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BRIEFING

PROFESSIONAL NEGLIGENCE
CLINICAL NEGLIGENCE

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On 18th June the Supreme Court handed down judgments in *Manchester Building Society v Grant Thornton* and *Khan v Meadows*. In this joint briefing we consider the judgments from both a professional negligence and clinical negligence perspective.

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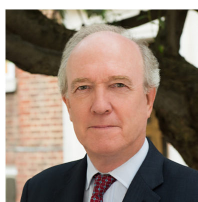

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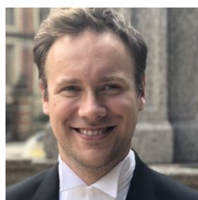

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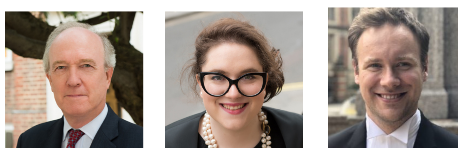

REHABILITATION OF THE "MOUNTAINEER'S KNEE"? *MANCHESTER BUILDING SOCIETY V GRANT THORNTON*

JOHN ROSS QC, FRANCESCA O'NEILL AND THOMAS YARROW

Introduction

As set out in the judgment of Lord Sumption in *BPE Solicitors v Hughes-Holland* [2017] UKSC 21 it took approximately 20 years for the House of Lords decision in *SAAMCO* to be reviewed at the highest level, and only a few years later the issues of professional advice cases has again been before the Supreme Court, with five separate judgments across the two cases setting out propositions and principles which have important bearing not only on professional negligence cases, but on the broader law of tort. This article considers the three judgments given in *Manchester Building Society v Grant Thornton UK LLP* [2021] UKSC 20.

The facts are somewhat commercially complex, and some jargon must be excused. The claimant building society purchased and issued lifetime mortgages. The borrowers were homeowners over the age of 50 in the UK and Spain who wanted equity in their properties released. The mortgage arrangements were such that neither interest nor capital was repayable until the borrower died, moved out, or voluntarily chose to repay and redeem the mortgage. Importantly the mortgage over the homeowner's lifetime was charged at a fixed rate.

Factual Background

In order for the society to fund these mortgage loans, they themselves borrowed money, but this time at a variable rate of interest. That meant that there was a risk that the variable cost at which the society was borrowing would exceed the fixed rate of interest they would recover from their

consumer clients. In order to 'hedge' against that risk, the society entered into interest rate swap contracts whereby the society agreed with a counterparty to pay a fixed rate of interest on a notional sum, while the counterparty would pay a variable rate on the same sum. In this way, the variable rate paid by the counterparty would match the variable rate paid by the society on their borrowings used to fund the mortgages, while the fixed rate paid by the society under the swaps would be less than the fixed rate they would recover from their customers. This would ensure a profit.

'Swaps' are a financial product which can be traded, and which therefore have what is known as a 'mark-to-market' (MTM) value (based on the expected recovery of interest payments over a defined lifetime of the product). Normal regulatory requirements required the society to account for any swaps on its balance sheet at their MTM value, while the mortgage loans were accounted for at their book value; this meant that where there was movement in interest rates the values of the swaps would diverge from the values of the mortgage loans and the society's accounts would look volatile. More volatile accounts would require an increase the amount of reserve capital the society was required to hold by the regulator.

To combat this problem, Grant Thornton advised the society that it could use a method of accounting known as 'hedge accounting'. Where hedge accounting was permitted, the value of the lifetime mortgages on the accounts could be adjusted to offset changes in the MTM value of the swaps. This would decrease the volatility showing in the accounts, and accordingly decrease the reserve capital required to be held by the society.

The difficulty was that hedge accounting could only be used where the hedge was expected to be 'highly effective', but in this case the swaps being entered into were for terms of 50 years, and were being used to hedge mortgage products offered to people over 50. There was therefore a mismatch between the dates on which the mortgages and the dates on which the hedging swaps would mature. This, along with other particular features of the arrangements, meant that the hedging in this case was not considered 'highly effective' and hedging accounting could not, in fact, legitimately be used. Grant Thornton's advice was wrong, and alleged to be negligent.

