEPAS’s sister company SCC. The question then arose as to whether CEPAS could recover in respect of losses which had been suffered by SCC. Applying Lord Griffiths’ “wider principle” the court held (paragraph 628):

“CEPAS may in principle recover damages in respect of losses caused to SCC as a consequence of the breach of contract by Arup because it did not receive from the defendants the performance of the bargain which it contracted for, namely that Arup failed to provide adequate designs for use by SCC on site and failed to verify the design assumptions.”

The case is an example of Lord Griffiths’ wider principle being applied, in a case where the third party’s loss was not said to have resulted from a transfer of property.

Saga Cruises

In Saga Cruises BDF Limited and Others v Fincantieri SpA [2016] EWHC 1875 (Comm) shipowners contracted with a yard for repair and refurbishment of a cruise ship called the “Saga Sapphire”.

The owners chartered the ship to a related company called Acromas. The ship’s first voyage post-refurbishment had to be abandoned because of a defect in the ship’s engines, which it was alleged would have been detected and remedied if the work had been done to the required contractual standard.

The resulting loss was suffered not by the owners but by Acromas. Could the owners recover for Acromas’s loss?

In the event the court held that, even if the work had been done to the required standard, the relevant defect would not have been detected and so the claim failed. The judgment does, however, contain an obiter passage about the transferred loss issue (paragraphs 221 to 222, 225 and 226).

“Chitty (paragraph 18-058) concludes that the effect of Darlington is to extend Linden Gardens so that at least in the context of defective performance of building contracts a transfer of the property affected by the breach to the third party is no longer required.

Acromas say that Darlington is analogous to the present case and rely on the evidence of Mr Rizzo that the Yard was aware that the purpose of the Works was for the Vessel to be used in Saga’s cruise business – in essence, by Acromas.”

“... given the essential nature of this contract – construction/engineering - the use of the Albazero exception as extended into Darlington does not seem impermissible. Further the factual set up of this contract, as confirmed by the evidence of Mr Rizzo, is that the whole purpose of the Works was to equip the Vessel for cruise operations and the Yard would expect any losses suffered by the Owners to be felt by the Owners’ cruise operating arm, not the Owners themselves. This brings the scenario to a very close parallel with the Darlington case.”

“... it seems that with Acromas being the contemplated operator of the Vessel, the Contract was indeed essentially for Acromas’ benefit.

Therefore were the point to arise, I would find for the Owners.”
Lowick Rose

In Lowick Rose a transferred loss problem again arose (at least in part) as a result of an attempt by a businessman called Michael Hunt to reduce the tax liabilities of a company which he owned. Lord Sumption gave the first judgment in Lowick Rose. He began:

“The distinct legal personality of companies has been a fundamental feature of English commercial law for a century and a half, but that has never stopped businessmen from treating their companies as indistinguishable from themselves. Mr Michael Hunt is not the first businessman to make that mistake, and doubtless he will not be the last.”

We know from the outset, then, that this is not going to end happily for Mr Hunt.

Management buyout

The case concerns a management buyout of a US company called Medical Industries America Inc. trading as “Evo”, a manufacturer of aspirators, inhalers and similar medical equipment.

Evo’s management team wanted to buy out Evo’s owners but needed funding. They approached a wealthy investor called Michael Hunt. He decided that he wanted to finance the transaction through his wholly owned company “Swynson”.

The transaction worked as follows:

(a) An English company was created called Evo Medical Solutions Limited (“EMSL”). EMSL’s shares were owned 71.4% by Evo’s management, 25% by Mr Hunt and 3.6% by an associate of Mr Hunt who joined its board.

(b) Swynson borrowed £15 million from Credit Suisse, guaranteed by Mr Hunt and secured on his assets.

(c) Swynson loaned £15 million (the “2006 Loan”) to EMSL. This loan carried interest at 6% above base rate payable monthly and was repayable on 31 October 2007. EMSL was also required to pay a £750,000 “arrangement fee”. Swynson took charges over EMSL’s assets and personal guarantees from the management team.

(d) EMSL acquired the entire share capital of Evo.

Before entering this transaction Swynson and EMSL jointly instructed a firm of accountants called Hurst, Morrison & Thompson ("HMT") to carry out due diligence on Evo. HMT’s engagement letter limited its liability to £15 million. HMT subsequently changed its name to “Lowick Rose”, but it is always referred to as HMT in the judgments. HMT’s report was negligent in that it failed to draw attention to some problems with Evo’s finances. If HMT had carried out their task properly the transaction would not have gone ahead.

2007 Loan

In 2007 Evo began to suffer cash-flow problems and EMSL began to default on its interest payments due to Swynson on the 2006 loan.

On 13 August 2007 Mr Hunt caused Swynson to lend EMSL a further £1.75 million (the “2007 Loan”). Interest was set at 5.5% above base rate with a facility fee of £2,400 per month. The 2007 Loan was to be repaid, like the 2006 Loan, on 31 October 2007.

2008 Loan

EMSL failed to repay the 2006 and 2007 Loans on 31 October 2007 when they fell due. Interest and arrangement fees continued to accrue. Evo continued to make a loss.

On 4 June 2008 Mr Hunt caused Swynson to make a further loan of £3 million to EMSL (the “2008 Loan”). Interest was LIBOR +1.5% with an exit fee of 2% per annum from drawdown to repayment. The date for repayment was 31 May 2010. At the same time Mr Hunt’s interest in EMSL was increased from 25% to 85%.

Refinancing

Mr Hunt now owned Swynson and had a majority interest in EMSL. This created a problem, because it made Swynson and EMSL connected companies. This meant Swynson would have to pay tax as if it were receiving interest payments due from EMSL even though EMSL continued to default on these payments.

