

**ARCHITECTS – NEGLIGENCE – NET CONTRIBUTION CLAUSE****STEPHEN WEST (1) DR CAROL WEST (2) v IAN FINLAY & ASSOCIATES****TECHNOLOGY & CONSTRUCTION COURT – 16 APRIL 2013****FACTS**

In June 2005, Mr and Mrs West bought a house in Putney with a view to carrying out major changes to its layout including the lower ground and ground floors. The Wests had a limited budget. After protracted discussions with the architect, a specification of works was agreed. This was on the basis that the Wests would arrange the procurement of certain discrete parts of the work (including the kitchen and conservatory) themselves so that they would not attract either the architect's percentage fee or the contractor's overheads or profit on these items. In June 2006, the Wests entered into a JCT 2005 Intermediate standard form of building contract with the main contractor.

The project was a disaster. After moving in, extensive damp was discovered in the lower ground floor. Further investigations revealed a long list of defects including inadequate damp proofing, the quality of the concrete slab installed in the kitchen area and serious problems with the plumbing and electrical works. The Wests had to move out of the property for 20 months whilst the remedial works were carried out.

The Wests brought a claim against the architects to recover the costs of dealing with the problems which included allegations of negligent and inadequate advice and failure to notice defects in the M&E installations. The main contractor became insolvent. The architect contended that even if it had discovered the defective workmanship, it would never have been rectified and completed by the main contractor because of its poor financial position. The architect also relied on a net contribution clause.

**DECISION**

The judge held the architect liable for failing to exercise reasonable skill and care in its design and inspection services.

The judge adopted the approach set out by Mr Justice Ramsay in *Cooperative Group Ltd v John Allen Associates Ltd (2010)*. The first stage in a claim against a construction professional for design is for the claimant to establish what would have happened if the professional had in fact exercised proper skill and care. If the claimant establishes that, had proper care and skill been used, he would have proceeded with the project in accordance with the proper design then the measure of damages will be the costs of remedying the defects but less a credit for any higher costs that would have been payable for a proper design in the first place.

In response to the architect's arguments on causation in respect of the M&E works, the judge held that this was a case (applying the principles in *Phethean-Hubble v Coles (2012)*) where the onus was on the architect, having been found in breach of duty, to show that even if it had acted with reasonable care the damage would probably still have occurred. On the evidence, the architect failed to establish that the main contractor would not have completed the works.

The net contribution clause limited the architect's liability to "*the amount that it is reasonable for us to pay in relation to the contractual responsibilities of other consultants, contractors and specialists appointed by you*". The clause could be read as meaning everyone with whom the Wests entered into a contract in relation to the project apart from the architect; this would include the main contractor. Alternatively, it could refer to the various specialist contractors or suppliers with whom the Wests were proposing to enter into direct contracts outside the main building contract. Against the factual background, the judge considered the latter to be the natural reading of the words. Further, applying Regulation 7(2) of the Unfair Terms in Consumer Contracts Regulations 1999, where there is doubt

about the meaning of a written term, the interpretation most favourable to the consumer should prevail. Accordingly, the liability of the main contractor did not limit the architect's liability to the Wests.

## **COMMENT**

Although, the judge concluded that the net contribution clause satisfied the fairness test in the Regulations, he rejected the architect's interpretation of the clause. As the evidence indicated that the main contractor was jointly to blame for many of the issues, the clause could have substantially reduced the amount of damages to be paid. The case emphasises the importance of careful drafting to ensure that the clause properly covers the particular circumstances of the project.

The claimants also alleged that the architect should have recommended the use of a standard form contract that provided for contractor's design. Such a contract would have required the contractor to have professional indemnity insurance in respect of its design obligations. The main contractor in this case did not have such insurance. The judge accepted that it would have been good practice for the architect to specify a form of contract that provided for contractor's design but concluded that in circumstances where the contractor's design had to be approved by the services engineer, the architect's approach was one that a reasonably competent architect could properly take.

The judge awarded general damages for inconvenience, distress and discomfort. This included an award of £2000 to the Wests' son who was a baby when the remedial works were being carried out.

**FINANCIAL ADVISERS – NEGLIGENT ADVICE – TAX SCHEMES****CLAIM AGAINST 20TWENTY INDEPENDENT LTD****FINANCIAL OMBUDSMAN SERVICE - APRIL 2013****FACTS\***

Five investors made claims against 20Twenty Independent Ltd alleging that the advice that they gave to invest in Crossover Films Partnerships (a film tax avoidance scheme) was unsuitable. The total losses amounted to almost £2.6 million.

One of the investors was advised that the investment was safer than putting money into his mortgage and another was advised that the investment would be an ideal vehicle for school fees planning.

Although the scheme did qualify for tax relief, the scheme involved loans and the claimants faced demands for repayment of loan capital and interest. These risks were not made clear.

**DECISION**

The Financial Ombudsman Service ("FOS") ruled that the advice given was "unsuitable" and that the claimants were not made aware of the true nature of the losses to which they could be exposed. It was decided that the investment was "so risky" that the investors should have been made aware that it could lead to a "total loss of possibly more than three times their initial contribution".