The society relied on that advice in preparing its financial statements between 2006 and 2011 until, in 2013, Grant Thornton informed the society that hedge accounting was not in fact permitted. In its 2012 accounts, the society therefore had to account for the MTM value of the swaps without adjusting the book value of the mortgages. At that stage the MTM swaps had a considerable negative value, in part caused by the financial crisis of 2008. Because of the mismatch in the book value of the mortgages and the value of the swaps when presented without hedge accounting, the society had insufficient capital to meet its regulatory requirements. In order to extricate itself from the situation the society had to terminate all of its interest rate swap contracts early at a significant loss (because of the negative MTM value); it additionally sold its mortgages with a slight profit.

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The society brought a claim against Grant Thornton. The main loss claimed, and the only one in issue by the time the case reached the Supreme Court, was for the amount paid to close out the swaps in 2013. Grant Thornton admitted negligence in advising that hedge accounting could be used, when it could not, <u>but argued that its negligence did not cause the loss and/or that the losses fell outside the scope of their duty of care</u>.

First Instance decision and the Court of Appeal

The trial judge, Teare J, found that, but for the negligent advice, the society would not have entered into the swap contracts which it later had to close at a loss. However, he derived from *SAAMCO* (via *Hughes Holland*), that Grant Thornton had not *assumed responsibility* for the matters from which the loss flowed; the losses actually flowed from market forces for which Grant Thornton did not assume responsibility. The judge went on to find, in case he was wrong, that the society had contributed to their loss by their own negligence and a 50% apportionment of liability should be made.

The Court of Appeal held that *assumption of responsibility* had been the wrong test and instead the judge should have considered whether this was an 'advice' or 'information' case (as per Lord Hoffman in *SAAMCO* and as explained by Lord Sumption in *Hughes Holland*). This was not a case where Grant Thornton had guided the whole decision making process, but had only provided information and was therefore legally

responsible only for the foreseeable financial consequences of its input being wrong. On the Court of Appeal analysis, and applying the so-called *SAAMCO* counterfactual approach, the society could not show that it had suffered any losses that it would not have suffered if Grant Thornton's information had been correct (i.e. that hedge accounting could be used). While it was true that they terminated the swaps early which they otherwise would not have done, they had not proved that they would have been better off if they had continued to hold the swaps past 2013; by all accounts the reality was that the swaps would have had an even more significant negative value by the time of the proceedings.

The society appealed to the Supreme Court.

The Supreme Court

In helpful agreement across all three judgments, the court confirmed that the 'advice' and 'information' distinction in professional advice cases was no longer a helpful one, and practitioners can now consign this dichotomy to the archives. The distinction was too rigid and likely to mislead. Despite this agreement on this aspect, and agreement on the outcome of the case, the three judgments thereafter differ both in their approach to the law of negligence and to the applicability of a *SAAMCO* analysis to a case such as this.

The majority led by Lords Hodge and Sales set out six 'questions' to be answered when analysing any action in negligence. It is useful to set these out in full:

(1) Is the harm (loss, injury and damage) which is the subject matter of the claim actionable in negligence? (**The actionability question**)
(2) What are the risks of harm to the claimant against which the law imposes on the defendant a duty to take care? (**The scope of duty question**)
(3) Did the defendant breach his or her duty by his or her act or omission? (**The breach question**)
(4) Is the loss for which the claimant seeks damages the consequence of the defendant's act or omission? (**The factual causation question**);
(5) Is there a sufficient nexus between a particular element of the harm for which the claimant seeks damages and the subject matter of the defendant's duty of care as analysed at stage 2 above? (**The duty nexus question**)
(6) Is a particular element of the harm for which the claimant seeks damages irrecoverable because it is too remote, or because there is a different effective cause (including novus actus interveniens) in relation to it or because the claimant has mitigated his or her loss or has failed to avoid loss which he or she could reasonably have been expected to avoid? (**The legal responsibility question**)

This case was principally concerned with the second and the fifth questions and, importantly for the majority, the scope of duty analysis was to come early in the scheme. The question to ask in determining that scope was to analyse the *purpose* for which the advice was given. The court, when dealing with a range of factual scenarios, should look to see what risk the duty was supposed to guard against and then look to see whether the loss suffered represented the fruition of that risk.