On 31 December 2008 Mr Hunt personally loaned £18.663 million to EMSL. The loan was interest free, although there was a provision for default interest. It was a term of the loan agreement that EMSL would use this money to pay Swynson, paying off the 2006 and 2007 Loans in full but leaving the 2008 Loan of £3 million outstanding.

Evo’s business did not recover. Swynson and Mr Hunt brought a claim against HMT for damages of £16.157 million, being the principal amount of all the loans (£19.75 million) less £265,798 which had been recovered under the management’s personal guarantees and £1.355 million which had been recovered from cash and assets in the hands of Evo.

Trial

At trial HMT conceded that it had owed a duty of care to Swynson. HMT also conceded that its advice had been in breach of contract and negligent. The court found that only the 2006 loan had been made on the strength of HMT’s advice, but that losses arising from the 2007 and 2008 loans were in principle recoverable as the cost of reasonable steps taken in mitigation, subject to an overall cap of £15m agreed in the letter of engagement.

HMT denied, however, that it owed any duty of care to Mr Hunt. The court agreed.

HMT argued that Swynson had suffered no loss by reason of having made the 2006 and 2007 Loans, and could recover nothing in respect of those loans, because EMSL had repaid those in full. In response, Swynson and Mr Hunt raised three arguments:
(a) the December 2008 refinancing was res inter alios acta and did not affect the amount of Swynson’s recoverable loss;
(b) Swynson was entitled to recover on the principle of transferred loss;
(c) HMT having been unjustly enriched by Mr Hunt’s provision of funds to EMSL to repay Swynson, Mr Hunt was subrogated to Swynson’s claims against them.

At first instance, the judge accepted the first of these arguments. She held that the repayment was not something Swynson had done in the ordinary course of its business in order to mitigate the consequences of HMT’s negligence, applying Viscount Haldane’s test of mitigation from British Westinghouse Electric & Manufacturing Co Ltd v Underground Electric Railways Co of London Ltd [1912] AC 673 at 689.

Swynson was therefore awarded damages of £15 million.

Court of Appeal

The Court of Appeal held by a majority that the judge had been right and the refinancing was res inter alios acta. They dismissed the appeal on that basis.

Supreme Court

Their Lordships allowed the appeal. They held that the refinancing was not res inter alios acta, that Swynson was not entitled to recover under the principle of transferred loss and that HMT had not been unjustly enriched.

Lord Neuberger described the principle of transferred loss in these terms:

“The principle of transferred loss arises where there is a contract between A and B relating to A’s property which is subsequently acquired by C, and the principle enables A to recover damages for B’s breach of contract which injures the property, even though the loss flowing from that injury is suffered by C and not by A. Self-evidently, it is an anomalous principle bearing in mind the well-established conventional rules relating to recovery of damages for breach of contract, namely that, subject to the terms of the contract, scope of duty, foreseeability and mitigation, A can only recover damages in respect of loss which A suffers as a result of B’s breach of contract. For that reason, the principle should only apply in defined and limited circumstances”.

Lord Neuberger explained the narrower form of the principle as applying when:

“(a) at the time of making the contract with A, B would reasonably have anticipated that A would transfer the property to a person such as C and that that person would suffer loss if B breached the contract, so that the contract can be seen as having been entered into by B partly for C’s benefit, and (b) there is nothing in the contract or the surrounding circumstances which negates the conclusion that the principle should apply.”

Note that Lord Neuberger considers the narrower form is predicated upon an anticipated transfer of ownership - something which was not present in any of Darlington (where the finance company recovered for defective work to a property which was owned by the local authority throughout), Harmon (which does not concern defective property at all), Panatown (where, but for the DCD, it seems Panatown would probably have recovered for defective work to a property which was owned by UIPL throughout), Mirant (where the power station ever changed hands) and Saga (where the ship never changed hands).

With respect to the broader principle Lord Neuberger said:

“… it is fair to say that the Panatown decision leaves a number of points open in this difficult area. One of those points is the correctness of another version of the principle, which was first articulated by Lord Griffiths in Lenesta Sludge, namely that B could be liable if A retains an interest in B performing his obligations, even though A has transferred away the property. However, it is unnecessary to address that point in this case, because it plainly could not apply in this appeal: following repayment of the original loan, Swynson cannot sensibly claim to have retained an interest in the performance of HMT’s duties.”

Lord Sumption said of the broader principle:

“Like others before me, I consider that there is much to be said for the broader principle. But it is not necessary to decide the point on this appeal because it is plain that the principle cannot apply in either form to the present facts …”

Lord Mance showed less enthusiasm for the broader principle, saying:

“Potential difficulties about the theory of performance interest are that it cannot prima facie embrace consequential losses suffered by the company actually (as opposed to contractually) interested in the quality of the property or services and that it is not clear whether or on what basis the company contractually entitled may be liable to account to the company actually interested …”

Lord Sumption stressed the qualification to the principle of transferred loss which is to be derived from Panatown:

“It is, however, important to remember that the principle of transferred loss, whether in its broader or narrower form, is an exception to a fundamental principle of the law of obligations and not an alternative to that principle. All of the modern case law on the subject emphasises that it is driven by legal necessity. It is therefore an essential feature of the principle that the recognition of a right in the contracting party to
recover the third party’s loss should be necessary to give
effect to the object of the transaction and to avoid a “legal
black hole”, in which in the anticipated course of events the
only party entitled to recover would be different from the only
party which could be treated as suffering loss. ... it is not
available if the third party has a direct right of action for the
same loss, on whatever basis.”

