public knowledge. Once that fraud against Ferranti became public knowledge, the share price collapsed.

77. The buyer of the shares suffered a substantial loss on realizing his shareholding. This loss was in part caused by the broker's fraudulent misrepresentation made to the buyer and in part by the separate but unknown fraud committed against Ferranti which caused the market to place too high a value on its shares. The main question in issue was whether the buyer could recover against the fraudulent representee only for that component of loss caused by the inflation in the share price as a result of reliance on the broker's fraudulent misrepresentation or whether the buyer could recover all the loss he had suffered as a result of entering into the transaction. This latter measure of damages would include damages for the loss suffered when the market price of the shares fell substantially on discovery of the fraud committed against Ferranti.

78. The House of Lords (reversing the Court of Appeal) held that the latter measure of damages was recoverable. In a case of fraud, the buyer is able (within certain limits) to recover for all of the damage he suffers as a result of entering into the transaction in question. This included the loss caused by the collapse of the share price when the separate fraud perpetrated against Ferranti came to light.

79. One of the important issues considered in Smith New Court was the time by reference to which loss is to be measured. In many cases, perhaps most cases, loss is measured by comparing the price paid by the representee with the value of the asset he received at the time he entered into the transaction. Based on this general approach, the loss crystallizes

immediately the transaction is entered into. There is no need to consider the continuing and future effects of other circumstances and of changes in asset values.

80. But this general rule is by no means a rigid and inflexible one. In some cases, it may take time to discover the falsity of a misrepresentation. In the meantime the asset may have declined further in value since its value at the time of the transaction. Even when the misrepresentation is discovered, it may be impossible, for a variety of reasons, to dispose of the asset immediately and crystallize the loss. The asset may decline still further in value whilst the representee remains *"locked in"* to the transaction. In cases such as these, providing the representee has acted sensibly and prudently and has acted reasonably in mitigating his loss, he may often recover the difference between what he pays for the asset and the value he realizes when he is ultimately in a position to dispose of it. This is the measure of loss which was awarded in Smith New Court. It is the one which Mr. Hirst favours in the lead cases.

81. The difficulty with applying this measure of loss to the lead cases appears from the speeches in Smith New Court itself. Lord Browne-Wilkinson observed (at p.267G-H):

> "The Guerin fraud [i.e. the fraud committed against Ferranti itself] has been committed before Smith [i.e. the buyer of the shares] acquired the shares on 21 July 1989. Unknown to everybody, on that date the shares were already pregnant with disaster. Accordingly when, pursuant to the Roberts fraud [i.e. the fraudulent misrepresentation made by the broker to the buyer of the shares], Smith acquired the Ferranti shares they were induced to purchase a flawed asset. *This is not a case of the difficult kind that can arise where the depreciation in the asset acquired between the date of acquisition and the date of realisation may be due to factors affecting the market which have occurred after the date of the Defendant's fraud.*" [Emphasis added.]

82. In the present case, the decline in equity values over the last three years means that much of the loss in policy values suffered by policyholders and former policyholders is indeed attributable to *"factors affecting the market which have occurred after the date of the Defendant's fraud."* The present situation concerning the Society is what Lord Browne-Wilkinson described as a case of the *"difficult kind"*.

83. Lord Browne-Wilkinson expressed no view of his own about how such a difficulty should be resolved. But Lord Steyn was more forthright. He cited (at p.279B) a passage from the judgment of Lord Cockburn in Twycross v. Grant (1877) 2 CPD 469 at p.544. That passage reads as follows:

> "If a man buys a horse, as a racehorse, on the false representation that it has won some great race, while in reality it is a horse of very inferior speed, and he pays 10 or 20 times as much as the horse is worth, and after the buyer has got the animal home it dies of some latent disease inherent in its system at the time he bought it, he may claim the entire price he gave; the horse was by reason of the latent mischief worthless when he bought it; but if it catches some disease and dies, the buyer cannot claim the entire value of the horse, which he is no longer in a condition to restore, but only the difference between the price he gave and the real value at the time he bought."

84. The decline in policy values since a policyholder bought his policy is, of course, comparable to the horse catching a disease subsequent to the transaction in question. Lord Steyn referred to the difficult problems that can arise where investors have been misled and a false market has been created. But, he continued (at p.279A-B):

> "None of these practical considerations justify the adoption of a special rule in respect of share transactions. The same legal principle must govern sales of shares, goods, a business or land."

Having made that observation about legal principle, he then went on to quote the passage from the judgment of Lord Cockburn cited above and said he found it instructive.