As the claims were submitted before 1 January 2012, the maximum award that the FOS can enforce is £100,000. (This has been increased to £150,000 for claims submitted after 1 January 2012).

The investors are reported to be looking to recover the balance of their losses through the courts (see *Clark v In Focus Asset Management* below).

**COMMENT**

The low interest rate environment of the last four or so years has led to product providers and advisers looking to develop and sell more complex products to enable higher returns to be made. This increased product complexity is likely to result in more claims being made against IFAs. Last year the FSA proposed a ban on the sale of unregulated collective investment schemes to retail investors.

It is recognised that many claims are likely to be made by wealthy investors in tax avoidance schemes who are facing significant tax bills flowing from the more aggressive stance taken by HM Revenue & Customs in challenging these tax arrangements. However, this case highlights the fact that in many cases the primary risk of these products is not whether tax relief will be granted. The majority of these products are highly-leveraged and are often structured using full recourse loans and are so complex that many investors do not understand the products they are buying into. If the investment fails, the investor can be liable for significantly more than their initial investment. An IFA who fails to fulfil their regulatory requirements is likely to face a claim for those losses.

\*The Financial Ombudsman's decision has not yet been published. The facts of this summary are taken from newspaper and journal articles.

**FINANCIAL ADVISERS – FSO – DOCTRINE OF MERGER****CLARK & ANOR v IN FOCUS ASSET MANAGEMENT & TAX SOLUTIONS LTD****PERMISSION TO APPEAL****BACKGROUND**

We reported on the first instance decision in January 2012. Mr Justice Cranston decided in December 2012 that a claimant could continue to pursue a claim against his adviser through the courts for the balance of his losses after accepting an award made by the Financial Services Ombudsman. In reaching this conclusion, he held that the decision in *Andrews v SBJ Benefit Consultants Ltd (2010)* was wrongly decided.

Permission to appeal this decision has now been granted by the Court of Appeal and the appeal is likely to be heard later this year.

**COMMENT**

The current situation where we have two conflicting High Court decisions is clearly unsatisfactory and clarification on this issue will be welcomed.

As the Ombudsman can only enforce an award up to a maximum of £150,000, whether or not acceptance of the award will prevent court proceedings for the balance of the losses being pursued is obviously an important issue to be decided.

We will report on the result of the appeal as soon as it is available.

**SOLICITORS – FUNDING – NON PARTY COSTS ORDER****GAVIN FLATMAN v GILL GERMANY; WEDDALL v BARCHESTER HEALTH CARE LTD****COURT OF APPEAL – 10 APRIL 2013****FACTS**

The claimants in both actions brought unsuccessful personal injury actions using a Conditional Fee Agreement but without after the event insurance. They were represented by the same firm of solicitors. The defendants obtained orders for costs but were unable to enforce them as the claimants were impecunious.

The defendants believed that the claimants' solicitors had funded the disbursements incurred in the litigation. They therefore sought disclosure of the funding arrangements so that they could make an application for a non-party costs order.

**DECISION**

An order for costs could be made against the solicitor if the solicitor was the "real party" who substantially controlled and benefitted from the proceedings. The Court held that, as legislation visualised the possibility of a solicitor funding disbursements, it would not be right to conclude that such a solicitor was "the real party" or even "a real party". Therefore funding disbursements alone would not justify a conclusion that a solicitor had stepped outside the normal role of a solicitor and be subject to an order to pay costs.

However, on the facts of this case, the court held that disclosure of the funding arrangements was justified. The documents disclosed in one of the actions revealed that the claimant had informed the solicitors in writing that he only wished to proceed with the claim if insurance was in place. Counsel had advised a 20-25% chance of success. Further, the claimant had stated that he did not wish to proceed but felt that he had no alternative since otherwise he would have to pay £10,000 in costs already incurred.

**COMMENT**

Following the implementation of the Jackson reforms this month, it is anticipated that more cases will be run without ATE insurance. It is likely that solicitors will often find themselves funding disbursements to the extent that they will not seek to recover them from the client if the claim fails. The Law Society considered it important to clarify this issue and intervened in the case. Solicitors will be relieved to know that they can fund disbursements without the potential risk of a non-party costs order.

The Court of Appeal held that suspicions about funding alone would not justify an order for disclosure of the funding arrangements. However, Lord Justice Leveson suggested that a defendant with a costs order against an impecunious claimant could "invite" the claimant to reveal the extent of any third party support and to provide any reason why the costs order should not be enforced. Claimants' solicitors could therefore be faced in future with a joint attack from the defendant and their client.

**SOLICITORS – NEGLIGENT ADVICE – COSTS – SUCCESSFUL PARTY****MAGICAL MARKING LTD v WARE & KAY LLP & ORS****CHANCERY DIVISION - LEEDS DISTRICT REGISTRY – 20 MARCH 2013****FACTS**

The solicitors were instructed by the claimants, Magical Marking Ltd (MML) and Mrs Phillis (one of two directors and the majority shareholder) in relation to a dispute with Mr Holly (the second director and minority shareholder). After being removed as a director, Mr Holly set himself up in a competing business using MML's confidential information. The claimants later contended that the solicitors had mishandled the situation and brought a professional negligence against them seeking damages in excess of £10 million.