All their Lordships agreed that neither the narrower nor the
broader principle allowed Swynson to recover for Mr Hunt’s loss.
Per Lord Mance:

“Neither the narrow or the broad version of the transferred
loss principle is in my view of assistance to Swynson. As to the
narrow principle, it is clear that Swynson did not contract
with HMT on behalf of or for the benefit of Mr Hunt. As to the
broad principle, even if accepted, I do not see how it can ap-
ply in circumstances where Swynson itself suffered loss
through being induced to support the management buyout by
lending to EMSL, but the loan was ultimately repaid by EMSL.
This is not a case where Swynson had any performance inter-
est other than being indemnified in respect of the loss which
it incurred in lending moneys to support the management
buyout. That performance interest has been satisfied. The
fact that it was satisfied by Mr Hunt making moneys availa-
ble to EMSL to repay Swynson does not bear on or expand
Swynson’s performance interest.”

Per Lord Sumption:

“... the relevant duty was owed to Swynson but the loss has in
the event been suffered by Mr Hunt. Since Mr Hunt did not
suffer his loss in his capacity as the owner of property, only
the broader principle of transferred loss could be relevant to
his case. ... it is plain that the principle cannot apply in either
form to the present facts. The reason is that it was no part of
the object of the engagement of HMT or indeed of any other
aspect of the 2006 transaction to benefit Mr Hunt. That is the
main reason why no duty of care was owed to him. ... Mr
Hunt’s loss arises out of the refinancing of December 2008,
which had nothing to do with HMT and did not arise out of
their breach of duty.”

Per Lord Neuberger:

“... following repayment of the original loan, Swynson cannot
sensibly claim to have retained an interest in the performance
of HMT’s duties.

I consider that the transferred loss argument on this appeal
suffers from two defects. First, this cannot be said to be a
case of injury to an asset or property which came into the
hands of Mr Hunt, because the loss suffered by Mr Hunt is not
the same as the loss which would have been suffered by
Swynson if the new loan had not led to the original loan being
redeemed. The losses may be very similar in nature (non-
repayment of a loan made to EMSL), in cause (EMSL’s finan-
cial problems), and in quantum (as the new loan was very
similar in amount to the original loan and identical to the
extent that it was used to pay off the original loan). However,
Mr Hunt has suffered loss in relation to the new loan whereas
Swynson would have suffered a loss in relation to the original
loan.

Secondly, the principle cannot apply because, at the time
HMT were advising Swynson, it was not reasonably foreseea-
ble that Swynson would have the original loan repaid through
the medium of a fresh loan made to EMSL by a third party. Of
course, as with most financing arrangements, it was reasona-
ably foreseeable that some sort of subsequent re-financing of
EMSL might happen one day, but that is not enough in order
for the principle to apply. If it is to apply, Swynson would have
to go further and demonstrate that it was anticipated that
some such refinancing would occur, so that a person such as
Mr Hunt, the new lender, can fairly be said to have been an
intended beneficiary of Swynson’s contractual rights against
HMT. That seems to me to be an untenable proposition in this
case.”

Conclusions

From Lowick Rose it can be seen that the “narrow ground” un-
doubtedly exists but may be confined to cases where there is a pre-
contract anticipation of transfer of ownership. Whether the “broad
ground” exists remains something of a mystery, but Lord Sumption
at least seems to think it has merit.

When drafting contracts and structuring deals we must always
ask: “if the other side does not perform, who suffers?” If the answer
is that it will be someone other than the contracting party then
there are (at least) three possibilities:

(a) Expressly provide in the contract that it is entered for the ben-
efit of the third party, and that the third party will be entitled
to enforce it against the contractor under the Contracts (Rights
of Third Parties) Act 1999. I have yet to see any contract
where this has been done. Every contract seems to exclude the
C(RTPA) 1999.

(b) Have the contractor provide a collateral warranty to the third
party, warranting that the contract has been performed. If the
identity of the third party is not yet known, include in the con-
tract a power to require that the contractor provide such a
warranty. Ensure the warranty is back-to-back with the con-
tract (i.e. is in the same terms, rather than imposing a weaker
obligation like the DCO in Panatown).

(c) Make clear to the other party (e.g. in the recitals to the con-
tract) that the property which the contract concerns is anti-
pated to be transferred to someone such as the third party, so
as to bring the case within the narrow version of the trans-

ferred loss principle.

(d) Expressly provide in the contract that the contracting party will be entitled to recover the relevant losses on behalf of the third party.

It is worth bearing in mind that these no-loss problems tend to arise when deals are structured with an eye to minimising tax liabilities, so that the anticipated profit from a transaction will be enjoyed by someone other than the contracting party. Company A contracts to supply Company B with (say) a piece of mining machinery. Unbeknownst to Company A, Company B has structured its affairs such that it will inevitably make almost no profit from the sale of the minerals extracted by the machine. Rather, it has contracted to sell them for very little profit to a related company in a low tax jurisdiction and it is that company which stands to enjoy any profit. This all seems like a good idea at the time, but when the machine doesn’t work, Company B may have a hard time proving and recovering its loss.

Lowick Rose illustrates a further issue to be alert to when re-structuring obligations. Namely that, if the original structure / transaction was entered into in reliance on negligent professional advice one should try to ensure that the resulting loss is retained by the party which has a contractual nexus with the professional, and not transferred into some third party.

The rule of English law - why Brexit, however blindly foolish it is, should not matter for arbitration

by Melanie Willems

In June 2016, before the referendum on whether the United Kingdom should leave the European Union, Emmanuel Macron - then the minister in charge of the French economy - said this:

“Leaving the EU would mean the ‘Guernseyfication’ of the UK, which would then be a little country on the world scale. It would isolate itself and become a trading post and arbitration place at Europe’s border.”