85. After making those general observations, Lord Steyn then expressed his own views (at p.285F-G) as follows:

> "In these circumstances Smith was truly locked into the transaction by reason of the fraud perpetrated on it. And the causative influence of the fraud is not significantly attenuated or diluted by other causative factors acting simultaneously with or subsequent to the fraud. The position would have been different if the loss suffered by Smith arose from a subsequent fraud. That would be a case like the misrepresented horse in Cockburn C.J's example in Twycross v. Grant 2 C.P.D. 469, 544-545, where the buyer plainly cannot recover the entire value of the horse if it subsequently catches a disease and dies. In the actual circumstances of this cases I am satisfied that there was a sufficient causal link between the fraud and Smith's loss. Moreover, for substantially the same reasons, I would hold that Smith's losses, calculated on the basis of the difference between the price paid and the proceeds of subsequent realisations, flow directly from the fraud."

86. Lord Steyn plainly viewed Lord Cockburn's comment as a correct statement of the law. He also regarded the case of the horse as illustrative of the general principle. On the facts of the case in Smith New Court, this was no obstacle to recovery since the shares were already *"pregnant with disaster"* when they were purchased by the plaintiff. It was not a case in which the deterioration in asset value had taken place as a result of factors occurring *since* the transaction. But the decline in the value of the Society's policies since those policies were purchased is, by definition, a case where the decline in asset value has occurred since the transaction was entered into.

87. It should be remarked that Lords Keith, Mustill and Slynn expressed their agreement with the speech of Lord Steyn (as well as with that of Lord Browne-Wilkinson).

88. From this it follows that, as the law appears presently to stand, a policyholder who successfully mounts a case of fraud against the Society would be unable to recover damages by reference to a decline in value that occurred after the policy was purchased. It is immaterial whether the decline in value in question happens to be the same as, or more than, that experienced by other with profits funds.

89. Surprisingly, whilst Mr. Hirst referred briefly (in paragraph 43 of his Opinion) to Lord Browne-Wilkinson's reference to "cases of the difficult kind" where depreciation occurs *after* the asset has been acquired, he omitted to refer to Lord Steyn's more robust assertion (in the same case) that a buyer of a horse who was induced to contract by a fraudulent misrepresentation "plainly" cannot recover for the damage suffered by the horse when it subsequently contracts an illness and dies. We are not clear whether Mr. Hirst overlooked the critical passage in the judgment of Lord Steyn (and the agreement of Lords Keith, Slynn and Mustill with Lord Steyn) or whether he thought Lord Steyn's comments irrelevant. But we are quite clear that those comments are of high relevance and preclude the possibility of recovery for subsequent falls in asset values.

90. But there may also be another factor at work here. The risk of the price of shares declining is a well-known one. People may have been persuaded, during the long bull market of the 1990s, that that risk had receded or lay in the future. But it is a fundamental truth of stock market investment that shares may go down as well as up. The risk of a fall in share prices is an ordinary incident of owning shares or any financial product whose

value depends on the value of shares. A person who buys an ordinary equity-based product must be taken to have accepted that risk. In the case of such a well-known risk, one would ordinarily treat the investor as having assumed the risk.

91. The case of a horse contracting an illness and dying after its purchase may be thought to be an event of a relatively unexpected kind. Obviously horses contract illnesses and die, just as much as human beings do. But such a risk would, in general, be regarded as a relatively small one, unless there were some particular reason to expect it to be likely.

92. In such circumstances, it seems to us that there is a stronger case for allocating the risk of the horse dying to the misrepresentor than there is for allocating the risk of a fall in equity values to the misrepresentor. Yet even the risk of the horse dying is not be reallocated to the fraudulent representor. The case for saying that the risk of a fall in stock market values should be allocated to the Society seems to us to be even weaker. This is on the assumption that the Society is to be dealt with in the same manner that it would have been dealt with if it had acted fraudulently. Of course, the Society (we are assuming) acted negligently rather than fraudulently. We have already referred to the observation of Lord Hoffman in SAAMCO (at p.216C-D) to the effect that even in cases of fraud, "the defendant is clearly not liable for losses ... attributable to causes which negative the causal effect of the misrepresentation." Mr. Hirst also referred to this passage (in paragraph 41 of his Opinion). It seems to us plain that the combined effect of these two leading cases (SAAMCO and Smith New Court) is that, despite the law's policy of deterring fraud and the general principle of holding a person liable for all of the consequences of the transaction in a case of fraud, the defendant is still not to be held liable for changes in asset values which occur after the transaction induced by fraud was

entered into. Needless to say, there could be no possible justification in a case of negligence.

