

Part IV

Common Law Legal Systems



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England and Wales

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I. Bank Civil Liability for Mis-selling and Advice

A. Introduction

The financial crisis of 2007–08 and ensuing economic slowdown have resulted in many legal and regulatory claims against UK banking institutions by their customers and third parties for mis-selling financial products and rendering inadequate advice and disclosure regarding their risks. Generally, English law liability rules tend to favour banks and impose a heavy burden on investors and customers to prove breach of any statutory, common law or fiduciary duties. A major hurdle for a claimant bank customer to overcome is to show that the bank owed it a duty of care in the sale of a product or the rendering of advice regarding the risks associated with the bank's products and investments. English common law generally allows a bank and its customer to contract out of the duty of care, resulting in an arm's length relationship between the bank and the customer in which the bank has no obligation to inform or advise its client, nor to reveal any of the risks associated with its product or to assess the suitability of its customer for the products it sells. Without a duty of care, the bank merely has an obligation not to make explicit material misrepresentations to its customers regarding its products.

As a result, claims against banks for breach of a duty of care or fiduciary duties under English law have rarely succeeded. Nevertheless, the impact of the financial crisis resulted in unexpected and crippling losses for millions of individuals and small businesses in addition to substantial losses for professional investors, all of which have resulted in an unprecedented number of civil lawsuits against banks for breach of the duty of care, in particular claims for misrepresentation, negligent advice, failure of the duty to warn and investigate. Moreover, several million complaints have been filed with the UK financial regulator—the Financial Conduct

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Authority and its predecessor the Financial Services Authority—against banks for failing to treat their customers fairly and for breach of other regulatory principles in the sale of financial products.

In addition, the harshness for bank customers of the common law's *caveat emptor* approach to bank sales has been limited to some extent by the English courts in several recent rulings following the financial crisis.¹ Moreover, European Union law has sought to make it more difficult for banks to dispense with the duty of care obligation by contracting and to guarantee certain minimum rights for bank customers—especially small business customers—to recover compensation from banks who have mis-sold financial products. This chapter attempts to understand the nature and scope of a bank's duty of care under English common law and UK statutory and regulatory law. In doing so, it reviews the basic principles of English contract law and related areas of tort and fiduciary duties law. UK regulatory law will be discussed to show how it attempts to reverse the erosion of the duty of care under the common law by requiring banks to treat all of their customers fairly and to adopt governance and organisational structures so that the development of financial products takes due account of the interests of bank customers. Finally, European Union law in the form of the Market in Financial Instruments Directive II will be discussed to show how banks will be required to undertake further reforms in governance and trading practices so that banks will have an obligation to recognise a duty of care for their customers in a far greater number of transactions.

B. The Duty of Care and Freedom of Contract

A fundamental principle of English law, which militates against successful claims against banks, is freedom of contract, whereby parties negotiate their own terms which are generally upheld by the courts pursuant to the doctrine of contractual estoppel to ensure commercial certainty and that a bank does not generally owe a duty of care to its customers to advise on the merits of transactions unless the bank has expressly undertaken to do so in which case the bank would be required to advise with reasonable care and skill.² Despite the growth of statutory and regulatory obligations for banks, 'party autonomy is at the heart of English commercial law'.³ In the absence of statutory or regulatory intervention, the courts give effect

¹ See *Rubenstein v HSBC* [2011] EWHC 2304 (QB) at [83] (discussed below). See also *Crestsign v The Royal Bank of Scotland* [2014] EWHC 3043 (Ch) at [88]–[89], [108].

² *Thornbridge Limited v Barclays Bank Plc* [2015] EWHC 3430 (QB) at [6], per Moulder J, upholding that a bank does not have a duty of care to advise a customer on the merits of a transaction unless the bank has undertaken to do so. *Thornbridge* also reaffirms a strict application of the doctrine of contractual estoppel that a bank customer that has signed an undertaking that it has not received advice from a bank on a particular transaction cannot later sue the bank for negligent advice even if the bank in fact had rendered erroneous advice or information about the transaction.

³ See *Belmont Park Investments Pty Ltd v BNY Corporate Trustee Service Ltd (Revenue and Customs Commissioners intervening)* [2011] UKSC 38; [2012] 1 AC 383, per Lord Collins at [103].

to the contractual terms which the parties have freely agreed in writing and are reluctant to imply terms into a contract.⁴ The courts respect the freedom of the parties to agree terms of their own choosing as expressed by the 'plain words' of the contract, and they are reluctant to interpret the words by using assumptions as to what they were purportedly intended to achieve without clear support from the natural and ordinary meaning of the words themselves.⁵ This is particularly so for banks involved in the sale of complex financial instruments.⁶ Moreover, the absence of any principle of good faith or unconscionability in English law further protects banks from a high volume of claims.⁷

A crucial case in recent years that reaffirms the principle of freedom of contract in litigation involving banks was *Bankers Trust International plc v PT Dharmala Sakti Sejahtera*,⁸ involving the sale of interest rate swaps to an Indonesian company, which suffered a loss of US \$45 million after the US Federal Reserve raised interest rates. The bank sued the Indonesian company for US \$65 million in English court. The defendant company argued that the bank was guilty of misrepresentation, breach of contract and breach of duty of care. The Court rejected these claims on the grounds that commercial parties engaged in business are presumed to understand or seek advice about their area of operation and documentation. Moreover, the Court accepted that the bank staff believed the company's personnel had a sophisticated understanding of the nature and risks of the interest rate swaps sold. The Court was not satisfied that the plaintiff bank had made any representations as to profitability, suitability and safety of the financial products or that a full and fair presentation as to the products would have resulted in a different outcome for the defendant company. Nevertheless, the Court affirmed the bank's duty not

⁴ The court's primary emphasis on giving effect to what the parties have freely agreed in writing without reference to the principles of good faith and unconscionability, has been attributed to the fundamental change in English contract law doctrine in the 19th century in which a communitarian and paternalistic approach to interpreting contracts was replaced by a market-oriented ideology that emphasised party autonomy and freedom of contract. See M Lobban, 'Contractual Fraud in Law and Equity' (1997) 17(3) *Oxford Journal of Legal Studies* 441–76, citing PS Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford: Oxford University Press, 1979) discussing the orthodox view of the transformation of English contract law, while citing other commentators (eg AWB Simpson, 'The Horwitz Thesis and the History of Contracts' (1979) *University of Chicago Law Review* 533) who argued that contract law in the 18th century was not so paternalistic as merchants and traders were allowed to set their own terms by, inter alia, evading the law of usury for certain transactions. Lobban, however, provides a more nuanced view of this transition from a communitarian to party autonomy approach for interpreting contractual terms in the case of fraud.

⁵ See *Anthracite Rtrade Investments (Jersey) Ltd v Lehman Brothers Finance SA (In Liquidation)* [2011] EWHC 1822 (Ch); [2011] 2 Lloyd's Rep 538 (the Court determined the meaning and effect of early close-out provisions in 2 cash settled put options incorporating the 1992 ISDA Master Agreement, which were part of larger investment structures devised and marketed by Lehman Brothers).

⁶ See *Belmont Park Investments Pty Ltd* (n 3) per Lord Collins at [104].

⁷ Sir Ross Cranston QC, 'The (non-)liability of Banks under English Law' (International legal symposium in honour of the 50th anniversary of the Marianne and Marcus Wallenberg Foundation, 'Functional or Dysfunctional—the Law as a Cure? Risks and Liability in the Financial Markets' (Stockholm Centre for Commercial Law, 29 and 30 August 2013) 1 (on file with author).

⁸ [1996] CLC 518.

to carelessly misstate facts but to state them fairly and accurately, and that there was a duty to present the financial implications of the products by a comprehensive graph and letter with disclosure about the downside and upside risks of the investment. Despite the court's recognition of the bank's duty not to act carelessly and to present the financial risks of investment products in a transparent manner, the defendant did not prevail on the merits of the bank's claim for enforcement of the contract.

i. Doctrine of Contractual Estoppel

British banks rely on the principle of freedom of contract to prevent their customers from relying on facts and occurrences that are extrinsic to the written terms of the contract. English common law permits this through the doctrine of contractual estoppel whereby parties are estopped from denying contractual terms expressed in writing, even if these are contrary to the real facts or give rise to unjust results.⁹ For example, the courts have upheld an entire agreement clause where the parties acknowledge they have not been induced to enter the contract by representations other than in the contract such that a party cannot subsequently assert a misrepresentation that occurred outside the written contract.¹⁰ As discussed above, the courts interpret contracts according to their natural and ordinary meaning¹¹ to achieve commercial common sense. The courts therefore can exclude any reference to facts—despite their truthfulness—that contradict the terms and undertakings entered into by parties to the contract. The courts however will set aside the doctrine if its strict application would be unreasonable under the circumstances where, for instance, there was unequal bargaining power and understanding of the nature of the risks between the parties, or that the bank had sold a complex product that it knew or should have known was unsuitable to a retail or unsophisticated commercial customer. Banks are permitted however to require retail customers who in fact suffer from unequal bargaining power to agree to undertakings in the written contract that they understand the nature of the risks in the financial product and that they are suitable customers to purchase the product, even though the bank may suspect that they are not suitable. The courts presume that such customers and larger commercial parties and professional investors do not suffer unequal bargaining power in commercial transactions and therefore do not warrant special protection.¹² In considering whether there is unequal bargaining power between the parties, the courts look to the disclosures of the parties

⁹ See *Barclays Bank Plc v Svizera Holdings BV* [2014] EWHC 1020 (Comm), per Flaux J at [58]. See also *Springwell Navigation Corporation v JP Morgan Chase Bank & Ors* [2010] EWCA Civ 1221 and *Cassa Di Risparmio Della Repubblica Di San Marino Spa v Barclays Bank Ltd* [2011] EWHC 484 (Comm) at 505, per Hamblen J.

¹⁰ *Cassa di Risparmio della Repubblica di San Marino v Barclays Bank Ltd* (n 9) at 525, per Hamblen J.

¹¹ *Re Lehman Brothers International (Europe) (In Administration)* [2013] EWCA Civ 188.

¹² See *Thornbridge Limited v Barclays Bank Plc* (n 2) per Moulder J at [79]–[83].

at the time the contract is entered into or at the relevant times as set forth in the contract.¹³

The doctrine of contractual estoppel was first developed in the case of *Peekay Intermark Ltd v Australia and New Zealand Banking Group Ltd*¹⁴ which involved an investment product being sold by the bank to an Isle of Man company (an investment vehicle for United Arab Emirate investors) with repayment linked to the performance of Russian government bonds. A bank employee had mis-described the product as yielding an interest in those bonds. The investor signed the documentation which contained risk warnings and terms that the customer understood the true nature of the contract and determined its suitability, had taken independent advice and was not relying on the bank. The Court ruled that the contract gave rise to an estoppel.

The doctrine was later confirmed in *Springwell Navigation Corp v JP Morgan Chase Bank and others*,¹⁵ which involved the bank selling US \$87 million of notes linked to Russian bonds to Springwell, the investment vehicle of the Polemis shipping group. Springwell claimed the bank was in breach of contractual, tortious and fiduciary duties for misrepresentation when it advised that the products were conservative, liquid and without currency risk. The Court of Appeal rejected this claim on the basis that these were mere statements of opinion, not even implied representations, and that the bank had objective and reasonable grounds for its views. The notes also contained terms and conditions which provided that the bank had not made any representations or warranties claimed by Springwell and various terms stating that the claimant had the knowledge and experience to assess suitability of the investment, to understand the risks, had obtained independent advice and been provided with all the information it requested.¹⁶ The Court held that Springwell was contractually estopped from claiming misrepresentation.

Contractual estoppel, particularly in commercial transactions where it has the purpose of promoting certainty, has also been confirmed in various first instance decisions. In *Titan Steel Wheels Ltd v Royal Bank of Scotland plc*,¹⁷ the Court upheld the validity of the mandate issued by the investor claimant to the bank for execution of transactions involving foreign exchange and currency options, which

¹³ See *Grupo Hotelero Urvasco SA v Carey Value Added SL* [2013] EWHC 1039 (Comm), per Blair J, a case involving an investment firm that had agreed to loan funds to a developer. Blair J interpreted a material adverse change clause in terms of the financial information of the borrower at the relevant times as set forth in the contract and whether any change in financial information provided by the borrower at a time not specified by the contract could be considered as material so as to affect significantly their ability to repay the loan and disadvantage the lender and awarded the borrower the benefit of the doubt regarding their access to and action upon financial information at the time of entering into the contract with the lender.