A year later, on 19 June 2017, the negotiations between the ‘Brexit’ representatives of the United Kingdom government and their EU counterparts have now started. The wider implications of the United Kingdom leaving the EU remain uncertain. In this article, we do not propose to consider the benefits (if any) or disadvantages of Brexit, but ask whether Emmanuel Macron was right to suggest that whatever shape Brexit will take, England would still remain a centre for arbitration.

In short, we agree with the French President. Whichever way you look at it, Brexit should be irrelevant to the success of English law in international commerce, and in dispute resolution in particular. In this article, we explain why we think that Brexit will do nothing to make English law and London any less attractive for resolving disputes in international contracts through arbitration. In doing so, we also take the opportunity to review a couple of recent decisions on arbitration agreements and contract interpretation under English law - illustrating that Brexit ought not change the legal position in England at all.

Rule Britannia?

While the nostalgic notions of British Empire which seemed to surface from time to time in the context of the United Kingdom’s exit from the EU are perhaps questionable, there is at least one area where England still rules. English law is pre-eminent in international commercial contracts. It is frequently chosen by parties to transactions or projects that have little or no connection with the United Kingdom. Statistical evidence supports this:

- In 2008, English law was accepted as most prevalent in cross-border matters by 59% of respondents in a survey of 100 multi-national businesses.
- In 2010, English law was the preferred choice in around 40% of corporate contracts that provided for arbitration (Queen Mary University Survey, 2010: ‘Choices in International Arbitration’).
- In 2016, English law was the preferred choice in 48% of cross-border transactions involving Singapore (Singapore Academy of Law Survey, 2016).

London also continues to be a hub for dispute resolution, and has been the most popular seat for international arbitrations worldwide for some time now.

- In Queen Mary University’s 2015 survey, 45 per cent of participants named London as the most preferred and widely used venue. 50 per cent more participants put London in first place in 2015 than did in the previous survey, in 2010.
- In 2016, the LCIA reports that more than 80% of parties are from outside the UK, and that this is increasing.

The English Commercial Court recorded that, over the period from 31 March 2012 to 1 April 2013, almost 81% of cases before it involved a foreign party, and around 49% of cases were entirely between foreign parties.

Arbitration in England is unaffected

All these surveys were of course carried out before the June 2016 referendum. Since then, the English legal profession has considered the likely impact of Brexit, and there is no shortage of publications commenting on it. To give one example, in January 2017 the Commercial Bar Association’s arbitration sub-group published a Brexit report. It concluded that:

“There is no substantial reason to suppose that the United
Kingdom’s withdrawal from the European Union should have a substantial impact on the appeal of London as a seat for the arbitration of international commercial disputes. The principal domestic and international instruments governing the enforcement of arbitration agreements and arbitration awards and the other factors influencing the appeal of London as a seat for international arbitration are unaffected by Brexit.”

Lawyers may be tempted to hedge their bets when predicting the future, which could explain the report’s reference to there being no ‘substantial’ reason to think that Brexit might have a ‘substantial’ impact. One could go a little further and instead say that, based on the legal framework that governs international arbitrations subject to English law and with a London seat, there is no ‘substantive’ reason why Brexit should have ‘any’ impact on the vast majority of commercial arbitrations.

The parties are still free to choose arbitration

Arbitration is consensual in nature. The jurisdiction of any arbitral tribunal depends on the agreement of the parties, set out in the arbitration clause. English law gives effect to arbitration clauses wherever possible. Brexit would have no effect on the validity or the interpretation of arbitration agreements under English law.

The Arbitration Act 1996 requires that arbitration clauses must be ‘in writing’ so that there is certainty as to the existence of an agreement to arbitrate. That requirement is construed relatively widely, and extends to agreements recorded in an exchange of emails, incorporating an arbitration agreement in another contract by reference, or even an oral agreement by reference to written terms - such as for instance, an oral agreement that the same terms set out in an earlier contract would apply (see Heifer International Inc v Christiansen [2007] EWCH 3015 (TCC)), or perhaps an oral agreement to resolve disputes under the (written) rules of the LCIA. English law is also willing to find valid arbitration agreements even where the parties have expressed their intention to arbitrate less clearly than they could have done. A clause referring to “UK arbitration” was upheld in Exmek Pharmaceuticals SAC v Alkem Laboratories Ltd [2015] EWCH 3158 (Comm).

Arbitration agreements are construed widely under English law. As the House of Lords noted in Premium Nafta Products Ltd v Fili Shipping Company Ltd [2007] UKHL 40, there is strong presumption that businessmen want all their disputes - be they contractual or non-contractual in nature - to be resolved by one and the same tribunal. English law will not adopt a legalistic interpretation when it comes to arbitration clauses, and there should be no mileage in arguing that certain disputes do not ‘arise out of’ or are ‘in connection with’ the relevant contract. It will be presumed that the parties intended the arbitrators to deal with all issues, unless they expressly excluded something from their remit.

A recent decision illustrating how the parties can confer wide powers on their arbitral tribunal

The recent decision of the High Court in Associated British Ports v Tata Steel UK Ltd [2017] EWHC 694 (Ch) illustrates how English law upholds the principle of ‘party autonomy’, and allows the parties to agree that their arbitral tribunals should have wide powers (if that is what they wish).

