Manchester Building Society -v- Grant Thornton UK LLP

[2018] EWHC 963 (Comm)

The Defendant accountancy firm was found not liable for losses incurred in breaking long-term swaps, which flowed from market movements for which it had not assumed responsibility.

The Manchester Building Society ("MBS") sought damages for breach of contract, negligence and/or breach of statutory duty in the sum of £48.5 million from its former auditor, Grant Thornton. Grant Thornton admitted negligence but submitted that no damages were recoverable. Teare J held that, applying the "scope of duty" principles, only £315,345 of the losses claimed were recoverable.

MBS had hedged lifetime mortgages by entering into long term swaps, many with a term of 50 years. MBS alleged that it had received negligent advice as to the treatment of such swaps under the relevant accounting standards, having been incorrectly informed by Grant Thornton in 2006 that it could apply hedge accounting, and that Grant Thornton had been negligent in its subsequent audits in failing to identify its error. The consequence of the error was that MBS' financial position was different from what had been reported and MBS lacked sufficient regulatory capital. Of the £48.5 million claimed by MBS, £32.7 million comprised losses incurred through breaking the swaps by MBS as a response to its loss of regulatory capital.

Although Grant Thornton admitted negligence, liability was denied on a number of grounds. First, Grant Thornton submitted that factual causation on the "*but for*" basis had not been made out as, had there been no negligent advice, MBS would have used alternative hedging products and so suffered the same loss. Second, Grant Thornton submitted that its negligence was not a cause in law, contending that the only "*effective causes*" of the losses were MBS's own commercial decision to issue lifetime mortgages and purchase long-term swaps and the collapse in interest rates due to the financial crisis. Third, Grant Thornton submitted that the losses claimed were outside the scope of the relevant duty such that no recovery could be made by MBS. Fourth, Grant Thornton alleged contributory negligence on the part of MBS. Finally, Grant Thornton relied upon the statutory defence set out in section 1157 of the Companies Act 2006.

Teare J rejected Grant Thornton's arguments on "*but for*" causation on the facts and on cause in law. However, having considered the decisions of the House of Lords in *South Australia Asset Management Corpn. v York Montague Ltd* [1997] AC 191 and the Supreme Court in *Hughes-Holland v BPE Solicitors* [2017] UKSC 21, Teare J held that Grant Thornton had not assumed responsibility for MBS being "*out of the money*" on the swaps in the event of a sustained fall in interest rates. All Grant Thornton had assumed responsibility for was certain "termination" or "penalty" costs, as well as a number of professional fees, totalling £420,460. This sum was then reduced by a quarter by reason of MBS's contributory negligence. Grant Thornton's reliance on the statutory defence in section 1157 was dismissed as Teare J did not consider that Grant Thornton had acted reasonably.