By analysing the purpose of the advice in defining the scope, in some cases the second question can be determined without looking at breach and factual causation, but in cases such as the present the "duty nexus" question at stage five provides a practical approach to working out implications of the answer to stage two.

In the opinion of the majority, and indeed Lord Burrows, the *SAAMCO* counterfactual provides a useful 'cross-check' on the scope of the duty of question, but that question should necessarily be *prior question* and a *SAAMCO* counterfactual analysis should not supplant or subsume the definition of the scope of the duty. A causation-based analysis to determining scope (as presented by Lord Leggatt) is less sure and less simple that a purpose-based approach, not least because in less straightforward cases, there is a greater scope for abstruse and highly debatable arguments to be deployed when inventing hypothetical worlds. In our view, this approach will not be encouraged by courts considering the application of the test.

On the facts of this case Grant Thornton had misrepresented that there was an effective hedging relationship between the swaps and the mortgages. The purpose of the advice was to deal with the issue of hedge accounting in the context of its implications for the society's regulatory capital. The negligent advice allowed the society to make the assessment that it had

the financial capacity to proceed, where otherwise it did not. In the majority's view this therefore made the facts of the case analogous to a dividend payment case, where an auditor negligently advises a company that it has capital resources at a level which would permit payment of a dividend when in fact it does not. No *SAAMCO* counterfactual analysis was necessary in such a case and the majority did not engage in one.

Accordingly, the scope of the duty included a duty to protect the society from the harm flowing from not having sufficient regulatory capital, and there was a sufficient nexus between the harm actually suffered and that duty. The judge's finding of contributory negligence was not challenged and was maintained.

Lord Leggatt's Judgment

Lord Leggatt reached the same conclusion, but via a route which the majority had elected not to pursue, namely to look more considerably at the arguments of causation in order to assess the scope of the duty of care. As stated above, it is our feeling that the majority of Judges in the lower courts will elect to follow the majority judgment rather than the slightly more esoteric approach favoured here.

Lord Leggatt's view was that the *SAAMCO* approach was a useful ingredient in establishing the scope of the duty of care in these types of cases. The *SAAMCO* test was a means of assessing whether there is a sufficient causal connection between the subject matter of the defendant's advice and the loss suffered by the claimant in order to justify the conclusion that the loss arose from a risk which was within the scope of the defendant's duty. The *SAAMCO* test either confirmed or gave effect to a core principle on scope of duty that an advisor is responsible only for loss resulting from that decision which is a consequence of what makes the advice incorrect.

His method was to ask first whether there was a 'basic loss' which was attributable (on a factual causation analysis) to the defendant's negligence – in this case clearly there was. And thereafter it was necessary to ask whether the basic loss which had been established flowed from any of the matters of which Grant Thornton negligently failed to inform the society and which made its advice incorrect. Here there was no doubt that there was a 'value gap' which the accounts produced by Grant Thornton concealed and that this was a cause of the loss - as without such a gap the costs incurred to close out the swaps would have been offset by a corresponding adjustment to the value of the lifetime mortgage books.

Applying the *SAAMCO* counterfactual, if Grant Thornton's advice had been correct, and there had been effective hedging between the mortgages and the swaps, the value of the lifetime mortgages would have been higher than it was by an amount equal and opposite to the MTM value of the swaps and Grant Thornton would not have incurred the loss in closing out the swaps which, in fact, the building society did.