Associated British Ports (“ABP”) owns and operates the tidal harbour at Port Talbot in Wales. Tata Steel is the owner of two steel works that make use of the harbour. Iron ore and other materials are imported through the harbour, and a significant proportion of all vessels that come to Port Talbot supply these steel works. In 1995, ABP and Tata entered into a license setting out the terms on which Tata could use the harbour. It had a term of 25 years. Clause 22 purported to give an arbitral tribunal appointed under the license considerable discretion in altering the terms of the agreement:

“... in the event of any major physical or financial change in circumstances affecting the operation of [the steel works] ... or [the tidal harbour] ... on or at any time after the 15th day of September 2007 either party may serve notice on the other requiring the terms of this Licence to be re-negotiated with effect from the date on which such notice shall be served. The parties shall immediately seek to agree amended terms reflecting such change in circumstances and if agreement is not reached within a period of six months from the date of the notice the matter shall be referred to an Arbitrator.”

In February 2016, Tata gave notice to ABP under Clause 22. Tata sought significantly lower fees based on the tonnage of goods shipped, including a 50% reduction in annual fixed fees, from £7 million to £3.5 million. Tata explained that the UK steel industry was facing significant market challenges, with a strong pound (presumably no longer a concern) and a doubling of steel imports into Europe, notably from China. Tata also noted the imposition of increased tariffs by the US on European steel imports. All this had happened against the background of Tata having to downsize and streamline its loss-making UK operations.

Absent a provision like Clause 22, none of this would have allowed Tata to change the terms it had agreed to in 1995. As discussed further below, unlike some civil law systems, English law takes the view that contracts are not invalidated, or fail to be renegotiated, because performance becomes more expensive or onerous for one party. But here the parties had included Clause 22. The question for the High Court was whether this clause was too uncertain to be enforceable. ABP argued that the clause should not be enforced because the event that triggered it - “any major physical or financial change in circumstances” - was just too open ended to create a binding obligation to submit a dispute to an arbitral tribunal. ABP said that any tribunal appointed under Clause 22 would have no objective criteria to apply in deciding what the new
license terms were going to be, and would just have carte blanche to rewrite the parties’ bargain. That, ABP submitted, was not something that the parties should be held to.

Rose J noted that English law was reluctant to hold that parties to a commercial contract had failed to create an enforceable obligation. She cited another recent decision where the Commercial Court had commented that:

“64. ... The role of the court in a commercial dispute is to give legal effect to what the parties have agreed, not to throw its hands in the air and refuse to do so because the parties have not made its task easy. To hold that a clause is too uncertain to be enforceable is a last resort or, as Lord Denning MR once put it, “a counsel of despair”: see Nea Agrex SA v Baltic Shipping Co Ltd [1976] 1 QB 933, 943.”

Rose J also noted that this was a contract that had been partially performed, and Clause 22 only kicked in after 12 years. The judge saw the commercial sense in including such a provision, as the performed, and Clause 22 only kicked in a Ō strive to uphold commercial contracts. Such a ‘renegotiation’ clause will not of course be appropriate for every contract. If the parties do not include a provision of this kind, then English law will hold them to their bargain - but in a long term contract, they have the option to refer the commercial basis of their dealings to a tribunal for review if they so choose.

The parties are still free to choose English law and the advantages that it offers

Arbitrating in London is the obvious choice if the contract is governed by English law. Choosing England as the seat means that the arbitration will be supervised by the English Courts, applying the Arbitration Act 1996. While governing law and seat go hand in hand and should ideally be identical, the applicable law of the contract is the more important choice. The applicable law can have a considerable impact on the rights and obligations of the parties, and it may drive the selection of the seat as a secondary (nonetheless important) choice.

Returning to the relevance (or lack thereof) of Brexit, the English law of contract as it applies between commercial parties is not dependent on EU law principles. While EU has made significant intrusions into the sphere of consumer law and provides a number of protections for consumers that were traditionally unknown to the more laissez-faire English law, nothing of the sort has happened in the field of commercial law since 1972. We do not yet know what will happen to the many hundreds of EU instruments that currently apply in the UK - but save perhaps for a limited number of cases, whatever the legal position will turn out to be after Brexit, it will not affect the kind of disputes that are referred to international arbitration in London with any immediacy (or indeed, as far as we can tell now, at all).

Why then do so many parties choose English law for their agreements? It has often been said that English law offers certainty and predictability. When it comes to interpreting or construing contracts, what you see is very often what you get. English law has a straightforward, objective approach to contractual interpretation. The ordinary meaning of the words used in the written contract frequently carries the day. Bargains struck between commercial parties are upheld. English law offers freedom of contract. There is little room for implied terms, doctrines of good faith or notions of deliberate breach or fault-based remedies tilting the balance unexpectedly in favour of one party.

Common sense prevails - the latest from the Court of Appeal in contract interpretation

Many contracts are poorly drafted, or perhaps less than perfectly drafted because they represent a compromise, with lawyers for both sides pushing and pulling at the wording to make it that little bit more favourable for their client. English law offers a reliable and common-sense approach to resolving these issues without departing from the written words. A recent decision by the Court of Appeal dealing with a less than perfectly drafted contract pro-
vides a good illustration. In *Sutton Housing Partnership Ltd v Rydon Maintenance Ltd* [2017] EWCA Civ 359, the London Borough of Sutton had engaged Rydon under a long term contract to manage its housing stock - something that involved extensive repairs, maintenance and (where necessary) construction work. The main provisions of the contract stated that Rydon could benefit from an incentive scheme, and they also gave Sutton a right to terminate for poor performance. The contract explained that Sutton’s right to terminate, and Rydon’s right to additional incentive payments, both depended on whether Rydon had met, or exceeded, so-called ‘minimum acceptable performance’ levels (MAPs). The contract also said that the MAPs were to be found in a key performance indicator (KPI) framework comprised largely of a spreadsheet - which soon turned out to be problematic.