¹⁴ [2006] EWCA Civ 386; see also Cranston, 'The (non)-liability of Banks under English Law' (n 7) 5.

¹⁵ [2010] EWCA Civ 1221.

¹⁶ *ibid*, [45], [49], [52], [141], [170]–[172], [182], available at: www.bailii.org/ew/cases/EWCA/Civ/2010/1221.html#back230.

¹⁷ [2010] EWHC 211 (Comm).

stated the investor would not rely on the skill or expertise of the bank when entering any transactions and the bank's terms of business expressly excluded advisory services and provided for execution-only services. The Court disagreed with the claimant's assertion that the resources available to the bank to assess the suitability of the products were greater than those of the investor and found that there was no inequality of bargaining power.

Further, in *Raiffeisen Zentralbank Österreich AG v Royal Bank of Scotland Plc*,¹⁸ the claimant bank sought to recover part of a syndicated loan it had lost owing to the collapse of Enron and alleged misrepresentation against the defendant bank, which arranged and syndicated the loan.¹⁹ The Court held that the representations were not misleading or fraudulent and observed that the claimant bank was experienced in the syndicated loan market, had previously participated in syndications with Enron and that it was an arm's length transaction entered after mature deliberations and the contractual provisions were in a form habitually used in the market. Further, the information memorandum and confidentiality agreement were disclosed and signed by the claimant.

In addition, the courts have recognised statutory exceptions to the doctrine of contractual estoppel in the form of the Misrepresentation Act 1967,²⁰ which aims to prevent exemptions from liability for misrepresentations (test of reasonableness, which includes inequality of bargaining power) and the Unfair Contract Terms Act 1977, which aims to prevent standard form contracts rendering a contractual performance substantially different from what was reasonably expected.²¹

ii. Good Faith and Fiduciary Duties

There is no general duty of good faith in English contract law.²² Lord Ackner in *Walford v Miles*²³ observed that a duty of good faith is 'inherently repugnant' in commercial negotiations. However, in some circumstances, it may be possible to imply a duty on the parties not to act in a manner that is commercially unacceptable to reasonable and honest people.²⁴ Even where a contract contains an express clause of good faith it will be interpreted to focus specifically on the purposes stated and that the parties will work together honestly to achieve those purposes.²⁵

Fiduciary duties involve the fiduciary subordinating its own interests to those of its principal. Examples of recognised fiduciary relationships include: trustee-beneficiary, agent-principal and director-company. English courts are reluctant

¹⁸ [2010] EWHC 1392 (Comm).

¹⁹ *ibid.*

²⁰ *IFE Fund SA v Goldman Sachs International* [2007] All ER (D) 476.

²¹ Unfair Contract Terms Act 1977, s 17(1)(a).

²² See discussion in Cranston (n 7) 15.

²³ [1992] 2 AC 128.

²⁴ *Yam Seng Pte Ltd v International Trade Corporation Ltd* [2013] EWHC 111 (QB).

²⁵ *Compass Group UK and Ireland Ltd (t/a Medirest) v Mid Essex Hospital Services NHS Trust* [2013] EWCA Civ 200.

to recognise fiduciary relationships in commercial contexts, unless analogies are drawn with existing categories.²⁶

An unsuccessful claim for breach of fiduciary duties was raised in *Saltri III Ltd v MD Mezzanine SA SICAR (t/a Mezzanine Facility Agent)*.²⁷ The case involved an acquisition of the Stabilus group by a private equity fund and involved an intercreditor agreement that subordinated mezzanine lenders to senior lenders. The business experienced severe financial problems and was transferred to an investment fund, subject to liabilities to the senior lenders; however, the mezzanine lenders received losses on principal ('haircuts') and received nothing in the restructuring. The mezzanine lenders accused the security trustee who accepted the transfer of breach of trust and fiduciary duty. The Court held that a person can act as a fiduciary in regards to some but not all of their activities. The duty alleged to be breached was in relation to enforcement, which was set out in the intercreditor agreement and superseded any fiduciary duties. The Court cited with approval the principle that the duties of parties governed by arm's length commercial contracts will be determined by the terms of the contract.²⁸ The Court held that the duties of the security trustee were not those of a fiduciary but of a mortgagee who is entitled to act in its own interests even if this is detrimental to the interests of the mortgagor as to the timing and manner of enforcement. Therefore the Court found that the bank was not in breach of its duty.²⁹

More recently, in October 2016, the High Court ruled that the investment bank Goldman Sachs had not exercised undue influence on the Libyan Investment Authority (LIA) when encouraging it to undertake risky derivatives trades.³⁰ The judge also refused to set aside trades that the Libyan wealth fund wanted declared as unconscionable. The ruling does not mention the duty of care per se, but constitutes an illustration of the *caveat emptor*/buyer beware principle in English law, as even despite lavish gifts from the bank to the LIA, 'their relationship did not go beyond the normal cordial and mutually beneficial relationship that grows up between a bank and a client'.³¹

C. Statutory and Regulatory Claims

Customer complaints against UK banks and financial services firms have received much attention in recent years, especially following the British banking crisis of 2007–08. The UK statutory and financial regulatory regimes have created new

²⁶ *Ross River Ltd v Waveley Commercial Ltd* [2013] EWCA Civ 910.

²⁷ [2012] EWHC 3025.

²⁸ *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41; *Halton v Guernroy* [2005] EWHC 1968; *Kelly v Cooper* [1993] AC 205; *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145; *Belmont Park Investments Pty Ltd v BNY Corporate Trustee Services Ltd* [2012] 1 AC 383.

²⁹ *ibid.*

³⁰ *The Libyan Investment Authority v Goldman Sachs International* [2016] EWHC 2530 (Ch).

³¹ *ibid.*, [427 b].

avenues of redress in cases involving vulnerable retail customers—including individuals and small businesses—who are bank customers. The Financial Conduct Authority and the former Financial Services Authority have both played an active role in utilising the Financial Ombudsman Service to settle disputes between banks and retail clients and small business customers.³² The Financial Services Markets Act 2000 established the Financial Ombudsman Service (FOS) that provides a scheme to allow customer complaints to be adjudicated against financial services firms in cases involving general insurance, banking and credit, and investment.³³ Consumer credit later came under its remit on 6 April 2007 based on the Consumer Credit Act 2006.³⁴

The Ombudsman regime has been extensively utilised to file millions of claims against banks for mis-selling financial products, including payment protection insurance (PPI) and derivative products such as interest rate swaps. Since the early 2000s, borrowers who purchased PPI to insure against the risk that they may be unable to maintain loan repayments have sought redress for mis-selling through the FOS and the courts. The courts have clarified the law on PPI mis-selling in several decisions assessing the lawfulness of PPI mis-selling regulations³⁵ and on the unfair relationship between a lender and borrower.

The case of *Harrison & Harrison v Black Horse Limited*³⁶ involved the legal question of whether a lender's failure to disclose the existence or amount of commission from an insurer on their sale of PPI to a customer amounts to unfairness in the relationship between the parties pursuant to section 140A of the Consumer Credit Act 1974 (CCA). Both the High Court³⁷ and Court of Appeal decided the claim against the borrower claimants and their appeal to the Supreme Court was subsequently withdrawn by consent.

The borrowers had also claimed that an unfair relationship was created by the lender's³⁸ breach of the regulator's intermediary conduct of business rules (ICOB rules) and the PPI policy was unsuitable owing to the length of the cover and its cost.³⁹ The facts of the case involved two loans obtained by the borrower from the lender, both taken out with PPI. The second loan was then discharged by refinance

³² The Financial Services Act 2012 abolished the Financial Services Authority and replaced it with a newly established Financial Conduct Authority. The FSA's prudential oversight function for banks, insurance firms and large investment banks was assumed by a newly created Prudential Regulation Authority. See Joint Committee on the draft Financial Services Bill, *Draft Financial Services Bill* (2010–12, HL 236, HC 1447).

³³ See Financial Services and Markets Act 2000, types of complaints: www.financial-ombudsman.org.uk/publications/technical.htm).

³⁴ See Consumer Credit Act 2006, s 59, www.legislation.gov.uk/ukpga/2006/14/section/59.

³⁵ See *R (on application of the British Bankers Association) v Financial Services Authority and Financial Ombudsman Service* [2011] EWHC 999.

³⁶ [2011] EWCA Civ 1128.

³⁷ Per Waksman J.

³⁸ The lender was part of the Lloyds TSB Group.

³⁹ The applicability of the ICOB rules to the bank's duty of care in the sale of PPI and other regulated financial products to commercial and individual customers has been reaffirmed in *Saville v Central Capital Ltd* [2014] EWCA Civ 337.

in 2009 and the PPI was cancelled. The PPI was sold by the lender to the borrower as agent for the actual insurer, Lloyds TSB General Insurance Limited; therefore, it was an insurance intermediary acting on an advised basis in relation to the specific PPI offered. The lender earned 87 per cent of the premium in commission from the insurer on the sale of the PPI, which was not at all disclosed to the borrowers.

In the County Court, the claim was dismissed on the grounds that the borrowers were not advised that PPI was compulsory, they had taken PPI before and understood what they were buying and had had the opportunity to understand the terms and freely accept them. In the High Court, Waksman J dismissed the appeal and held there was no breach in relation to cost and policy length and that there was no proof of unfair relationship.

On further appeal, Tomlinson LJ gave the judgment in the Court of Appeal and made the following rulings:

1. There was no breach of ICOB (Insurance: Conduct of Business Rules) rules (and the corresponding statutory duty under section 150 of the Financial Services and Markets Act 2000 (FSMA)).
2. A claim that the PPI was expensive will not be valid. A lender is not required to advise a borrower that a cheaper alternative with the same cover is available elsewhere or on the suitability of the PPI in terms of the cost as the borrowers did not indicate this was relevant to them.
3. If a lender complies with ICOB or ICOBS (Insurance: Conduct of Business Source) it will be very difficult to prove unfairness under section 140A of the Consumer Contract Act (CCA). The level of the commission, at 87 per cent was high; however it did not render the relationship unfair as ICOB did not require its disclosure.⁴⁰ Further, the regulator's (then the Financial Services Authority) list of 15 common failings in its Policy Statement of August 2010 did not include non-disclosure of commission as a failure in PPI selling practices. This ruling therefore prevents a court from considering non-disclosure of commission when assessing fairness between the parties under section 140A.
4. If there is a claim of unfairness under section 140A CCA, the court must consider whether the relationship between the parties is unfair and matters relating to both the lender and borrower.
5. A lender subject to either ICOB or ICOBS is required only to advise on the products it sells, not on whether other cheaper policies are available in the market.
6. Claims of PPI mis-selling must prove the alleged breach of ICOB or ICOBS has caused the borrower actual loss, which is not too remote and that the borrower has mitigated their loss. Claiming a refund of the PPI costs paid is not enough.

⁴⁰ Various FSA consultations concluded disclosure of commissions would not add to consumer protection.

7. The amount of compensation will be reduced where the borrower has been contributorily negligent, which will be significant if they fail to exercise their right to cancel.

This decision has raised the bar of proof even higher for borrowers seeking compensation for alleged PPI mis-selling—in particular, it cannot be argued that a lender's failure to disclose their commission created an unfair relationship under section 140A of the CCA. Alternatively, borrowers can seek redress through the FOS which applies a fairness test to decide cases and tends to result in a more favourable outcome for borrowers.⁴¹

Subsequent claims have been brought, however, in the courts on the basis of distinguishing the case on the facts. For example, the claimants in *Langley v Paragon Personal Finance Limited* (unreported) argued the case was different as it involved a broker, but the Court rejected this claim and awarded the lender Paragon indemnity costs. Arguably, the receipt of a high commission for selling PPI is relevant to a borrower as disclosure of this fact could result in the borrower seeking advice or products from another PPI seller or even a loan from another lender. Despite *Langley v Paragon*, the High Court judgment in 2011 upholding the PPI mis-selling regulatory scheme against a challenge by the British Bankers Association (BBA) had the effect of increasing the number of successful claims.

The cumulative effect on PPI mis-selling claims of these High Court judgments appears *prima facie* to be overall neutral. The slightly later 2011 decision in *Harrison* (see above), which found in favour of the lender, had the potentially opposite effect of discouraging and limiting claims. A future case with a new factual scenario may challenge the current status quo on PPI mis-selling.