It followed from his analysis that the full cost of closing out the swaps was attributable to a risk which Grant Thornton owed a duty of care to protect against.

Lord Burrows' Judgment

Lord Burrows' judgment is much more closely aligned with that of Lords Hodge and Sales, albeit he calls their approach 'novel' in structuring their six questions. He notes that their approach does not appear to start with establishing a duty of care, sees the *SAAMCO* principle as concerned with the 'duty nexus' question, and treats contributory negligence alongside remoteness. He disagrees with this approach.

He was criticised by the majority for apparently admitting policy considerations into a scope of duty analysis, incorporating inspection of a 'fair and reasonable allocation of the risk of loss as between the parties', although having read the majority judgment, Lord Burrows advanced his view that this underpinning policy did not represent a significant difference between his judgment and theirs.

Respectfully, we disagree with that. One of the essential purposes of binding authority in the Supreme Court is to provide guidance to lower courts and to practitioners as to the correct approach to disputes that may arise. The "6 point test" articulated by Lords Hodge and Sales does this: it sets out a regime which has broader applicability in all sorts of tortious claims. Policy considerations are important, but those are considerations that ought to remain the domain of legislators rather than Judges.

Conclusion

In our view, it is good thing that the distinction between "advice" and "information" cases has been consigned to the dustbin of legal history. This distinction may have served a useful distinction in limited the scope of duties owed by advisory service providers in certain circumstances, but it was overly obscure and did not provide either legal practitioners or those in the commercial world with certainty. Following the decision in *Hughes-Holland*, practitioners were left having to decide a crucial distinction in disputes, but were not furnished with appropriate tools to allow a ready conclusion to be reached. The Supreme Court in this decision has recognised that, and the clarity is most welcome.

SCOPE OF A DOCTOR'S DUTY OF CARE: *KHAN V MEADOWS* IN THE SUPREME COURT

PAUL STAGG

Along with its judgment in *Manchester Building Society v Grant Thornton UK LLP* [2021] UKSC 20 which is reviewed in detail by my colleagues John Ross QC, Francesca O'Neill and Tom Yarrow in their article, the Supreme Court handed down judgment in *Khan v Meadows* [2021] UKSC 21. The decision in the *Khan* case is a rather more factually straightforward example of the principle that the damages which a professional may be required to pay for a breach of a duty of care may be limited by the scope of the duty owed.

The claimant was aware that she was a carrier of the haemophilia gene after the birth of her nephew with that condition in 2006. When she was considering having a family of her own, she consulted her GP to seek advice as to whether she carried the gene. The GP arranged blood tests which were suitable for checking whether the claimant herself had haemophilia but which could not establish whether she was a carrier of the gene. Another GP later informed her that the results were normal. Believing that she could not pass the condition to her child, she became pregnant. Sadly, her son, A, was born with haemophilia. Had she known that he was affected by the condition, she would have chosen to terminate her pregnancy. It became apparent as A got older, however, that he is also autistic. That condition is unrelated to haemophilia, but its effects make the haemophilia much more difficult to manage. The costs of managing A's haemophilia were agreed in the sum of £1.6 million; damages covering the management of both conditions were almost six times that sum, being agreed at £9 million.

At first instance [2017] EWHC 2990 (QB), [2018] 4 WLR 8, Yip J awarded £9 million. She said that although the claimant had sought advice specifically about whether she could pass haemophilia on to a child, A's birth would not have occurred but for the negligent advice given by the doctors. The GPs had assumed a responsibility which would have avoided A's birth if properly fulfilled.