Sutton became dissatisfied with Rydon’s performance and wanted to terminate. Rydon argued that the contract did not actually contain any MAPs, certainly not for the relevant contract years. The only reference to MAPs to be found anywhere in the KPI framework was in a worked example for the first year of the contract. The worked example showed that MAPs were 3% below the performance target. Jackson LJ in the Court of Appeal deduced that the parties had wanted to set the MAPs at 3% for all contract years, even though they had not expressly said that. To hold otherwise would have limited Sutton’s right to terminate for poor performance to the first contract year, whilst equally preventing Rydon from earning incentive payments in any of the following years, something which a reasonable person would not have taken as their intention. The construction adopted by the Court of Appeal stopped short of implying a new term into the contract: it is a good example of how English law construes the intention of the parties objectively, and in a commercially sensible manner, by looking at what they have written in their contract - but does not rewrite the agreement, or subject it to a test of reasonableness.

**Contrasting approaches to contract interpretation under English law and civil law**

In contrast, in civil law systems we understand that there is more scope for the subjective intention of the parties to prevail over the contract wording, and there may also be greater propensity for statute to introduce further terms into the agreement, depending on the industry or sector. French law is a good example. The relevant part of the Civil Code was recently amended, with the changes having come into force as of 1 October 2016. Article 1102 of the French Civil Code describes how the principle of freedom of contract underlies French law, and declares that the parties are free to contract (or not), and determine the content and form of the contract, “... within the limits imposed by legislation.” It seems that any statutes which are deemed to reflect French public policy cannot be derogated from. It can be difficult to locate relevant statutes.

French law introduces a duty of good faith which applies both to the performance of the contract, but also to any negotiations leading up to it. As regards such negotiations, the October 2016 reforms now make it clear that a party has to disclose information that would directly affect the other party’s intention or willingness to contract.

A third change is that French law now recognises the concept of hardship - a doctrine that had previously featured in other civil law systems, but not in France. The October 2016 changes now provide that a party may renegotiate the contract if continuing performance on the originally agreed terms would be excessively onerous, always provided that it has not expressly accepted the relevant risk in the contract. English law adopts a narrower approach: there is no automatically applicable duty of good faith (although clauses expressly applying good faith are upheld), a party is not under a positive duty of disclosure during negotiations (but a contract can be void for misrepresentation where it has been induced by a false statement), and there is no doctrine of hardship (although contracts can be frustrated where performance becomes impossible, and *force majeure* clauses may excuse a party in certain defined circumstances).

**What other advantages does English law offer?**

English law practitioners would identify a couple of other advantages that are unaffected. English law - when applied by arbitrators or judges with English training - should lead to reasoned and principled awards of damages. It compensates parties based on principles that most businessmen would understand and agree with. There are no mysterious 'lump sum' awards as can be found in civil law decisions, and there are no punitive damages as can be awarded in the United States. English law has also strove to make itself useful to businessmen and commerce for several centuries. The English law of contract is predominantly based on judicial precedent in the shape of case law, alongside statute. The law of contract can therefore adapt and evolve more quickly than codified systems which require legislative reforms that may be slow in coming. English law has grown and kept pace with modern business practices and technology. It can deal with complicated financial structures and technically complex issues, as in the energy, engineering and construction industries (sectors where English law is often favoured). This prevalence of English law works to its advantage. Because more complex contracts are subject to English law, English judges and arbitrators resolve more such disputes. Jurisprudence can develop. While decisions on contractual interpretations are limited to the agreement in question, it helps to have recourse to a body of law on recurring issues and commentary on the standard forms that often provide the foundation for the parties’ contracts.

If you are asking your counterparty in negotiations to accept English law, familiarity may work in your favour. The common law is the basis of around 30% of the world’s jurisdictions. As the de facto market leader, English law has become increasingly familiar.
even to those from other legal backgrounds. English is also the lingua franca of international trade. If you are negotiating in English, then why not also resolve your disputes in English?

Lastly, the London offers a sophisticated legal infrastructure. This allows parties to access a mature legal services market, with specialist lawyers available to advise on any number of complex transactions. The Arbitration Act 1996 and English law as it applies to arbitrations and arbitration agreements provides party autonomy and strongly supports the arbitral process. The Commercial Court gives effect to arbitration agreements and assists the parties where this is required and appropriate. It deals robustly with challenges to awards (e.g. under Section 68 on the basis of a serious procedural irregularity). The Commercial Court can also grant injunctions, including worldwide freezing orders, in support of arbitration proceedings or the enforcement of awards. Again, the exercise of the High Court’s supervisory role in arbitrations with a seat in England would not be affected by Brexit.

Conclusion

The Lord Chief Justice of England and Wales, Lord Thomas, said:

“In some quarters it has even been suggested that Brexit makes the law of the UK uncertain. This is all quite wrong. Brexit will have no effect on London’s key strengths.”

He was right to be emphatic. However, the English legal profession cannot be complacent in the face of Brexit. Practitioners (counsel and arbitrators alike) will continue to have to explain the true position to clients and colleagues who will, quite understandably, have questions. This also provides an opportunity for taking stock, and reminding ourselves of the reasons why parties come to arbitrate their disputes in London. There is always room for improvement, including when it comes to the duration and costs of proceedings. But whilst we might not all be proud of the leaders that our society seems to throw up like a cat regurgitating fur balls, at very least we can still, humbly and gratefully, take pride in our legal system.