In summary, all banks that sell financial products and services to UK clients and customers are generally subject to a duty of care in the sale of these products and services. The duty of care, however, is subject to limitations imposed by the principle of freedom of contract and the contractual estoppel doctrine. A bank has a duty of care not carelessly to misstate facts—which is breached to the extent that its representations or statements are inaccurate or false. However, a duty of care to advise its clients of the risks or on the suitability of a product 'should not be readily inferred in a commercial relationship'.⁴² As discussed in section II below, depending on the financial product or investment sold, the duty of care could entail a duty to investigate the suitability of the products sold to customers and, if appropriate, a duty to warn customers of the risks of investing in these products.

⁴¹ The vast bulk of mis-selling claims against British banks have been decided by the FOS in favour of customer claimants based on the UK regulatory principle of treating customers fairly. See FOS, 'consumer factsheet on payment protection insurance' www.financial-ombudsman.org.uk/publications/factsheets/payment-protection-insurance.pdf. See also 'How does the Ombudsman approach redress where a PPI policy has been mis-sold?': 'What we consider to be fair and reasonable redress will depend on the individual circumstances of the complaint', www.financial-ombudsman.org.uk/publications/technical_notes/ppi/redress.html.

⁴² See *Bankers Trust International plc v PT Dharmala Sakti Sejahtera* [1996] CLC 518 at 531, per Mance J.

II. The Tests for Determining the Bank's Duty of Care and to Investigate and Warn

As implied in the previous section, a bank's duty of care could entail a duty to investigate the suitability of the products sold to customers and a duty to warn customers of the risks of investing in the products. As discussed above, however, these duties are subject to limitations imposed by the principle of freedom of contract and the contractual estoppel doctrine.

A. Commercial and Consumer Clients

Under English law, establishing a bank's duty of care in a tort claim for pure economic loss is the first—and possibly most important step—in holding the bank liable for its duty to investigate the suitability of the product for its customer and duty to warn its customers of the risks related to the financial products and services it provides. The duty of care arises if one of three tests are met for establishing a duty of care:⁴³ (1) assumption of responsibility; (2) a threefold test showing whether the loss to the claimant was a reasonably foreseeable consequence of what the defendant did or failed to do; whether the parties' relationship was sufficiently proximate; and whether it was fair, just and reasonable to impose a duty of care; and (3) the incremental or policy test: that the law should develop novel categories of negligence incrementally and by analogy with established categories.⁴⁴

The first test assesses whether the defendant, objectively, assumed responsibility for their statements or conduct in relation to the claimant, or can be treated as having done so. Alternatively, the second test consists of three elements that the claimant must show to demonstrate a duty of care in negligence:

- the harm must be reasonably foreseeable as a result of the defendant's conduct;
- the parties must be in a relationship of proximity; and
- it must be fair, just and reasonable to impose liability.

This three-limbed test is known as the *Caparo Industries*⁴⁵ test to establish the existence of a duty of care. It was applied by the Court of Appeal in a 2009 case⁴⁶ to show whether a duty of care had been created by a bank to professional investors

⁴³ Lord Bingham cited the 3 tests in an important House of Lords decision, *Commissioners of Customs and Excise v Barclays Bank plc* Times Law Reports, 22 June 2006; [2006] UKHL 28.

⁴⁴ This third condition is addressed in greater detail in *Sutherland Shire Council v Heyman* (1985) 157 CLR 424, 481.

⁴⁵ See *Caparo Industries plc v Dickman* [1990] 2 AC 605.

⁴⁶ *So v HSBC Bank plc* [2009] EWCA Civ 296.

for alleged misrepresentations in the offer document. The Court held that for the duty of care to be established the *Caparo Industries* test required that the investor show whether the loss was a reasonably foreseeable consequence of the bank's conduct, whether the relationship between the parties was of sufficient proximity, and whether it was fair, just and reasonable to impose a duty of care on the bank towards the investor. Alternatively, the third test is known as the incremental test, which provides that new categories of negligence should be developed incrementally and by analogy with established categories.⁴⁷ This test has been criticised, however, for providing limited assistance in determining whether a duty of care has arisen because it does not provide any measurable criteria, and some observers refer to it as a policy catch-all test.⁴⁸

In the context of a bank's potential liability for breaching its duty of care, Lord Bingham made the following general observations:

1. These were cases where one party could accurately be said to have *assumed responsibility* for what was said or done to another: the paradigm situation being a relationship having *all the indicia of contract save consideration*.
2. An assumption of responsibility was to be regarded as a sufficient but not a necessary condition of liability, a first test which, if answered positively, might obviate the need for further inquiry; if answered negatively, further consideration was called for.
3. The assumption of responsibility test was to be *applied objectively* and was not answered by what the defendant thought or intended.
4. The problem here was that the further the test was removed from the actions and intentions of the actual defendant, and the more notional the assumption of responsibility became, the less difference there was between that test and the threefold test.
5. The threefold test itself provided no straightforward answer to the vexed question whether or not in a novel situation a party owed a duty of care: see *Caparo*.
6. The incremental test was of little value in itself and was only helpful when used in combination with a test or principle which identified the legally significant features of a situation.
7. The closer the facts of the case in issue to a case in which a duty of care had been held to exist, the readier a court would be, on the approach adopted in *Caparo*, to find that there had been an assumption of responsibility or that the proximity and policy conditions of the threefold test were satisfied. The converse was also true.
8. The outcomes of the leading cases were in almost every instance sensible and just, irrespective of the test applied.

⁴⁷ *Customs & Excise Commissioners v Barclays Bank plc* (n 43) [32]–[33], 43, discussing application of *Caparo* test to the facts in *Customs*.

⁴⁸ *Customs & Excise Commissioners v Barclays Bank plc* (n 43) [32], per Lord Bingham, [49] per Lord Rodger, [72] per Lord Rodger.

9. That was not to disparage the value of and need for a test of liability in tortious negligence, which any law of tort must propound if it was not to become a morass of single instances. But it concentrated attention on the detailed circumstances of the particular case and the particular relationship between the parties in the context of their legal and factual situation as a whole.⁴⁹

Despite the *Caparo* limitations in establishing a duty of care between a bank and commercial or individual clients, which make it difficult to prevail in a claim against the bank, the duty of care issue is the most frequently invoked issue in financial litigation regarding the bank's rendering of advice, or failing to give advice. Commercial or consumer investors who claim that there has been a breach of the duty of care at common law may also assert an additional claim for breach of regulatory requirement for the provision of suitable and adequate advice in the sale of financial products or investments. Section 138D (previously section 150) of FSMA provides a statutory right of action where breach of UK regulatory requirements cause loss to a private investor. As with claims for negligence or misrepresentation at common law, however, the claimant still has a high bar to surmount under section 138D to establish liability of the bank.

B. Causation and the Bank's Duties to Consumer Clients and Commercial Customers

Even if the bank's customer can establish that the bank owed it a duty of care, it additionally must show that the breach caused the loss in question and that the loss was foreseeable. As discussed in the previous section, the nature and scope of the bank's duty of care to its retail clients or consumer customers is defined by the *Caparo Industries* three-step test for establishing a duty of care (see above). The causation issue has arisen in several prominent cases where investor claims against banks have failed as they were unable to prove the reasonable foreseeability of loss. In *So v HSBC Bank plc*,⁵⁰ the Court applied the *Caparo Industries* three-limbed test to ascertain whether a duty of care had been established:⁵¹ whether loss was a reasonably foreseeable consequence of the bank's conduct, whether the relationship between the parties was of sufficient proximity and whether it was fair, just and reasonable to impose a duty of care on the bank towards the investor. In this case, the investors transferred US \$30 million into the bank account of a fraudster and the bank issued to the investors a letter of instruction which stated that the bank would act only on the instructions of investors to pay out the funds in the account; however, the letter was issued negligently. The Court held the investors' loss was

⁴⁹ See Lord Bingham, *Customs & Excise Commissioners v Barclays Bank plc* (n 43) at [192].

⁵⁰ [2009] EWCA Civ 296.

⁵¹ *Caparo Industries plc v Dickman* (n 45); *Customs & Excise Commissioners v Barclays Bank plc* (n 43).

not caused by the bank's breach of duty but because there was no joint account giving them direct control over their money with HSBC.⁵²

Another case, *Camerata Property Inc v Credit Suisse Securities (Europe) Ltd (No 2)*,⁵³ involved both the common law and statutory duties regarding a bank providing negligent advice on the riskiness of an investment product. In this case, the bank advised an investor to buy a note betting on the dollar weakening against the euro. The investor lost the investment when the US investment bank Lehman Brothers collapsed in 2008; however, if this collapse had not happened, the note would have paid off substantially. The Court found that even if the bank would have advised to sell the note, the investor would have retained the note, therefore there was no reliance and causation. Further, the investor claimed that they were negligently advised to buy the note, that it was an unsuitable investment and that therefore there was a breach of section 150 of FSMA. The claims failed; however, even if fault by the bank had been established, the 2008 collapse of Lehman Brothers was reasonably unforeseeable in 2007 when the note was purchased.

Similarly, causation was an issue in *Al Sulaiman v Credit Suisse Securities (Europe) Ltd*,⁵⁴ where the investor claimed that the risks of leveraged investments in structured notes had not been adequately explained to her. The Court found that any explanation would not have affected her desire to achieve higher returns and she would have invested in the notes in any event. Moreover, she was advised to sell the notes or put up margin; however, she refused and this broke any chain of causation.

Rubenstein v HSBC Bank plc,⁵⁵ however, is an example of a successful claim against a bank, where a solicitor sought advice about investing the proceeds of the sale of his home. The bank advised him to invest in AIG bonds and said that the bond was the same as a cash deposit, however the solicitor's money was invested in an enhanced variable rate fund in which the investor was entitled only to its value at the time of requesting withdrawal, which depended on the underlying assets in the fund, including derivatives. The trial judge held that the bank was negligent in its advice, on which the solicitor had relied and breached various statutory duties. However, the solicitor received only nominal damages at first instance as the Court found that the loss was caused by unprecedented market turmoil which was unforeseeable and too remote. However, on appeal, the Court disagreed and found that the loss was not too remote, and that 'what had caused Mr Rubenstein to suffer a loss might be said to be the very thing which he had wished to avoid: the risk of loss to his capital'.⁵⁶

⁵² *So v HSBC Bank plc* (n 46) [71] and [73], available at: www.bailii.org/ew/cases/EWCA/Civ/2009/296.html.

⁵³ [2012] EWHC 7 (Comm).

⁵⁴ [2013] EWHC 400 (Comm).

⁵⁵ [2012] EWCA Civ 1184, available at: www.bailii.org/ew/cases/EWCA/Civ/2012/1184.html.

⁵⁶ *ibid*, [70]–[71]. The Court discusses its reasoning further at [94], [95], [103], [115], [121], and discusses the facts of the case at [85]–[93].

C. UK Regulatory Law

The competent UK regulatory authorities have adopted legally binding regulatory rules and standards to ensure that banks treat their customers fairly and afford them adequate redress for violations of statute and regulation. This has had the effect of expanding the scope of the banks' potential liability. As discussed in section I, the most prominent application of UK regulatory rules to banks' mis-selling of financial products came in respect of the sale of payment protection insurance (PPI). The Financial Services Authority adopted regulatory guidelines and a policy statement on PPI complaints handling.⁵⁷ The FSA Statement on PPI mis-selling included amendments to the Handbook rules, guidance on how PPI sales complaints should be decided, an open letter to the BBA and others including a list of 'common failings' in PPI sales and guidance on a redress mechanism and a root cause analysis for customers who had not complained.

The lawfulness of the FSA's PPI mis-selling policy statement and guidelines were upheld by the High Court against a legal challenge by the BBA.⁵⁸ The main legal issue raised by the BBA was whether the FSA had the authority to issue a policy that included a statement that the FSA's main Principles (general statements by the FSA of conduct required of financial services firms)⁵⁹ would be taken into account when the Financial Ombudsman Service made decisions on whether compensation would be 'fair and reasonable' under section 228(2) of FSMA.

