Manchester Building Society v Grant Thornton UK LLP [2019] EWCA 40 (Civ) 30.1.19

The Court of Appeal has today dismissed the claimant's appeal, in this important decision on the application of SAAMCO in auditors' negligence cases. Nicola Rushton QC considers why their analysis is useful for future cases of financial professional negligence.

In summary, the Court reaffirmed the classic advice/information distinction and the importance in "information" cases of proving that the same loss would not have been suffered if the advice had been correct. Since the discovery of the negligent advice merely crystallised mark-to-market losses on swaps which would have been suffered anyway, those losses were not recoverable.

The Claimant building society ("MBS") issued fixed interest lifetime mortgages. These released equity on terms that loan and interest were only repayable when the borrower entered a care home or died. To hedge the risk from variable interest rates on funds it borrowed, MBS entered into long term swaps.

From 2005 a change in accounting standards meant those swaps had to be recorded on its balance sheet, causing volatility in its financial position. In 2006, MBS's auditor, Grant Thornton ("GT"), advised MBS could apply hedge accounting in recording the swaps and mortgages. This allowed MBS to revise the mortgage values, off-setting changes in the value of the swaps' values and reducing the volatility. In reliance on this advice, MBS purchased further swaps and made further loans.

Following the 2008 crash, interest rates fell and the swaps became a liability. In 2013 MBS discovered it could not in fact use hedge accounting. Its balance sheet became exposed to significant volatility and to the full losses suffered on the swaps. As a result of the necessary revision to its accounts, it no longer held sufficient regulatory capital and had to break the swaps at their then fair value, suffering a loss of £32.7m.

MBS claimed GT were responsible for this loss, because it had flowed from the need to break the swaps after the negligent advice had been discovered. The trial judge Teare J. held that causation in law and fact was established. But for the negligent advice MBS would not have bought the swaps, and it would not have needed to break the swaps in 2013 if the advice had been correct. However, he held that GT had not assumed responsibility for these losses, which flowed from market forces, but were only liable for the £285,460 transaction costs of breaking the swaps.

The Court of Appeal dismissed MBS's appeal, but its reasoning was much more trenchant than the trial judge's. In a unanimous decision they concluded that:

1. The trial judge should have decided whether this was an "advice" or an "information" case, as defined by *SAAMCO* and *BPE v. Hughes-Holland*. Although Lord Sumption had described the labels as inadequate, the distinction they represented was an important one. It was not sufficient for the judge to make an open-ended enquiry into whether the defendant had "assumed responsibility" for the losses.
2. "Advice" cases were ones where it was left to the adviser to consider what matters should be taken into account in deciding whether to enter into the transaction. In such cases, the adviser was liable for all the foreseeable losses flowing from entering into the transaction. However, unless the adviser was responsible for guiding the whole process in this way, then it was an "information" case. In such cases, the adviser was only responsible for the foreseeable financial consequences of the information or advice being wrong. As to the label, what mattered was whether the advice/information related to one aspect, or related to whether to enter into the transaction as a whole. It did not depend on whether what was provided was advice.
3. To determine the foreseeable financial consequences of the information or advice being wrong, it is necessary to exclude all losses which would have been suffered if the advice had

been correct. This is the key tool for distinguishing between losses caused by entering into the transaction, and losses caused by the advice or information being wrong.

4. Applying the SAAMCO principle therefore generally involved the following steps (flow-chart style!):
    a. consider first if it is an advice or an information case.
    b. a case is only an "advice" case if it was left to the adviser to decide what matters should be taken into account in deciding whether to enter into the transaction.
    c. In an advice case, the adviser has assumed responsibility for the decision to enter into the transaction, and so is responsible for all the financial consequences of doing so.
    d. If it is not an advice case, it is an "information" case.
    e. in an information case, the adviser is only responsible for the foreseeable financial consequences of the advice/information being wrong.
    f. This involves considering what loss would have been suffered if the advice had been correct. Only losses which would not have been suffered in such circumstances are recoverable.
5. This was clearly an "information" case, and the judge should have held that it was. It was therefore necessary to consider if the same loss would have been suffered if the advice had been correct.
6. It was striking that the loss claimed by MBS was the fair, mark-to-market value of the swaps when sold. Receiving fair value does not ordinarily give rise to any loss.
7. To prove recoverable loss, MBS would have had to prove the counter-factual that the mark-to-market loss would not have been suffered if it had continued to hold the swaps. It had been unable to do that. The closing out of the swaps merely crystallised the losses that resulted from the swaps being "out of the money", but it did not create that loss. The judge had therefore been wrong to find the the same losses would not have been suffered if the

advice had been correct. However he was correct in his overall conclusion that those losses were caused by market forces and so were not recoverable.

By reaffirming both the classic advice/information distinction, and that in “information” cases, the key test is whether the same loss would have been suffered if the advice had been correct, this court of three commercial judges has strengthened the SAAMCO test as an analytical tool. It is interesting especially that they defined what were “information” cases in such an inclusive way – as being all those which were not clearly advice cases. The first instance judgment had been confusing. The clear-edged approach in this judgment should make SAAMCO easier to apply in financial professional negligence cases like this one.

Case note by Nicola Rushton QC, Hailsham Chambers

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