Unintended consequences - be clear what you advise on

by Ryan Deane

In the recent case of BPE Solicitors v Hughes-Holland [2017] UKSC 21, the Supreme Court unanimously re-affirmed and clarified the principle established by the House of Lords in South Australian Asset Management Corporation v York Montague [1996] UKHL 10 (the “SAAMCO principle”). This article explains the clarification and the practical consequences it has for those seeking professional advice.

The SAAMCO principle

The problem that the SAAMCO principle was established to address was colourfully illustrated by Lord Hoffmann in the SAAMCO case itself. He asked during the course of argument what the liability of the doctor should be in the following hypothetical scenario:

“A mountaineer about to undertake a difficult climb is concerned about the fitness of his knee. He goes to a doctor who negligently makes a superficial examination and pronounces the knee fit. The climber goes on the expedition, which he would not have undertaken if the doctor had told him the true state of his knee. He suffers an injury which is an entirely foreseeable consequence of mountaineering but has nothing to do with his knee.”

In legal terms, the issue is what damages are recoverable in a case where (i) but for the negligence of a professional adviser his client would not have embarked on some course of action, but (ii) part or all of the loss which he suffered by doing so arose from risks which it was no part of the adviser’s duty to protect his client against.

In SAAMCO the House of Lords held that in order to answer this question one must first determine the scope of the advisor’s duty. Lord Hoffmann drew a distinction between two types of cases. In ‘information’ cases a professional provides only part of the material to be relied on by the client in making his own decision on whether to proceed. In these circumstances the adviser is not held responsible for all the consequences of his advice, but only the consequence of the information being wrong.

By contrast, in ‘advice’ cases it is for the professional to identify and consider all relevant matters that need to be taken into account when deciding whether or not to proceed. The adviser is responsible for guiding the whole decision making process, and becomes responsible for the decision itself. Accordingly, the professional will be liable for all the foreseeable consequences of a transaction entered into upon negligent advice, such as a rise or fall in the relevant market.

Lord Hoffmann explained that his mountaineer hypothetical was an example of an ‘information’ case. The doctor was not advising the patient on whether to undertake the climb, but was instead providing a discrete piece of information to the mountaineer to factor into his own decision making process. The mountaineer was ultimately responsible for the consequences of his decision to go mountaineering.

Subsequent cases have struggled with the application of Lord Hoffmann’s distinction between information and advice cases, leading to unprincipled judgments and inconsistent decisions. The Supreme Court took the opportunity in BPE Solicitors v Hughes-Holland to clarify the position.
Background

The defendant solicitors (“BPE”) had acted for Mr Gabriel when he made a loan to his friend Mr Little. Mr Gabriel was subsequently adjudicated bankrupt and his trustee in bankruptcy (Mr Hughes-Holland) took his place in the litigation.

The loan was made in connection with the development of a building owned by one of Mr Little’s companies (High Tech). Mr Gabriel understood that the proceeds of the loan would be used to pay the costs of the development. In fact, Mr Little intended to, and did, utilise the main part of the proceeds to enable one of his companies (Whiteshore) to purchase the property from High Tech, enabling the latter to discharge an existing secured loan. The balance was used to discharge an existing VAT liability of High Tech. The development did not proceed. In due course the building was sold, but Mr Gabriel recovered nothing on the sale (because the proceeds did not cover the costs) and lost his entire advance less only a modest payment made by Mr Little.

The loan documentation drafted by BPE (a facility letter and a charge) was based on a draft prepared for an earlier transaction and stated that the loan would be “made available as a contribution to the costs of the development of the property” and that the purpose of the loan was to “assist with the costs of the development of the property”. This reflected Mr Gabriel’s understanding but not Mr Little’s intention. The trial judge found that Mr Gabriel would not have made the loan if he had known of Mr Little’s intention.

A curious feature of the case was that BPE’s instructions to act for Mr Gabriel had been provided by Mr Little, who left a voice mail message for the solicitor involved informing him that he intended to sell the property to Whiteshore and that Mr Gabriel would lend him the money. The loan documentation as drafted did not, therefore, reflect Mr Little’s actual intentions or the instructions he had provided to BPE (which BPE had not in fact confirmed with Mr Gabriel, their client).

Mr Gabriel sued everyone involved, but his claims against Mr Little, High Tech and Whiteshore were dismissed at trial, as was a claim against BPE for dishonest assistance. Mr Gabriel also advanced a claim against BPE for negligence. That claim succeeded at trial and gave rise to the subsequent appeals.

The basis of the claim in negligence was that BPE should have explained to Mr Gabriel how the funds were in fact going to be applied. Instead of doing so, it negligently drafted the loan documentation in a manner which did not reflect Mr Little’s intentions, and thereby misled Mr Gabriel into believing that the funds would be utilised in accordance with his understanding. Mr Gabriel claimed the whole of his lost advance.

At trial, BPE argued that the development had never been viable, meaning that Mr Gabriel would have lost the whole of his loan even if the proceeds had been used as he intended. The trial judge agreed with BPE that if the development was “unviable and bound to fail so that Mr Gabriel would never have recovered his loan” then BPE would not be liable for the losses claimed. He nonetheless went on to say that he did not “think it would be right for me to conclude that this was necessarily going to be a doomed venture for Mr Gabriel from the outset”. Having held that BPE had acted negligently he gave judgment in favour of Mr Gabriel.

However, the Court of Appeal overturned this finding and held that, even if the loan had been used to develop the property, it would not have been improved in value and Mr Gabriel would have suffered the same amount of losses in any event. In the face of this finding, Mr Gabriel argued that, nonetheless, he had been informed of how the third party intended to use the loan, he would have appreciated the transaction was not viable and not made any loan to the third party. On this basis, he argued he was entitled to all his losses from the transaction.