The judgment was a setback for the banks, as PPI sales have been a notorious source of customer complaints for years. The judgment upheld the validity of PPI mis-selling complaints that were filed against banks for conduct that preceded the FSA's adoption of the PPI mis-selling policy statement in 2010. The decision allows PPI claims to be judged by reference to the new rules and guidance of the 2010 policy statement, even if the sale complied with the applicable rules in effect at the date of sale. Moreover, the policy statement adopted a 'root cause analysis' of systemic but historical failings of bank mis-selling practices in which banks would be advised by the regulator to contact customers who may never have made a complaint and to offer them compensation if there was something sufficiently questionable about the bank's PPI policy or practice. The decision has had an important impact on the banking industry's liability to compensate customers for PPI mis-selling. In 2015, though PPI claims have fallen, the FOS has upheld over 60 per cent of mis-selling claims.

⁵⁷ See the FSA's Policy Statement 10/12 of 10 August 2010: '*The Assessment and Redress of Payment Protection Insurance Complaints*' (the Statement, available on http://www.fsa.gov.uk/library/policy/policy/2010/10_12.shtml).

⁵⁸ See *R (on application of the British Bankers Association) v Financial Services Authority and Financial Ombudsman Service* (n 35) (per Ouseley J).

⁵⁹ Contained in Ch 2 of 'Principles for Business' (PRIN) in the FSA Handbook, include: Integrity; Skill, care and diligence; Customers' interests; Communications with clients; and Customers' relationships of trust.

The effect of the 2011 High Court judgment was to facilitate the initiation and continuation of thousands of complaints and claims against banks that are still being heard by the FOS and the courts.

D. European Legislation—MiFID II

European Union legislation substantially impacts UK financial regulatory law. The Market in Financial Instruments Directive (Directive 2004/39/EC) (MiFID I) was regarded as a milestone in the European Union's regulation of financial markets. MiFID I sets out specific provisions for harmonising the regulation of investment services across the EU and guaranteeing an adequate level of investor protection. The UK implemented MiFID I in 2007. Following the regulatory reforms which took place worldwide after the 2007–08 financial crisis, the European Commission issued legislative proposals to repeal MiFID I through the adoption of Directive 2014/65/EU (MiFID II) and Regulation No 600/2014 (MiFIR).⁶⁰ The European Commission has issued a number of delegated acts further specifying the rules under MiFID II⁶¹ and MiFIR.⁶² Recently, under a regulation and a directive issued on 23 June 2016 the application of MiFID II and MiFIR has been postponed until 3 January 2018.⁶³ Moreover, MiFID II is expected to be transposed into national laws by 3 July 2017. In the wake of the 2016 Brexit referendum, the MiFID legislation will continue to apply until the UK starts the withdrawal procedure pursuant to Article 50 of the 2007 Lisbon Treaty and officially leaves the EU.⁶⁴

⁶⁰ See Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (recast) (2014) OJ L 173/349; see Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 (2014) OJ L 173/84.

⁶¹ See Commission Delegated Regulation of 25.04.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive; see Commission Delegated Directive of 07.04.2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council with regard to safeguarding of financial instruments and funds belonging to clients, products governance obligations and the rules applicable to the provision or reception of fees, commissions or any monetary or non-monetary benefits.

⁶² See Commission Delegated Regulation of 18.05.2016 supplementing Regulation (EU) No 600/2014 of the European Parliament and of the Council with regard to definitions, transparency, portfolio compression and supervisory measures on product intervention and positions; see also, 'Overview and state of play of RTS and ITS relating to MiFID/MiFIR (last updated: 01.02.2017) <http://ec.europa.eu/finance/securities/docs/isd/mifid/its-rts-overview-table_en.pdf>.

⁶³ See Regulation (EU) 2016/1033 of the European Parliament and of the Council of 23 June 2016 amending Regulation (EU) No 600/2014 on markets in financial instruments, Regulation (EU) No 596/2014 on market abuse and Regulation (EU) No 909/2014 on improving securities settlement in the European Union and on central securities depositories (2016) OJ L175/1; see also Directive (EU) 2016/1034 of the European Parliament and of the Council of 23 June 2016 amending Directive 2014/65/EU on markets in financial instruments (2016) OJ L175/8.

⁶⁴ Under Art 50(2): 'A Member State which decides to withdraw shall notify the European Council of its intention. In the light of the guidelines provided by the European Council, the Union shall negotiate and conclude an agreement with that State, setting out the arrangements for its withdrawal, taking

This means that the UK will have to comply with the current MiFID's application and transposition dates, unless the terms of withdrawal are agreed before.

In relation to the banks' duty of care, it is worth mentioning those rules of the revised legislation that set out organisational requirements and conduct of business provisions. As to the investment firms' organisational requirements, reference is made to the new provisions on product governance arrangements relating to firms which develop financial products and to those which sell them. The purpose of such provisions is to enhance the firms' understanding of the products they develop or sell and to ensure that they are suitable to the clients to whom they are being sold.⁶⁵ To this end, investment firms are required to maintain, operate and review the process for approval of each financial instrument and significant adaptations of existing financial instruments before it is marketed or distributed to clients.⁶⁶ Moreover, specific record-keeping provisions have been laid down in the context of the organisational requirements. In particular, records shall include the recording of telephone conversations or electronic communications relating to, at least, transactions concluded when dealing on own account and the provision of client order services that relate to the reception, transmission and execution of client orders. Investment firms must also notify new and existing clients that telephone communications or conversations between the investment firm and its clients that result, or may result, in transactions will be recorded.⁶⁷

Sales targets and remuneration rules are also relevant in the context of a bank's duty of care. Indeed, such rules are based on the European Securities and Markets Authority's Guidelines on Remuneration Policies and Practices and aim at ensuring that staff incentives do not result in conflict of interests or impinge upon the firm's obligation to act in the best interest of the client.⁶⁸ Finally, as to conduct of business, Articles 25 and 27 of MiFID II narrow the list of execution-only products and widen the list of information investment firms have to provide with regard to best execution.⁶⁹

Compared to MiFID I, MiFID II aims to enhance the level of protection of different categories of clients. However, there will be room for further analysis once the implementation process is completed in accordance with the Commission's ongoing level 2 rule-making process and the final level 3 compliance and enforcement stage. Before the Brexit referendum, the UK competent authorities

account of the framework for its future relationship with the Union. That agreement shall be negotiated in accordance with Article 218(3) of the Treaty on the Functioning of the European Union. It shall be concluded on behalf of the Union by the Council, acting by a qualified majority, after obtaining the consent of the European Parliament.

⁶⁵ See Art 16 of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (recast) OJ L 173/349.

⁶⁶ Directive 2014/65/EU, Art 16(3).

⁶⁷ Directive 2014/65/EU, Art 16(6) and (7).

⁶⁸ Directive 2014/65/EU, Art 24(10).

⁶⁹ Directive 2014/65/EU, Arts 25 and 27.

were considering the necessary changes for transposing MiFID II and MiFIR into domestic legislation.⁷⁰ In particular, they were assessing the impact that the new EU legislation may have on the ability of UK credit institutions and investment firms to contract out of their duty of care to retail and wholesale customers and to use the doctrine of contractual estoppel to limit their liability to both consumer and commercial customers.⁷¹ As mentioned above, the extent and scope of the EU legislation will not be known until 2018. The UK vote for 'leave' has triggered a period of uncertainty. Nonetheless, 'firms must continue to abide by their obligations under UK law, including those derived from EU law and continue with implementation plans for legislation that is still to come into effect'.⁷²

III. The Bank's Duty to Professional Investors

English courts have generally followed the doctrine of *Hedley Byrne*⁷³ and *Caparo Industries*⁷⁴ in holding that a claimant does not have a legal claim against a third party with whom the claimant does not have a direct relationship (ie privity of contract), unless there are facts to show that the third party has made some representations to, or established some type of direct relationship with, the claimant in respect of its claim. Following the financial crisis of 2007–08, a growing number of legal claims were filed by professional and other sophisticated investors against third party banks who acted as arrangers or managers in the sale of structured finance and other complex financial products. For example, a professional investor holding a structured debt instrument issued as part of a securitisation who suffered losses as a result of negligent statements or misrepresentations in the sale of that product might look for redress to those parties who made the statements and promoted the products (the 'managers') or to those parties who structured the investment (the 'arrangers'). A preliminary issue would be whether the managers/arrangers acted *reasonably* and, if they did not, whether they are *liable* in negligence for making a false statement about the product or rendering negligent advice to its customer in deciding whether to purchase the product. If they did not act reasonably or acted deceitfully, to prove liability the investor must first show

⁷⁰ The Financial Services and Markets Act 2000 (Qualifying EU Provisions) (Amendment) Order 2016. This Order applies some amendments to the Financial Services and Markets Act 2000 (Qualifying EU Provisions) Order 2013. The purpose of these amendments is twofold: (1) to make the Markets in Financial Instruments Regulation (MiFIR) a qualifying EU provision for various parts of FMSA; and (2) to ensure that the FCA and PRA have the appropriate powers to perform their roles under MiFIR.

⁷¹ See HM Treasury, 'Transposition of the Market in Financial Instruments Directive II' (March 2015) HMT Consultation Paper www.gov.uk/government/uploads/system/uploads/attachment_data/file/418281/PU_1750_MiFID_II_26.03.15.pdf.

⁷² FCA, 'Statement on European Union referendum result' (2016) www.fca.org.uk/news/statements/statement-european-union-referendum-result.

⁷³ *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1963] 2 All ER 575; [1964] AC 465.

⁷⁴ *Caparo Industries plc v Dickman* (n 45).

whether the bank—as a manager or arranger of the product—owed a duty of care to the investor.

In these cases, the English courts have generally resisted expanding the scope of liability to third party banks because, as arrangers or managers of the sale of the complex financial product, they were not the issuers or the sellers of the product or securities in question. Instead, a special purpose vehicle (SPV) that was a separate legal entity was the seller or the issuer. Therefore, the banks were not parties to the contract with the claimant investors who purchased the investment products. Moreover, the investment contract entered into by the investors with the SPV expressly stated that the investors did not rely on any representations that were not stated in writing in the contract. In other words, any marketing statements or promotions provided by the bank as arranger or manager had no legal effect with respect to liability in the issuance or sale of the investment product.

A. The Bank's Duty of Care as Manager or Arranger in Offering Circulars and other Marketing Documents for Securities

The UK regulatory regime reinforces this market practice by not attributing responsibility for false statements or misrepresentations to managers or arrangers in an offering circular for debt instruments issued in a securitisation.⁷⁵ This is because the issuance of such debt instruments in a securitisation is typically an exempt transaction under FSMA. Even if listed on a regulated market, they will be 'specialist securities' that are dealt with in a 'professionals-only market' where sophisticated investors can be expected to assess the risks and protect their own interests. In this type of market, the regulatory standards will at most place responsibility only on those who expressly state that they accept responsibility for misstatements in the offering circular. Moreover, the UK regulations require that at least one person be named on the offering circular as accepting responsibility for its content; this will almost always be the issuer, and not the manager or arranger.

A bank's liability as a manager or arranger for misstatements in an offering circular for *exempt* or *specialist* debt instruments issued in a securitisation,

⁷⁵ Many of the securitisation litigation cases arising from the financial crisis relate to residential mortgage-backed securities (RMBS). RMBS are structured in the following way: loans are made to a current or potential homeowner by a loan originator, who often funds the loans through a warehouse line of credit supplied by a sponsor. The originator then transfers the loans to the sponsor, who pools thousands of them and then transfers the pool to a depositor, a bankruptcy remote entity affiliated with the sponsor that is created solely to receive and transfer the rights to the loans. The depositor transfers the pools to an issuing trust, and securitises the pool by dividing it into several tranches, corresponding to a different level of risk and reward. In exchange for the mortgages, the trust provides the depositor with certificates that represent interests in the trust. The depositor issues the certificates to underwriters, who then sell them to investors. See K Alexander and SL Schwarcz, *Macroprudential Regulation—A Conceptual Approach* (Oxford: Oxford University Press, 2017).

therefore, is highly questionable, as it is unlikely that a duty of care will arise by virtue of the offering circular itself. There must be an express statement that the manager/arranger has accepted responsibility for representations made in the offering circular; otherwise, the issuer will likely be the named party on the document to be held liable for any misrepresentations. In contrast, regarding *non-exempt* or *non-specialist* securities, it can be argued under English law that those who have authorised the contents of the document (ie prospectus or offering circular), such as the managers/arrangers, are responsible for its contents, and responsibility can be demonstrated merely by appending the bank's name to the bottom (or top) of the first page of the circular or offering document. This is not the case, however, regarding debt instruments issued in a securitisation, as it is unlikely that a duty of care will arise between the manager/arranger and investor merely on the basis of the contents of the offering circular itself. For example, a bank may be the lead 'manager' or 'co-lead manager' of an issuance of debt securities based on a securitisation, and the bank's name may be listed on the first page of the offering circular. In the London market, practitioners would presume that the bank's name listed prominently on the circular would be done for the bank's own marketing purposes, and not as a representation of the truthfulness of the document's contents. As a matter of law and practice, therefore, it will rarely be enough, without more, to show that the bank's role as manager or arranger of a particular issue is enough to create a duty of care between the bank and the potential investor in the issue.