The Court of Appeal [2019] EWCA Civ 152, [2019] 4 WLR 26 allowed the GPs' appeal. The purpose of the consultation which led to the blood test was specifically to ascertain whether the claimant was a carrier of the haemophilia gene, rather than what risks there would be that she would have a disabled child. The scope of the GPs' duty was to ensure that accurate advice was given on that issue, and they were liable only for the financial consequences of their advice on that issue being incorrect. They invoked the well-known and homely example cited by Lord Hoffman in *South Australia Asset Management Corp v York Montague Ltd* [1997] AC 191 ("*SAAMCO*") at 213D-F:

> Rules which make the wrongdoer liable for all the consequences of his wrongful conduct are exceptional and need to be justified by some special policy. Normally the law limits liability to those consequences which are attributable to that which made the act wrongful. In the case of liability in negligence for providing inaccurate information, this would mean liability for the consequences of the information being inaccurate.
>
> I can illustrate the difference between the ordinary principle and that adopted by the Court of Appeal by an example. 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.
>
> On the Court of Appeal's principle, the doctor is responsible for the injury suffered by the mountaineer because it is damage which would not have occurred if he had been given correct information about his knee. He would not have gone on the expedition and would have suffered no injury. On what I have suggested is the more usual principle, the doctor is not liable. The injury has not been caused by the doctor's bad advice because it would have occurred even if the advice had been correct.

On appeal, it was argued (at [21]-[22]) that the *SAAMCO* analysis simply had no application to clinical negligence cases. It was arbitrary and unfair to distinguish, as the case law does, between a parent who did not wish to become pregnant at all (who would recover for any foreseeable disability from which the child suffered) and a parent who wished to avoid a pregnancy where the child might suffer from a particular condition. In any event, the case law established that compensation should be paid for "disabilities arising from all the normal incidents of conception, intra-uterine development and birth".

The appeal was heard by the same seven-judge panel of the Supreme Court as had heard the *Grant Thornton* case, and again three judgments were given; a majority judgment of Lord Hodge and Lord Sales, with which three of their colleagues agreed, and separate judgments by Lord Leggatt and Lord Burrows.

At [28], Lord Hodge and Lord Sales posed the same six questions as in *Grant Thornton* at [6]:

> (1) Is the harm (loss, injury and damage) which is the subject matter of the claim actionable in negligence? (the actionability question)
> (2) What are the risks of harm to the claimant against which the law imposes on the defendant a duty to take care? (the scope of duty question)
> (3) Did the defendant breach his or her duty by his or her act or omission? (the breach question)
> (4) Is the loss for which the claimant seeks damages the consequence of the defendant's act or omission? (the factual causation question)
> (5) Is there a sufficient nexus between a particular element of the harm for which the claimant seeks damages and the subject matter of the defendant's duty of care as analysed at stage 2 above? (the duty nexus question)
> (6) Is a particular element of the harm for which the claimant seeks damages irrecoverable because it is too remote, or because there is a different effective cause (including novus actus interveniens) in relation to it or because the claimant has mitigated his or her loss or has failed to avoid loss which he or she could reasonably have been expected to avoid? (the legal responsibility question)

This analysis, they said at [30], showed the flaw in the claimant's submission, which was to conflate the issues relating to scope of duty and the relation of the harm to the duty (questions 2 and 5) with issues relating to factual causation (question 4) and foreseeability.

Having reviewed the legal foundation for the *SAAMCO* analysis at [31]-[37], Lord Hodge and Lord Sales stated at [38] that it would often be helpful to define the scope of the duty of care before considering issues of breach and causation. It was not therefore helpful to invoke a general principle that an award of damages "seeks, so far as money can, to put the claimant in the position in which he or she would have been absent the defendant's negligence" (at [58]). Losses could be incurred by a claimant which simply fell outside the scope of the duty of care. They disagreed with Lord Burrows' approach in considering duty of care and breach without also considering the scope of the duty (at [59]).