Applying the SAAMCO principle, the Court of Appeal held that BPE only owed Mr Gabriel a duty to provide discrete information and advice to allow him to decide for himself whether to make a loan to the third party and not to advise on what course of action to take or as to the commercial risks of the relevant loan. Accordingly, BPE were only liable to the extent that loss was attributable to something wrong in their advice.

As Mr Gabriel would have suffered the same losses even if the loan had been used to develop the property, his losses were not attributable to BPE’s failure to report how the third party intended to use the loan but, instead, to his decision to make the loan. The claimant was prepared to risk the possibility that the third party would default and the property would not increase in value despite being developed and so could not recover damages from his solicitors for those risks eventuating. The claimant alone was responsible for the decision to make the loan.

Decision of the Supreme Court

Lord Sumption, giving the judgment of the Supreme Court, said that the SAAMCO decision had often been misunderstood. The misunderstanding arose from a tendency to overlook certain fundamental features of its reasoning.

He reiterated that where the professional supplies information which the client will take into account in making his own decision on the basis of a broader assessment of the risks, the professional has no legal responsibility for the decision because it falls outside the scope of his duty.

The principle has nothing to do with causation, as the term is usually understood. It is often accepted that the losses suffered by the client are, as a matter of causation, properly attributable to the adviser. That, however, is focusing on the wrong issue. Even if the client can prove that he would not have entered into a transaction but for receiving the negligent advice, that is insufficient to bring losses resulting from the transaction within the scope of the adviser’s duty.

Lord Sumption recognised that the distinction between advice and information cases had given rise to confusion because of the
descriptive inadequacy of the labels. They were neither distinct or mutually exclusive categories. He explained that information given by a professional to a client is usually a specific form of advice, and most advice will involve conveying information. Instead of focusing on terminology, however, one should focus on the nature of the distinction, which he described as follows:

“In cases falling within Lord Hoffmann’s “advice” category, it is left to the adviser to consider what matters should be taken into account in deciding whether to enter into the transaction. His duty is to consider all relevant matters and not only specific factors in the decision. If one of those matters is negligently ignored or misjudged, and this proves to be critical to the decision, the client will in principle be entitled to recover all loss flowing from the transaction which he should have protected his client against.

By comparison, in the “information” category, a professional adviser contributes a limited part of the material on which his client will rely in deciding whether to enter into a prospective transaction, but the process of identifying the other relevant considerations and the overall assessment of the commercial merits of the transaction are exclusively matters for the client.”

The important point, on which the distinction had been blurred even at the appellate level, was that if an advisor gives information that he knows is critical to the client’s decision whether to enter into a transaction that does not transform an information case into an advice case. That would make the breach of duty more serious, and the argument on causation stronger, but would ignore the logically prior issue of the scope of the advisor’s duty. Lord Sumption clarified that in information cases, the burden of proof is on the claimant to establish that the loss he is claiming was in fact caused by the falsity of the information provided. It is not sufficient for the claimant to prove that he sustained loss by entering into the transaction and to leave it to the professional to show that some or all of that loss was the consequence of other causes.

Application to the facts

Applying this analysis to the facts in BPE Solicitors, the first question was whether BPE had assumed responsibility for Mr Gabriel’s decision to lend money to Mr Little. Lord Sumption came to the clear view that they had not. He held that their instructions were to draw up the facility agreement and the charge, and nothing more. They did not know, and did not need to know, what had passed between Mr Gabriel and Mr Little, except that they had agreed upon a loan of £200,000 secured by a charge on property. They simply included in the draft facility agreement by oversight language which by an unhappy chance confirmed that assumption.

The Deputy Judge at first instance had been wrong to hold that the solicitors’ breach of duty “meant that Mr Gabriel was not able to know the true nature of the loan transaction into which he was entering”. That was not relevant to the scope of the BPE’s duty of care. Lord Sumption continued:

“On the footing that BPE was not legally responsible for Mr Gabriel’s decision to lend the money, but only for confirming his assumption about one of a number of factors in his assessment of the project, the next question is what if any loss was attributable to that assumption being wrong. The answer is that if it had been right, Mr Gabriel would still have lost his money because the expenditure of £200,000 would not have enhanced the value of the property. The development would have been left incomplete, the loan unpaid and the property substantially worthless when it came to be sold into a depressed market. None of the loss which Mr Gabriel suffered was within the scope of BPE’s duty. None of it was loss against which BPE was duty bound to take reasonable care to protect him. It arose from commercial misjudgements which were no concern of theirs.”

On this basis the Supreme Court unanimously dismissed the appeal.

Practical lessons

The SAAMCO principle is important because it will enable a negligent professional to avoid liability for losses suffered by the client in certain circumstances. Each party to a professional relationship should be aware of the principle both at the time when the professional is acting and during any subsequent litigation.

In particular, to avoid potential disputes it is in both parties’ interests to clarify the terms of the retainer and any subsequent changes to it. This will not necessarily be determinative of the scope of the professional’s duty, but will go a way towards reducing the scope for argument.

A client seeking advice as to whether or not to enter into a transaction should make this clear, and should be careful not to appear as seeking information only as to one or more aspects of it. A professional, on the other hand, should take care not to ‘over market’ the services he is providing so as to give the impression that he is providing advice as to the viability of the transaction when in fact he is merely providing information as to one aspect of it.

A claimant bringing a claim against a professional who has only provided information needs to be realistic about his ability to prove, as a necessary part of his case, that the loss was indeed a consequence of the relevant negligence, and not of entering into a transaction that was in any event flawed. This may involve proving a difficult negative. A professional defending a claim should seek clarification, as early as possible, as to exactly how the claimant intends to establish that the loss claimed was within the scope of the duty.