Nevertheless, as discussed in the cases above, a duty of care can arise by a manager or arranger by voluntarily assuming responsibility for the truthfulness or correctness of what is stated in an offering document for the issue of debt securities based on a securitisation. The English courts have held that a duty of care can arise between the manager/arranger and investor in debt securities of a securitisation where the offering document does not contain an express disclaimer of responsibility for the manager/arranger. In such a case, English courts will look to the facts of each case to determine whether a manager or arranger did in fact assume responsibility for any representations contained in the offering document and additionally will look to extrinsic communications between the manager/arranger and investor to see if the manager/arranger provided specific answers to a particular investor's questions that the manager/arranger knew—or should have known—would induce that specific investor to invest in the issue. This factual situation arose in a 2008 case known as the *Boxclever* litigation that took place in the London Commercial Court. In this case, the French bank Natixis brought a claim against the Canadian bank (CIBC) and the German bank WestLandesbank (WestLB) for losses based on a note it purchased in a securitisation of the Boxclever group. Natixis alleged, amongst other things, that CIBC, as co-lead manager of the issue, and WestLB, as arranger of the issue, owed it a duty of care in respect of representations made in the offering circular and based on extrinsic communications. The case settled, however, and no judicial opinion was issued.

A subsequent case, *IFE v Goldman Sachs*,⁷⁶ stands for the above proposition that where there is an express disclaimer of responsibility for the manager/arranger in the offering documents there will be no duty of care and therefore no liability for the manager/arranger for unreasonable or false statements made in the offering documents on which the investor may have relied. In this case, IFE had purchased from Goldman Sachs (GSI), bonds and warrants issued by a French company, Autodis SA, for €20 million, which formed part of syndicated credit facilities provided to Autodis for the acquisition of an English company, Finelist Group plc. The credit facilities were provided in tiers, IFE financed the mezzanine facility, which was arranged by GSI, who also underwrote the mezzanine facility. Autodis' acquisition was unsuccessful, it was revealed that Finelist's financial position was misrepresented and it was placed into receivership. IFE brought an action against GSI for its losses, on the grounds of misrepresentation, pursuant to section 2(1) of the Misrepresentation Act 1967,⁷⁷ and common law negligence. IFE claimed it was induced to enter into the transaction by information provided by GSI in the syndication information memorandum (SIM), which presented a picture that was in fact misleading and which was not corrected or qualified after they had cause to doubt its reliability as a result of receiving two reports from accountants. GSI had made an express disclaimer in the SIM as to the accuracy or completeness of the SIM: that the information in it had been derived from many sources and was not to form the basis of any contract; that GSI had not independently verified the information and gave no representation, warranty or undertaking, express or implied, and did not accept responsibility for its accuracy; and that the information was not to be assumed to have been updated and did not constitute a representation by any person that the information would be updated. The court dismissed the claim and made the following rulings:

1. A reasonable person would not have understood that GSI was making any implied representations as alleged by IFE.⁷⁸
2. There was a difference between actual knowledge that information previously supplied was misleading and acquiring information which merely gave rise to a possibility that the information previously supplied was misleading, which did not give rise to a duty to investigate the matter further, or advise the participant.

⁷⁶ *IFE Fund SA v Goldman Sachs International* (n 20).

⁷⁷ 'Where a person has entered into a contract after a misrepresentation has been made to him by another party thereto and as a result thereof he has suffered loss, then, if the person making the misrepresentation would be liable to damages in respect thereof had the misrepresentation been made fraudulently, that person shall be so liable notwithstanding that the misrepresentation was not made fraudulently, unless he proves that he had reasonable ground to believe and did believe up to the time the contract was made that the facts represented were true.'

⁷⁸ Goldman argued that its representations stated, among other things, that it was not aware of any facts which showed that the statements about Finelist's financial performance made in the Memorandum were or might be incorrect in any material way; and/or which showed that the opinions expressed in the Memorandum Reports were not or might not be reasonable.

3. GSI was not acting as an adviser to IFE or purporting to carry out any professional service, it was acting for the sponsors, therefore it did not owe the duty of care which IFE alleged.
4. Contractual disclaimer terms between the parties ruled out any representation that the information would be reviewed at any stage before the recipient acquired the bonds.
5. The only implied representation was one of good faith.
6. The extensive disclaimer, which negated any assumption of responsibility, meant that no duty of care arose.

The *IFE v Goldman Sachs* case also clarifies the application of a statutory remedy for misrepresentation under the Misrepresentation Act 1967 by holding that the effect of an express disclaimer in an offering circular is to prevent a representation from having been made in the first place, thereby precluding an allegation of misrepresentation under the Misrepresentation Act 1967.

In *Raiffeisen Zentralbank Österreich AG v Royal Bank of Scotland plc*,⁷⁹ the Court cited with approval the *IFE* test for the express statement test: ‘the court has to consider what a reasonable person would have understood from the words used in the context in which they were used; The Court in this case further elaborated on this test in relation to the relevant factors in construing the express statement: ‘nature and content of the statement, the context in which it was made, the characteristics of the maker and of the person to whom it was made, and the relationship between them’.⁸⁰

The Court also cited *IFE* as authority for the rule that whether any representations were made has to be decided by reference to the provisions of the information memorandum (IM) and the confidentiality agreement as they are an important part of the context in which the representations are said to have been made, and are thus relevant to any inquiry as to what representation a reasonable reader of the IM would regard as having been made.⁸¹ Further, the Court approved the finding in *IFE* of ‘an implied representation that, in supplying the information memorandum, Goldman Sachs was acting in good faith, ie was not knowingly putting forward information likely to mislead’.⁸² Moreover, the Court cited⁸³ with approval a passage from *IFE* on the nature of the ‘disclaimers’ in the SIM:

The relevant paragraphs of the SIM are not in my view to be characterised in substance as a notice excluding or restricting a liability for negligence, but more fundamentally as going to the issue *whether there was a relationship between the parties* (amounting to or equivalent to that of professional adviser and advisee).⁸⁴

⁷⁹ [2010] All ER (D) 111. The facts of the case were summarised in section I.B.i.

⁸⁰ *ibid*, [82].

⁸¹ *ibid*, [97].

⁸² *ibid*, [264].

⁸³ *ibid*, [294].

⁸⁴ *IFE Fund SA v Goldman Sachs International* (n 20) [70]–[71] per Toulson J, approved by Court of Appeal per Waller J at [28].

Following the *Raiffeisen Zentralbank* and *IFE* cases, the classic English judicial formulation of the narrowness of the bank duty of care doctrine in the structured financial product market occurred in *Cassa di Risparmio della Repubblica di San Marino SpA v Barclays Bank Ltd*,⁸⁵ also a case involving the mis-selling of complex structured financial products. This important case is now viewed as a test case for other potential cases involving the mis-selling of complex structured finance investments. The claim related to a series of structured finance notes (CDO²) with a total nominal value of €406 million which were structured by Barclays and sold to Cassa di Risparmio della Repubblica di San Marino SpA (CRSM) in 2004 and 2005 and to a subsequent restructuring of the transactions. CRSM issued proceedings, alleging fraudulent misrepresentation, and claimed damages for deceit, or alternatively under section 2(1) of the Misrepresentation Act 1967, or alternatively for a breach of an implied term of the contracts of sale or restructure. However, all claims brought by CRSM against Barclays were dismissed by Hamblen J of the Commercial Court in a judgment delivered on 9 March 2011.

The total amount lent by Barclays to CRSM's subsidiaries, the Delta Companies, was €700m, spread over several tranches and over a period of eight months, and supported by five Credit Linked Notes (CLNs) transactions with aggregate principal of €450m. The four disputed CLNs were comprised of €176m credit default swaps (CDS) on the Delta Companies, and €230m in CDO². The CDO² were all single tranche synthetic transactions, where CRSM purchased a bespoke mezzanine tranche and Barclays effectively held the equity and senior tranches. Each CDO consisted of six inner CDOs and AAA-rate asset-backed securities (ABS) such that the overall rating of each Note was AAA. CRSM intended to hold the Notes until maturity; the key risk for CRSM was the 'credit risk' of the CDO²s—that is, the risk that CRSM would cease to receive the full coupon and would not get back the full principal amount when the Notes matured, if a sufficient number and combination of 'credit events' (eg insolvency or default on a debt) occurred in relation to entities named in the portfolios underlying the CDO²s. In March 2005, CRSM expressed concern about the presence of certain names in the reference portfolios, following which Barclays implemented on 14 June 2005 a restructuring of the four CDOs, with two components: (1) replacing some of the reference entities and (2) adding 'cross-subordination' to the CDO structures. In late 2005 the quality of the CDO began to deteriorate as defaults in the underlying reference entities began to occur. In April 2006, Barclays agreed to repurchase the various CDOs and in February 2010 Barclays formally notified CRSM that the principal of some of the Notes had been reduced to zero. The Court made the following rulings:

1. The use of ratings in representations to clients; a statement by an arranging bank about a AAA rating was not a general statement about risk or probability of default, but only a statement about the rating agency's opinion.⁸⁶

⁸⁵ [2011] EWHC 484 (Comm).

⁸⁶ *ibid*, [264].

2. Historical default data, gathered over long periods covering all phases of the business cycle, are a reliable source for estimating expected future default rates.⁸⁷
3. Hamblen J rejected CRSM's claim that the model used to compute Barclays' expected P&L could also be used to estimate the probability of default (PDs) expected over the life of the Notes.⁸⁸
4. A contractual term in the sales contracts (similar to an ISDA non-reliance clause) would in any event have precluded the claim under contractual estoppel, with no finding of fraud. By the term, CRSM warranted that it understood and accepted the terms, conditions and risk of purchasing the notes.⁸⁹

The Court affirmed the following principles of law:

1. It was established law that the tort of deceit involved the making of a false representation by a defendant, knowing it to be untrue, or being reckless as to whether it was true, and intending the claimant should act in reliance on it.⁹⁰
2. Section 2(1) of the Misrepresentation Act, required proof of: (1) a representation made by the defendant; (2) which was false; (3) which induced the claimant to enter into the relevant contract; and (4) as a result of which the claimant suffered loss.⁹¹
3. A representation was a statement of fact made by the representor to the representee on which the representee was intended and entitled to rely as a positive assertion that the fact was true. In order to determine whether or what representation was made by a statement required: (1) construing the statement in the context in which it had been made; and (2) interpreting the statement objectively according to the impact it might be expected to have on a reasonable representee in the position and with the known characteristics of the actual representee. In order to be actionable, a representation had to be as to a matter of fact. A statement of opinion was therefore not in itself actionable. Where, however, the facts were not equally well known to both sides, a statement of opinion by one who knew the facts best might carry with it a further implication of fact, namely that the representor by expressing that opinion had impliedly stated that he believed that facts existed which reasonably justified it. A statement as to the future might imply a statement as to present intention. By itself, silence could not found a claim in misrepresentation. However, an express statement which was literally true might nevertheless involve a misrepresentation because of matters which the representor omitted to mention. In a deceit case, it was also necessary that the representor should

⁸⁷ *ibid*, [296].

⁸⁸ *ibid*, [302].

⁸⁹ *ibid*, [525].

⁹⁰ *ibid*, [210]. *AIC Ltd v ITS Testing Services (UK) Ltd; The Kriti Palm* [2006] All ER (D) 381 (Nov).