They then went on to reject the claimant's submissions that *SAAMCO* had no application to clinical negligence cases or that an exception should be carved out for such cases. There was "no principled basis" (at [62]) for such an exclusion. The submissions based on 'but for' causation of A's birth or the foreseeability of him being born with autism did not address the question of the scope of the duty (at [64]-[65]). There was nothing novel about the imposition of a duty in these circumstances, and questions of whether it was fair, just and reasonable to impose such a duty are not relevant (at [66]). The outcome was that, because the GPs were consulted by

the claimant to put her "in a position to enable her to make an informed decision in respect of any child which she conceived who was subsequently discovered to be carrying the haemophilia gene". The scope of the duty was therefore to ensure that the claimant was properly informed in relation to that condition, not other possible conditions which the child might foreseeably have. Accordingly, she was only entitled to damages for the consequences of A's haemophilia, not his autism.

There are, perhaps, two points which clinical negligence practitioners must bear in mind from these judgments.

First, it must be borne in mind that the six questions posed by the Supreme Court are specifically directed towards the question of the scope of a duty of care. They are careful to state at [28] that they are "not an exclusive or comprehensive analysis". The case was not concerned with the quite separate question of whether any duty of care was owed at all, which is an inquiry which logically precedes the determination of the scope of any such duty. It was, rightly, common ground that the GPs owed the claimant a duty of care in relation to the advice that they gave her. Nor was it concerned with the issue of foreseeability, which is a different question to that posed in question 1, which whether the loss is of a type which is actionable (such as personal injury, damage to property or, in certain cases, economic loss) rather than non-actionable (such as distress, annoyance, disappointment etc). It was common ground that it was foreseeable that A could be born with autism. Foreseeability is an aspect of remoteness of damage, which is one of the "legal filters" addressed in question 6 (at [56]).

Secondly, it is very important to remember that doctors' duties of care will not normally be narrowly confined to preventing particular types of damage. As was said by the majority (at [63]):

> In many, and probably a large majority of, cases of clinical negligence the application of the scope of duty principle results in the conclusion that a type of loss or an element of a claimant's loss is within the scope of the defendant's duty, without the court having to address the *SAAMCO* counterfactual. Where a surgeon negligently performs an operation and causes both physical injury and consequent economic loss to the patient, both types of loss will normally be within the scope of the defendant's duty of care. In other words, by undertaking the operation on the patient the surgeon takes responsibility for physical harm caused by any lack of skill and care in performing the operation and for consequential economic loss. Similarly, when a general medical practitioner negligently prescribes unsuitable medication, thereby causing injury or failing to prevent the development of an otherwise preventable medical condition, both the injury or condition and the consequential economic loss will generally be within the scope of the defendant's duty. The negligent care of a mother in the final stages of pregnancy can sadly have the result of the birth of a baby with brain damage and the defendant is normally liable to pay compensation for both the injury and the consequential additional cost of caring for the disabled child. In the *Parkinson* and *Groom* cases the object of the service undertaken was to prevent the birth of any child as in each case the mother did not want to have any more children. In *Parkinson* the service undertaken was to prevent a pregnancy while in *Groom* the task which should have been performed was to make sure that the mother was not pregnant notwithstanding her recent sterilisation. In both cases the added economic costs of caring for a disabled child, whatever his or her disability, were within the scope of the defendant's liability because of the nature of the service which the defendant had undertaken. In none of those cases did the *SAAMCO* counterfactual have a role to play.

It is also important to bear in mind that if a patient presents to a doctor seeking advice about a specific condition, the doctor's duty of care is not necessarily restricted to that task. As Lord Leggatt said (at [84]):

> .... a doctor's duty will sometimes extend to addressing a matter on which the patient has not asked for advice but which the doctor recognises or ought to recognise poses a material risk to the patient. ....

Whether or not that is so, of course, will depend on the facts. For example, it may not be legitimate to impose a duty on a busy GP with a full practice list to identify

some condition about which the claimant makes no complaint unless it is fairly obvious that there is something wrong. With those qualifications, however, Khan is a timely reminder to clinical negligence practitioners to focus at an early stage on the essential question: why did this patient see this doctor? It is not enough simply to assume that because a patient went to see a doctor, the necessary treatment or advice fell within the scope of a doctor's duty of care.

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