A hard fought battle ensued culminating in a three week trial involving a trial bundle exceeding 50 lever arch files and detailed expert evidence. The claimants' main grievance in relation to the advice given in respect of the damage caused by Mr Holly's unlawful competition was rejected. However, the judge found that the solicitors were negligent in failing to advise the claimants to make an offer to purchase Mr Holly's shares before his removal; leaving them vulnerable to an unfair prejudice claim under s459 Companies Act 1985. The judge accordingly awarded the claimants damages of £28,000 which representing what the Judge considered to be the consequential uplift of Mr Holly's costs of the s459 litigation included within Mrs Phillis's settlement payment to him.

The claimants sought an order for costs against the defendant solicitors, interest on the awarded damages from the date of the upheld breach and permission to appeal. The solicitors also sought permission to appeal the Judge's decision to allow late amendment of pleadings (to include the only alleged cause of action upheld to have given rise to the damages liability).

**DECISION**Costs

The judge first had to decide who was the "successful party". This was not simply a question of identifying which party ended up making a payment to the other. Following the line of Court of Appeal decisions beginning with *Roache v Newsgroup Newspapers Limited (1998)*, the judge held that he must consider who as "a matter of substance and reality" had won? He distinguished the authority of *Fox v Foundation Piling Ltd (2011)* in which it was held that the paying party at the end of a trial could not complain if they had not protected themselves with a Part 36 offer as, in that case, it was common ground who was the successful party.

Applying *Roache*, the judge concluded that the solicitors ought to be regarded, in substance, as the successful party. However, the judge further concluded that the solicitors' refusal to admit any negligence justified a 15% reduction in the costs payable.

Interest

The solicitors opposed any award of interest on the damages, even though the claimant could be said to have been deprived of the value/use of the money, because the causative breach was not pleaded until the action had run virtually its entire course. The Judge applied his discretion to award interest for only the second half of the relevant period.

Appeals

Neither side was permitted to appeal as all the decisions being disputed were discretionary.

## COMMENT

Although not a nominal award of damages, £28,000 represented a tiny fraction (less than 1%) of the claimed sum. It must therefore be correct to regard the solicitors as the "successful party". In addition, the allegation upon which the claim succeeded was only made by way of a last-minute amendment on the final day of the trial; the case as pleaded at the commencement of the trial was entirely unsuccessful.

The case illustrates the difficulty faced in planning for all eventualities in any litigation. Although the defendants can seek to enforce their costs order, there will be significant irrecoverable costs on assessment in addition to the 15% disallowed. Victory will therefore come at a price.

The judge specifically held that the solicitors should not be criticised for having vigorously defended the whole of the claim and for not making a Part 36 offer. Despite this, the case also illustrates the importance of making an "early doors" offer. An offer of this level of damages would never have been accepted by the claimants. However, issues and decisions as to whose offers have been beaten/defeated, and the resulting costs consequences, are often easier for the parties to confront and settle - and for the courts to deal with if they can't - than the trickier issues of "Who won?". Clearly, consideration should always be given to make an early offer before costs escalate.

**SURVEYORS – VALUATION - BUY TO LET PURCHASER****SCULLION v BANK OF SCOTLAND PLC (T/A COLLEYS)****APPEAL TO SUPREME COURT****BACKGROUND**

The eagerly awaited appeal to the Supreme Court has been withdrawn. We reported on the Court of Appeal decision in June 2011. The Court of Appeal, overturning the decision at first instance, held that the valuers who had been instructed by a prospective mortgage lender to carry out a mortgage valuation did not owe a duty of care to Mr Scullion who bought the property as a buy-to-let purchaser. Mr Scullion's appeal was due to be heard by the Supreme Court this month.

In order to reach this conclusion, the Court of Appeal distinguished the case of *Smith v Bush [1990]*. In *Smith v Bush*, the House of Lords found that purchasers of modest residential properties for owner occupation could rely upon a lender's valuation, on the public policy grounds that they would not have the means to obtain their own valuation advice. In contrast, the Court of Appeal was influenced by the commercial nature of the transaction in this case. The court held that Mr Scullion was not an 'ordinary domestic householder purchasing his home' and the purchase was a purely commercial arrangement.

**COMMENT**

The withdrawal of the appeal by Mr Scullion means that the Court of Appeal decision stands as the final say on this issue. This will be widely welcomed by valuers and their insurers. A number of cases are reported to have been stayed pending the outcome of this appeal and the fear of a further flood of negligent valuation claims by buy to let purchasers has been removed. Any buy to let purchaser that wishes to bring a claim based on a valuation prepared for a prospective mortgage lender, will now have to be prepared to take the matter all the way to the Supreme Court.

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