⁹¹ *ibid*, [212]–[213] and [232]–[233]. *Raiffeisen Zentralbank Österreich AG v Royal Bank of Scotland plc* [2010] All ER (D) 111 (Jun) applied; *County NatWest Bank Ltd v Barton* [1999] All ER (D) 782 applied; *Dadourian Group International Inc v Simms* [2009] All ER (D) 175 (Mar) applied.

understand that he was making the implied representation and that it had the misleading sense alleged.⁹²

4. It was established that the mental element to prove a claim in deceit was proof of fraud: that a false representation had been made knowingly, without belief in its truth, or recklessly, careless whether it be true or false. The unreasonableness of the grounds of the belief, though not of itself supporting an action for deceit, would be evidence from which fraud might be inferred.⁹³
5. It was established law that parties can agree that one party had not made any pre-contract representations, or that any such representations had not been relied on, even if this occurred and that such an agreement might give rise to a contractual estoppel. Clear words were necessary; however, it did not apply where there had been a misrepresentation as to the effect of the contractual documents which gave rise to the estoppel.⁹⁴
6. The statement by Barclays that a CDO had been rated AAA by a credit rating agency had not implied anything more than that the note had been given that rating by an agency, based on its expert opinion; it was not a statement by Barclays about default probabilities or risk.⁹⁵ Therefore, the purchase misrepresentations had not been made.⁹⁶ Even if a representation that the notes would have had a very low risk of default had been made by Barclays such a representation was a matter of opinion and/or expectation, made on reasonable grounds.⁹⁷ Further, CRSM had not proved that it had in fact relied on the purchase representations, had they been made.⁹⁸ Moreover, Barclays had not in fact made any representation that it would not profit from the restructuring.⁹⁹
7. To prove deceit, CRSM would have to establish that the relevant employees of the defendant individually had the necessary subjective understanding and intention for fraud. On the evidence, the relevant employees of the defendant had no intention to mislead the claimant.¹⁰⁰

⁹² *ibid*, [215]–[223] and [232]–[233]. *Smith v Land and House Property Corpn* 28 Ch D 7 applied; *Clydesdale Bank Ltd v Paton* [1895–99] All ER Rep 1136 applied; *Brown v Raphael* [1958] Ch 636 applied; *Goose v Wilson Sandford & Co* [2000] All ER (D) 324 applied; *Kyle Bay Ltd v Underwriters subscribing to policy no 019057/08/01* [2007] All ER (D) 93 (Feb) applied; *Raiffeisen Zentralbank Österreich AG v Royal Bank of Scotland plc* (n 91) applied.

⁹³ *ibid*, [225]–[230]. *Derry v Peek* [1886–90] All ER Rep 1 applied; *Bradford Third Equitable Benefit Building Society v Bolders* [1941] 2 All ER 205 applied; *Standard Chartered Bank v Pakistan National Shipping Corp (No 2)* [2000] 1 All ER (Comm) 1 applied; *AIC Ltd v ITS Testing Services (UK) Ltd; The Kriti Palm* (n 90) applied.

⁹⁴ *ibid*, [505]. *Board of Trade v Steel Bros & Co Ltd* [1952] 1 Lloyd's Rep 87 applied; *Peekay Intermark Ltd v Australia and New Zealand Banking Group Ltd* [2006] All ER (D) 70 (Apr) applied.

⁹⁵ *ibid*, [263] and [264].

⁹⁶ *ibid*, [266].

⁹⁷ *ibid*, [267], [371] and [463].

⁹⁸ *ibid*, [482].

⁹⁹ *ibid*, [278].

¹⁰⁰ *ibid*, [368], [406], [424], [449] and [457].

8. CRSM was contractually estopped from making misrepresentation claims by clauses 5 and 6 of the purchase contracts.¹⁰¹ However, the claimant was not estopped by clause 6 from the claims in respect of representations made in relation to the restructuring transaction, as any representations made did not cause the claimant to misunderstand the risks of entering the restructuring transaction, but they were rather statements as to the criteria to be applied in carrying out the restructuring.¹⁰²
9. In relation to the arbitration claim, the term that CRSM alleged was not to be implied into the contract, as such a term was not capable of clear expression, was not necessary to make the contract work, nor was it reasonable as its inclusion would potentially undermine the practices of the banking market, as arbitration was a common practice. Furthermore, it contradicted the express terms of the contract, and was not what a reasonable person would have understood the contract to mean.¹⁰³

Cassa di Risparmio v Barclays was followed by *Standard Chartered Bank v Ceylon Petroleum Corporation*.¹⁰⁴ In this case, the parties entered into oil derivative transactions, which required SCB to make payments to CPC when oil prices were high while CPC was required to make payments to SCB if the price of oil fell below an agreed floor. When oil prices fell rapidly, CPC became ‘out-of-the-money’ on its derivative transactions and refused to pay SCB the full sums owing. SCB sued for repayment. CPC contended that because it had no experience in commodity derivative transactions and was engaging in novel and sophisticated transactions, SCB had held itself out to CPC as adviser and encouraged it to enter into transactions that did not hedge its risks, but instead provided the prospect of insignificant upfront fixed profits in return for taking on vast and disproportionate downside risk.

The Court rejected the counterclaim and set out the various tests for establishing duty of care in tort:¹⁰⁵

1. the assumption of responsibility test, coupled with reliance;
2. the threefold-test (whether the loss was reasonably foreseeable, whether the relationship between the parties was of sufficient proximity and whether in all the circumstances it was fair just and reasonable to impose such a duty); and
3. the incremental test.

¹⁰¹ *ibid*, [514] and [525]–[526].

¹⁰² *ibid*, [525]–[527].

¹⁰³ *ibid*, [544]–[545]. *BP Refinery (Westernport) Pty Ltd v Hastings Shire Council* 52 ALJR 20 applied; *A-G of Belize v Belize Telecom Ltd* [2009] 2 All ER (Comm) 1 applied; *Mediterranean Salvage and Towage Ltd v Seamar Trading and Commerce Inc; The Reborn* [2010] 1 All ER (Comm) 1 applied. [2011] All ER (D) 113.

¹⁰⁵ *ibid*, [478]–[480]. *Bankers Trust v PT Dharmala Sakti Sejahtera* (n 42) applied; *Williams v Natural Life Health Foods Ltd* [1998] 1 WLR 830 considered; *JP Morgan Chase Bank v Springwell Navigation Corp* [2007] 1 All ER (Comm) 549 considered.

Further, the Court held that to establish inducement by misrepresentation for the purpose of a claim under section 2 of the 1967 Misrepresentation Act, it was necessary to show that, but for the representation, the claimant would not have entered into the contract.¹⁰⁶

The *IFE*, *Cassa di Risparmio* and *Standard Chartered Bank* decisions were cited in *Graiseley Properties Ltd v Barclays Bank Plc*¹⁰⁷ and *Brown v Innovatorone plc*.¹⁰⁸ The Court in *Graiseley Properties Ltd* cited with approval the test for implied representations set out by Toulson J at paragraph 50 in *IFE*:

In determining whether there has been an express representation, and to what effect, the court has to consider what a reasonable person would have understood from the words used in the context in which they were used. In determining what, if any, implied representation has been made, the court has to perform a similar task, except that it has to consider what a reasonable person would have inferred was being implicitly represented by the representor's words and conduct in their context.¹⁰⁹

Brown v Innovatorone plc cited with approval the test for implied representations and restated as follows:

That involves considering whether a reasonable representee in the position and with the known characteristics of the actual representee would reasonably have understood that an implied representation was being made and being made substantially in the terms or to the effect alleged.

The Court in this case also cited with approval the ruling in *IFE* that a disclaimer meant there was no assumption of responsibility and therefore, no duty of care arose.

Based on the above cases, the English courts have taken a narrow view of the duty of care of banks in promoting structured financial products to third party commercial investors who are sold the products by separate legal entities based on contracts that contain express disclaimers that the investors are relying only on representations made in the written contract of sale and not on any representations that the bank may have made—verbal or otherwise—to promote and sell the product. Professional investors have attempted to circumvent these disclaimers by asserting claims in negligence, misrepresentation and/or deceit against the banks that they have engaged in culpable conduct that undermines the integrity of the transaction, and that the banks should be held liable for any false or misleading representations extrinsic to the contract that induced the claimants to purchase the investment product, even though the claimants state in the contract's disclaimer that they have not relied upon an representations extrinsic to the contract. The consistency of the English courts in limiting the bank's duty of care in the sale of structured finance and other wholesale debt investments is well established in

¹⁰⁶ *ibid*, [552].

¹⁰⁷ [2013] All ER (D) 100 (Nov).

¹⁰⁸ [2012] All ER (D) 273 (May, 2013).

¹⁰⁹ *Graiseley Properties Ltd v Barclays Bank Plc* (n 107) [19].

case law and undoubtedly is part of a broader legal policy to maintain London's preeminent position in the global capital markets for the issuance and trading of these instruments. It would be in line with this reasoning to suggest that the bank's duty of care would be even further restricted had a case arisen where an investor claimed to suffer loss as a result of the actions of a bank they had no binding contract with.

Generally, the legal principles and doctrines of contract, tort and fiduciary duties that determine the content and scope of the bank's duty of care to its customers and third parties are also applicable to other professional service providers, such as the Lloyd's reinsurance network and auditors.¹¹⁰ Generally, the English courts recognise the principles established in *Hedley Byrne*¹¹¹ and *Caparo Industries*¹¹² that hold that a claimant does not have a legal claim against a third party (ie professional services provider) with whom the claimant does not have a direct relationship (ie privity of contract), unless there are facts to show that the third party has made some representations to, or established some type of direct relationship with, the claimant in respect of its claim. The three tests for establishing a duty of care¹¹³ articulated by Lord Bingham in *Commissioners of Customs and Excise v Barclays Bank plc*¹¹⁴ are applicable: (1) assumption of responsibility; (2) a threefold test showing whether the loss to the claimant was a reasonably foreseeable consequence of what the defendant did or failed to do; whether the parties' relationship was sufficiently proximate; and whether it was fair, just and reasonable to impose a duty of care; and (3) the incremental test: that the law should develop novel categories of negligence incrementally and by analogy with established categories.¹¹⁵

In *Merrett Syndicates Ltd*,¹¹⁶ the assumption of liability test was set forth by the House of Lords in a case involving Lloyd's names as plaintiffs who were members of syndicates managed by the defendant underwriting agents. The relationship between names, members' agents and managing agents was regulated by the terms of agency agreements which gave the agent 'absolute discretion' in respect

¹¹⁰ As stated above, banks are not subject to autonomous duties, but rather duties deriving from contract law, tort law, trust law or fiduciary duties, and public law, especially regulatory law under FSMA. See the discussion of public regulatory law in s II.A that derives from s 138D of the Financial Services and Markets Act 2000 (implementing the relevant provisions of the EU Market in Financial Instruments Directive 2004).

¹¹¹ *Hedley Byrne & Co Ltd v Heller & Partners Ltd* (n 73).

¹¹² *Caparo Industries plc v Dickman* (n 45).

¹¹³ In setting forth these tests, Lord Bingham cited the leading cases: *Hedley Byrne & Co Ltd v Heller & Partners Ltd* (n 73), *Ministry of Housing and Local Government v Sharp* [1970] 2 QB 223, *Smith v Eric S Bush* [1989] 2 All ER 514, *Caparo Industries plc v Dickman* (n 45), *Henderson v Merrett Syndicates Ltd* (n 28); *White v Jones* [1995] 1 All ER 691, [1995] 2 AC 207; *Spring v Guardian Assurance plc* [1994] 3 All ER 129, [1995] 2 AC 296; *Williams v Natural Life Health Foods Ltd* (n 105) and *Phelps v Hillingdon London Borough Council* [2000] 4 All ER 504, [2001] 2 AC 619.

¹¹⁴ *Commissioners of Customs and Excise v Barclays Bank plc* (n 43).

¹¹⁵ This third condition is addressed in greater detail in *Sutherland Shire Council v Heyman* (n 44).

¹¹⁶ *Henderson v Merrett Syndicates Ltd* (n 28).

of underwriting business conducted on behalf of the name but *it was accepted that it was an implied term of the agreements that the agents would exercise due care and skill in the exercise of their functions as managing agents* (italics added). The plaintiffs brought proceedings against the defendants alleging that the defendants had been negligent in the conduct and management of the plaintiffs' syndicates, and wished, for limitation purposes, to establish a duty of care in tort in addition to any contractual duty that might be owed by the defendants.

The High Court addressed the following issues:

1. whether members' agents owed a duty of care to direct names notwithstanding the contractual relationship between the parties;
2. whether managing agents appointed as sub-agents by members' agents owed a duty of care to indirect names;
3. whether members' agents were responsible to names for any failure to exercise reasonable skill and care on the part of managing agents to whom underwriting was delegated by the members' agents; and
4. whether the members' agents were required to exercise skill and care only in relation to those activities and functions which members' agents by custom and practice actually performed for the names personally.

The judge found in favour of the plaintiffs on all the issues. The defendants' appeal to the Court of Appeal was dismissed. A further appeal to the House of Lords was dismissed on the following grounds:

1. Where a person *assumed responsibility* to perform professional or quasi-professional services for another who *relied* on those services, the relationship between the parties was itself sufficient, without more, to give rise to a duty on the part of the person providing the services to exercise reasonable skill and care in doing so. Accordingly, managing agents at Lloyd's owed a duty of care to names who were members of syndicates under the agents' management, since the agents by holding themselves out as possessing a special expertise to advise the names on the suitability of risks to be underwritten and on the circumstances in which, and the extent to which, reinsurance should be taken out and claims should be settled, plainly assumed responsibility towards the names in their syndicates. Moreover, names, as the managing agents well knew, placed *implicit reliance* on that expertise, in that they *gave authority* to the managing agents to bind them to contracts of insurance and reinsurance and to the settlement of claims. The fact that the agency and sub-agency agreements gave the agent 'absolute discretion' in respect of underwriting business conducted on behalf of the names did not have the effect of excluding a duty of care, contractual or otherwise. The discretion given to agents merely defined the scope of the agents' authority, not the standard of skill and care required of agents in carrying on underwriting business on behalf of names.
2. An *assumption of responsibility* by a person rendering professional or quasi-professional services coupled with a *concomitant reliance* by the person

for whom the services were rendered could give rise to a tortious duty of care irrespective of whether there was a contractual relationship between the parties. In consequence, unless the contract between the parties precluded him from doing so, a plaintiff who had available to him concurrent remedies in contract and tort was entitled to choose that remedy which appeared to him to be the most advantageous. In the case of direct names their contract with their members' agents did not operate to exclude a tortious duty, since it was an implied term that the agents would exercise due care and skill in the exercise of their functions as managing agents under the agreement and that duty of care was no different from the duty of care owed by them to the names in tort. Accordingly, it was open to direct names to pursue either remedy against the agents. Likewise, indirect names were not prevented by the chain of contracts contained in the agency and sub-agency agreements from suing managing agents in tort. In particular, the fact that the managing agents had, with the consent of the indirect names, assumed responsibility in respect of the relevant activities to another party, ie the members' agents, under a sub-agency agreement did not prevent the managing agents assuming responsibility in respect of the same activities to the indirect names.¹¹⁷

B. The Bank's Liability to Pay Compensation/Damages for Breaching the Duty of Care

This section addresses damages that arise in tort for a bank that breaches its duty of care. These damages would also apply in the case of breaches of the duty to investigate and to warn. The general purpose of damages in tort is to put the claimant in the same position as if the tort had not been committed.¹¹⁸ In order to award damages in tort, a court will consider the following issue heads.

¹¹⁷ Clause 2(a) of the agency agreement prescribed by Lloyd's Byelaw No 4 of 1984 contained an express undertaking by the underwriting agent to act as the underwriting agent of the name, whether the agent was acting as a members' agent or was a combined agent acting as managing agent in respect of a syndicate of which the name was a member, the only difference being that in the former case the members' agent carried out the underwriting through the agency of a managing agent under the terms of the prescribed form of sub-agency agreement, whereas in the latter case the agent carried out the underwriting itself. It followed that members' agents were responsible to the names for any failure to exercise reasonable skill and care on the part of managing agents to whom underwriting was delegated by the members' agents.

¹¹⁸ *Livingstone v Rawyards Coal Co* (1880) 5 App Cas 25 at 39, per Lord Blackburn; *Monarch Steamship Co v Karlshamns Oljefarbriker AB* [1949] AC 196 at 221, [1949] 1 All ER 1 at 12–13, HL, per Lord Wright; *Liesbosch Dredger v SS Edison* [1933] AC 449 at 463, HL, per Lord Wright. Exceptionally there may be liability for loss of expectation: *White v Jones* (n 113); *Ross v Caunters* [1980] Ch 297, [1979] 3 All ER 580.

i. Remoteness

The wrongdoer is only responsible for any type of damage which should have been foreseen by a reasonable person¹¹⁹ as being something of which there was a real risk,¹²⁰ even though the risk would actually occur only in very exceptional circumstances, or in the most unusual case,¹²¹ unless the risk was so small that the reasonable person would feel justified in neglecting it¹²² or brushing it aside as far-fetched.¹²³ The magnitude of the risk, namely the likelihood of the occurrence and the gravity of potential results, must be weighed against the expense of eliminating it.¹²⁴ The assessment by the courts of remoteness of damages is demonstrated in some recent cases cited below.

In *Rubenstein v HSBC Bank plc*,¹²⁵ the Court observed in the context of a negligent investment advice claim:

If such an investment goes wrong, there will nearly always be other causes (bad management, bad markets, fraud, political change etc): but it will be an exercise in legal judgment to decide whether some change in markets is so extraneous to the validity of the investment advice as to absolve the adviser for failing to carry out his duty or duties on the basis that the result was not within the scope of those duties.

The Court concluded that the plaintiff's loss was not too remote because:

what went wrong was the investment itself, and for the very reason that it was structured in a way which exposed Mr Rubenstein to the very risk (of loss to his capital by reason of market movements) which he had wanted to avoid by investing, as he was led to believe he had, in a safe investment equivalent to a cash deposit.¹²⁶

¹¹⁹ *Overseas Tankship (UK) Ltd v Morts Dock and Engineering Co Ltd, The Wagon Mound* [1961] AC 388, [1961] 1 All ER 404, PC; *Overseas Tankship (UK) Ltd v Miller Steamship Co Pty, The Wagon Mound (No 2)* [1967] 1 AC 617 at 640, [1966] 2 All ER 709 at 716, PC. There is no liability for a foreseeable injury when it is not of a type which the defendant was under a duty to guard against: *Banque Bruxelles Lambert SA v Eagle Star Insurance Co Ltd* [1997] AC 191, sub nom *South Australia Asset Management Corp v York Montague Ltd* [1996] 3 All ER 365, HL (negligent valuer liable only for difference in values immediately after valuation, not for later losses from general collapse of property market).

¹²⁰ *Overseas Tankship (UK) Ltd v Miller Steamship Co Pty, The Wagon Mound (No 2)* [1967] 1 AC 617 at 642, [1966] 2 All ER 709 at 718, PC.

¹²¹ *Koufos v C Czarnikow Ltd* [1969] 1 AC 350 at 385, sub nom *Koufos v C Czarnikow Ltd, The Heron II* [1967] 3 All ER 686 at 692, HL, per Lord Reid (see [851] note 1 ante); *Stewart v West African Terminals Ltd* [1964] 2 Lloyd's Rep 371 at 375, CA, per Lord Denning MR; *Sullivan v South Glamorgan County Council* (1985) 84 LGR 415; *Draper v Hodder* [1972] 2 QB 556, [1972] 2 All ER 210, CA; *The Trecarrell* [1973] 1 Lloyd's Rep 402.

¹²² *Koufos v C Czarnikow Ltd* [1969] 1 AC 350 at 385–86, sub nom *Koufos v C Czarnikow Ltd, The Heron II* [1967] 3 All ER 686 at 692, HL, per Lord Reid, and see at 411 and 708, per Lord Hodson.

¹²³ *Koufos v C Czarnikow Ltd* [1969] 1 AC 350 at 422, sub nom *Koufos v C Czarnikow Ltd, The Heron II* [1967] 3 All ER 686 at 715, HL, per Lord Upjohn; and see *Overseas Tankship (UK) Ltd v Miller Steamship Co Pty, The Wagon Mound (No 2)* [1967] 1 AC 617 at 643, [1966] 2 All ER 709 at 719, PC.

¹²⁴ *Overseas Tankship (UK) Ltd v Miller Steamship Co Pty, The Wagon Mound (No 2)* 1 AC 617 at 642, [1966] 2 All ER 709 at 718, PC.

¹²⁵ [2013] 1 All ER (Comm) 915 at 945.

¹²⁶ *ibid*, 947.

In *Brown v KMR Services Ltd*,¹²⁷ Hobhouse LJ stated:

If it was the duty of the defendants to protect the plaintiff from losses of the kind which he subsequently suffers, how can it be just or appropriate to say that, because those losses are larger than either party anticipated, the plaintiff must bear those losses not the defendants?

In *Camerata Property Inc v Credit Suisse Securities (Europe) Ltd (No 2)*,¹²⁸ Flaux J observed that:

even if Camerata could establish its general wrong advice case and even if it could show that it would not have invested in the Note had it been given the right advice, the claim for damages would still fail because the actual cause of the loss was issuer default as a consequence of the collapse of Lehman Brothers, which was wholly unexpected and unforeseeable.

ii. Measure of Damages

In the context of negligent advice, damages are to place the claimant in the same position as if the misrepresentation had not been made,¹²⁹ under both common law¹³⁰ and the Misrepresentation Act 1967 for negligent misrepresentation,¹³¹ but damages under the Act in substitution for rescission for innocent misrepresentation attract the contractual measure, placing the plaintiff in the same position as if the misrepresentation had been true.¹³²

The first instance judge in *Rubenstein*¹³³ set out the measure of damages as the sum that will place the claimant in the position he would have been in if the contract with the bank had not been breached, that is, if the bank had succeeded in recommending the most suitable investment, using that investment as a comparator.

iii. Interest

English courts have discretion to award simple interest on the damages in respect of which judgment is given or payment is made before judgment.¹³⁴ Interest is at

¹²⁷ [1995] 4 All ER 598 at 643.

¹²⁸ [2012] EWHC 7 (Comm) at 68.

¹²⁹ *Doyle v Olby (Ironmongers) Ltd* CA; *Downs v Chappell* [1997] 1 WLR 426, CA; *Shelley v Paddock* [1980] 1 QB 348 CA; *Archer v Brown* [1985] QB 401, [1984] 2 All ER 267; *McConnel v Wright* [1903] 1 Ch 546, CA; *Twycross v Grant* (1877) 2 CPD 469, CA.

¹³⁰ *Esso Petroleum Co Ltd v Mardon* [1976] QB 801, [1976] 2 All ER 5, CA.

¹³¹ *Roycott Trust Ltd v Rogerson* [1991] 2 QB 297, [1991] 3 All ER 294, CA; *Cemp Properties (UK) Ltd v Dentsply Research and Development Corp* [1991] 2 EGLR 197, CA; *Chesneau v Interhome Ltd* (1983) 134 NLJ 341, CA; *Downs v Chappell* [1996] 3 All ER 344, [1997] 1 WLR 426, CA; *Thomas Witter Ltd v TBP Industries Ltd* [1996] 2 All ER 573.

¹³² *William Sindall plc v Cambridgeshire County Council* [1994] 3 All ER 932 at 962, [1994] 1 WLR 1016 at 1045, CA, per Evans LJ discussing the Misrepresentation Act 1967, s 2(2).

¹³³ *Rubenstein v HSBC Bank Plc* [2011] EWHC 2304 (QB) (02 September 2011), per Judge Havelock-Allan at [124]–[127].

¹³⁴ Senior Courts Act 1981, s 35A(1) (s 35A added by the Administration of Justice Act 1982, s 15(1), Sch 1, Pt 1); the County Courts Act 1984, s 69(1) (amended by the Civil Procedure Act 1997, s 10, Sch 2, para 2(2)).

such rate as the court thinks fit or as rules of court provide on all or any part of the damages for all or any part of the period between the date when the cause of action arose and the date of the judgment or, in the case of any sum paid before judgment, the date of the payment. According to this principle, pre-judgment interest which, in respect of losses, could run only from the respective date of sale of the financial product to the date the investment was sold or cashed-out.

iv. Proving Loss and Damages

Generally, the calculation of damages for the investor's loss is the difference between the purchase price and the value of the asset left with the investor after cashing-out the investment.¹³⁵ There is no deduction for coupon payments that were already received by the investors prior to cashing-out. Measuring the difference between what the claimant paid for the asset it acquired and the benefits left in the claimant's hands (eg income received from the asset during the period the claimant owned it, plus the proceeds from its sale or its value as at the trial date) was considered by an Australian court in *HTW Valuers (Central Qld) Pty Ltd v Astonland Pty Ltd*.¹³⁶

There are no set provisions for courts to calculate damages in cases where several claimants have standing to sue. These cases would either be treated as separate claims against the bank or fall under general UK class action rules¹³⁷ (with their own legal regime containing principles like 'first come first served' or pro rata distribution within a certain limit). All claimants would obviously separately have to fulfil the same basic requirements regarding privity of contract, misrepresentation and reliance or negligence and duty of care, as well as suffer actual loss to be able to sue for the bank's avoidable behaviour.

IV. Limiting the Bank's Liability—Contributory Negligence

A. Contributory Negligence

Under English law, a claimant should take reasonable steps to mitigate their loss in tort¹³⁸ and the defendant must prove that the plaintiff has acted unreasonably.¹³⁹

¹³⁵ See *HTW Valuers (Central Old) Pty Ltd v Astonland Pty Ltd*. (2004) 217 CLR 640, [3463].

¹³⁶ *ibid*, [3373].

¹³⁷ Civil Procedure Rules, pt 19.6, www.justice.gov.uk/courts/procedure-rules/civil/rules/part19.

¹³⁸ *Admiralty Comrs v SS Chekiang* [1926] AC 637 (HL), per Lord Sumner; *Admiralty Comrs v SS Susquehanna, The Susquehanna* [1926] AC 655 at 663, HL, per Lord Sumner; *The Liverpool (No 2)* ER 465 at 474, [1959] 2 Lloyd's Rep 611 at 624 per Lord Merriman P (revsd on other grounds [1960] 3 All ER 307, CA).

¹³⁹ *Roper v Johnson* (1873) LR 8 CP 167; *Garnac Grain Co Inc v HMF Faure & Fairclough Ltd* [1968] AC, [1967] 2 All ER 353, HL; *London and South of England Building Society v Stone* [1983] 3 All ER 105,

Where any person suffers damage as the result partly of his own fault and partly of the fault of any other person, their claim for damages is not defeated but will be reduced to such extent as the court thinks just and equitable having regard to the claimant's share in the responsibility for the damage.¹⁴⁰ The apportionment may be expressed by the court determining the percentage by which the plaintiff contributed to the harm that they suffered and then reducing what would otherwise have been the total of the damages by that percentage. Notwithstanding the above, the trial judge in *Rubenstein v HSBC Bank*¹⁴¹ held that if he had found in favour of the plaintiff on liability, he would not have reduced damages for contributory negligence because the plaintiff had asked the key question about risk of the product and was advised that the risk of investing in it was the same as a cash deposit and therefore he did not need to enquire further about the product.¹⁴²

B. Apportionment of Liability for Multiple Tortfeasors

The bank's exposure to tort liability can be reduced if there are two or more joint tortfeasors liable for the entire damage resulting from the tort.¹⁴³ If each of several persons, not acting jointly, commits a tort against another person substantially contemporaneously and causing the same or indivisible damage, each several tortfeasor is liable for the whole damage.¹⁴⁴ If each of several persons commits an independent tort consecutively against the same person, each is liable for the damage caused by his tortious act, assuming the damage proximately caused by each tort to be distinct.¹⁴⁵ Thus, if the second tortfeasor's act caused no further

[1983] 1 WLR 1242, CA; *Gebruder Metelman GmbH & Co KG v NBR (London) Ltd* [1984] 1 Lloyd's Rep 614 at 631, per Sir John Donaldson MR; *Richardson v Redpath Brown & Co Ltd* [1944] AC 62, [1944] 1 All ER 110, HL.

¹⁴⁰ See particularly cases where the client had ignored advice from the finance professional: *Spreadex Ltd v Sekhon* [2008] EWHC 1136 (Ch): the plaintiff was found to be 85 per cent at fault; *Bank Leumi (UK) plc v Wachner* [2011] EWHC 656 (Comm): Flaux J would have been prepared to hold Mrs Wachner 75 per cent responsible for her loss if he had found in her favour on liability.

¹⁴¹ *Rubenstein v HSBC Bank Plc* [2011] EWHC 2304 (QB) (02 September 2011), per Judge Havelock-Allan.

¹⁴² Reduction of damages for contributory negligence is also available under the Law Reform (Contributory Negligence) Act 1945.

¹⁴³ *Ferguson v Earl of Kinnoull* (1842) 9 Cl & Fin 251, HL; *Clark v Newsam* (1847) 1 Exch 131; *London Association for Protection of Trade v Greenlands Ltd* [1916] 2 AC 15 at 31; *Fish & Fish Ltd v Sea Shepherd UK* [2013] EWCA Civ 544, [2013] All ER (D) 191 (May).

¹⁴⁴ *Devonshire (Owners) v Barge Leslie (Owners)* [1912] AC 634 at 657, HL; *Bank View Mill Ltd v Nelson Corpn and Fryer & Co (Nelson) Ltd* [1942] 2 All ER 477 at 483 per Stable J (revsd on other grounds [1943] 1 KB 337, [1943] 1 All ER 299, CA); *Dingle v Associated Newspapers Ltd* [1961] 2 QB 162 at 189–190, [1961] 1 All ER 897 at 916, CA, per Devlin LJ; *Rahman v Arearose Ltd* [2001] QB 351 at [17], (2000) 62 BMLR 84 at [17], CA, per Laws LJ.

¹⁴⁵ *Dingle v Associated Newspapers Ltd* [1961] 2 QB 162 at 188–89, [1961] 1 All ER 897 at 916, CA, per Devlin LJ; *Holtby v Brigham & Cowan (Hull) Ltd* [2000] 3 All ER 421, [2000] ICR 1086, CA; *Rahman v Arearose Ltd* [2001] QB 351, (2000) 62 BMLR 84, CA.

damage or merely duplicated damage caused by the first tort, the second tortfeasor will not be liable;¹⁴⁶ but, if his act aggravated the damage caused by the first tort, each tortfeasor will be liable only in respect of the part of the damage which his tort caused, assuming that it is possible to separate and quantify the aggravation of damage.¹⁴⁷ Where liability is premised on the material contribution of several tortfeasors to the risk of harm, rather than to the harm itself, their liability is attributed according to their relative degree of contribution to the risk.¹⁴⁸ Any person liable in respect of any damage suffered by another person may recover a contribution from any other person liable in respect of the same damage (whether jointly with him or otherwise).¹⁴⁹

In proceedings for contribution to damages, the amount of the contribution recoverable from any person is such as may be found by the court to be just and equitable having regard to that person's responsibility for the damage;¹⁵⁰ and the court has power to exempt any person from liability to make contribution, or to direct that the contribution is to amount to a complete indemnity.¹⁵¹ The court must have regard both to causation and to the relative blameworthiness of the parties.¹⁵² Where the damages assessed have been

¹⁴⁶ *Carslogie Steamship Co Ltd v Royal Norwegian Government* [1952] AC 292 at 303, [1952] 1 All ER 20 at 25, HL (explaining *The Haversham Grange* [1905] P 307, CA); *Performance Cars Ltd v Abraham* [1962] 1 QB 33, [1961] 3 All ER 413, CA; cf *Baker v Willoughby* [1970] AC 467, [1969] 3 All ER 1528, HL (effect of second tort on first tortfeasor's liability).

¹⁴⁷ *Holby v Brigham & Cowan (Hull) Ltd* [2000] 3 All ER 421, [2000] ICR 1086, CA; *Rahman v Arearose Ltd* [2001] QB 351, (2000) 62 BMLR 84, CA. In the absence of evidence to apportion damage between independent tortfeasors where the damage is not indivisible, the law will, it seems, apportion the damage equally: see *Bank View Mill Ltd v Nelson Corpn and Fryer & Co (Nelson) Ltd* [1942] 2 All ER 477 at 483 per Stable J (revsd on other grounds [1943] KB 337, [1943] 1 All ER 299, CA).

¹⁴⁸ *Barker v Corus UK Ltd* [2006] [2006] UKHL 20, [2006] 2 AC 572, [2006] 3 All ER 785.

¹⁴⁹ Civil Liability (Contribution) Act 1978, ss 1(1) and 7(1); *Adams v Associated Newspapers Ltd* [1999] EMLR 26, CA.

¹⁵⁰ Civil Liability (Contribution) Act 1978 s 2(1).

¹⁵¹ Civil Liability (Contribution) Act 1978 s 2(2); and *Diboll v City of Newcastle* [1993] PIQR P16, CA; *Adams v Associated Newspapers Ltd* [1999] EMLR 26, CA; *Cressman v Coys of Kensington (McDonald, Pt 20 defendant)* [2004] EWCA Civ 47, [2004] 1 WLR 2775, 148 Sol Jo LB 182; *Dubai Aluminium Co Ltd v Salaam (Livingstone, third parties)* [2002] UKHL 48, [2003] 2 AC 366, [2003] 1 All ER 97; *Niru Battery Manufacturing Co v Milestone Trading Ltd (No 2)* [2004] EWCA Civ 487, [2004] 2 Lloyd's Rep 319, [2004] 2 All ER (Comm) 289 at [50], [73] and [78] per Clarke LJ, and at [81] per Sedley LJ; *Charter plc v City Index Ltd (Gawler, Pt 20 defendants)* [2007] EWCA Civ 1382, [2008] Ch 313, [2008] 3 All ER 126.

¹⁵² *Miraflores (Owners) v George Livanos (Owners)* [1967] 1 AC 826 at 845, sub nom *The Miraflores (Owners) and The Abadesa (Owners)* [1967] 1 All ER 672 at 677, HL, per Lord Pearce; *Brown v Thompson* [1968] 2 All ER 708 at 709, [1968] 1 WLR 1003 at 1008, CA, per Winn LJ; *Baker v Willoughby* [1970] AC 467 at 490, [1969] 3 All ER 1528 at 1530, HL, per Lord Reid; *Madden v Quirk* [1989] 1 WLR 702 at 707, [1989] RTR 304 at 309 per Simon Brown J. In apportioning damages, the court may exceptionally have regard to non-causative aspects of a defendant's conduct if there is a close connection between them and the acts or omissions giving rise to liability: *Re-Source America International Ltd v Platt Site Services Ltd (Barkin Construction Ltd, Pt 20 defendant)* [2004] EWCA Civ 665, (2004) 95 Con LR 1; *Brian Warwick Partnership v HOK International Ltd (HOK International Ltd, Pt 20 defendant)* [2005] EWCA Civ 962, 103 Con LR 112.

apportioned as between defendants, the costs remain entirely within the court's discretion and need not be apportioned between the defendants in the same proportion as the damages.¹⁵³

V. Conclusion

This chapter's goal was to provide an overview of the legal regime surrounding a bank's duty of care under the law in force in England and Wales. While traditionally courts tended to be more lenient towards banks and require alleged victims to prove the existence and the breach of a duty of care, the atmosphere has recently changed owing to the financial crisis and the European Union's legislative reaction. The banks' obligations are no longer limited to explicit misrepresentations in breach of contract, especially in cases where the bargaining power between the parties is unequal. Moreover, customers are increasingly protected by UK regulatory law, including the Financial Ombudsman system. While there remains no general duty of good faith in contracting under English law, repugnant and dishonest behaviour is frowned upon enough to influence the court's deliberations. The establishment of a bank's duty of care and the measure of damages to its client must still satisfy the requirements of common law of tort, but is now supported by binding regulatory instruments supervised by the UK's Financial Conduct Authority as well as the European Securities and Markets Authority adoption of technical implementing standards under MiFID II. It remains to be seen how Brexit will influence the relationship between the UK and the EU in banking regulation, particularly the extent to which regulatory law will continue to influence the scope and content of a bank's duty of care.

¹⁵³ *Moy v Pettman Smith (a firm) (No 2)* [2003] EWCA Civ 467, [2003] PNLR 31 (revsd on other grounds: [2005] UKHL 7, [2005] 1 All ER 903, [2005] 1 WLR 581); *Nationwide Building Society v Dunlop Haywards (DHL) Ltd* [2009] EWHC 254 (Comm), [2009] 2 All ER (Comm) 715, [2009] 1 Lloyd's Rep 447. Cf apportionment of cases between claimant and defendant where there is a successful defence of contributory negligence: *William A Jay & Sons v JS Veevers Ltd* [1946] 1 All ER 646; *Howitt v Alexander & Sons* 1948 SC 154, Ct of Sess; *McCarthy v Raylton Productions Ltd* [1951] WN 376, CA (costs following the event). As to the situation where the claimant counterclaims, see *Smith v WH Smith & Sons Ltd* [1952] 1 All ER 528, CA.