93. If an investor has no legitimate complaint with regard to risk disclosure or if he understands the risks inherent in equity-based investments and nonetheless proceeds with the investment, it is impossible to relate the loss caused by investment performance to the misrepresentation of the GAR risk. In the words of Lord Hoffman, the "defendant is clearly not liable for losses ... which negative the causal effect of the misrepresentation." The Society did not, by its misrepresentation, expose the investors to the risk of a fall in the value of equities. The investor exposed himself to that risk by his decision to invest in a with profits fund. He would have suffered the same exposure to the same risk even if the facts about GAR had been in accordance with the Society's representation.

94. Mr. Hirst does not, of course, suggest that the Society should be liable for all of the losses suffered by investors as a result of market falls. He confines liability to those falls attributable to relative under performance. But we can find no justification for this view. Both general market losses and relative under performance fall within Lord Steyn's excluded category. We can see no justification for treating them differently. Nor does Mr. Hirst identify any argument or principle which would permit such a course. Nor does he explain why the particular case of relative under performance can escape Lord Steyn's clear opinion.

95. We accept, as is obvious, that if the Society's relative under performance were culpable, there would be a liability for it. But such a form of liability would require a finding of culpability.

96. We can detect no principled argument or justification enabling us to support Mr. Hirst's opinion on this question. The causal link that must exist between liability and loss cannot be established where the basis of liability is a misrepresentation about a particular matter (the GAR risk) but the loss results from subsequent (and, it must be assumed, non-culpable) investment performance.

97. It should also be remembered that the case against the Society is in fact not one of fraud but negligence. Even if it had been one of actual fraud, in the absence of a finding of culpable investment performance, there should be no damages awarded for investment under performance, whether general or relative. But, in any event, since the case is one of negligence, it would certainly be wrong to try to extend the boundaries of liability for fraud beyond those permitted by law so that a case of negligent misrepresentation may then be allowed to ride on the coat-tails of the extension.

98. It seems to us reasonably clear that Mr. Hirst has confused two different questions. The first is the time by reference to which damages are to be assessed. The second is the question of which items of loss may properly be the subject of compensation. Mr. Hirst has implicitly reasoned that if the correct time for assessing damages is, exceptionally, later than the date the transaction was entered into, this means that all damage suffered up to that time is compensable. This is a mistake. Issues of the scope of duty and causation still have to be addressed. In particular, damage caused by later market movements is not recoverable.

99. We would also point to a degree of arbitrariness in Mr. Hirst's inclusion of damages for the Society's relative under performance. He does not analyse precisely what is meant

by the Society's under performance in comparison with other with profits funds and we have referred to some of the difficulties which calculation may throw up. But we can deduce Mr. Hirst's meaning from the methodology for assessing damages that he proposes. He has in mind making a comparison between the Society's performance and the average performance of other with profits funds. But let it be supposed that the Society's performance, although below the average, was as good as or better than some other with profits fund. Is that relevant? Why should the Society be liable for a below average performance if its performance exceeded at least some others who are not liable? Some investors might have invested with one of the other with profits funds that performed worse than the Society or only performed marginally better than the Society (if they had chosen not to invest with the Society). If the damages awarded to those investors are measured by the performance of the average with profits fund, they will receive a windfall. They will be over compensated. Conversely, those investors who would have been fortunate enough to have invested in the better performing with profits funds would be under compensated by this method.

100. An average is a statistical measure in summary form and without regard to distribution and deviation of the effect of the various data points of which it is the average. It has no significance in measuring the actual performance of any given with profits fund or the actual loss of any given investor. Still less does it capture any measure of loss which is causally related to the wrongful act complained of. Why the loss recoverable from the Society should be influenced by the fact that one or more other with profits funds, by good luck or good management, experience a stellar performance

remains obscure. We cannot accept or agree with it. Such matters bear no relation to the effects of the misrepresentation concerning the GAR risk.

101. We are not so unyielding to Mr. Hirst's efforts as to fail to recognize that he is attempting to discover a workable solution to a difficult problem involving a large number of complainants that has a practical and common sense appeal. But, with respect to him, he has made the problem more difficult than it is. If the Society had been found culpably responsible for relatively poor investment performance, it would then become necessary to engage the problems which Mr. Hirst's statistical average solution throws up. The law does not warm to statistical solutions. It frequently has to work with probabilistic solutions (i.e. solutions based on degrees of likelihood or probability); and it may be that its willingness to entertain one branch of the study of statistics has emboldened Mr. Hirst to suppose that it might embrace a different branch of that discipline. But we are not aware that it has ever done so as a primary tool of loss measurement.

102. In our opinion of 19 September 2002, we ourselves suggested a limited role for the average performance of with profits funds. But it is essential to appreciate that that was not for the purpose of calculating the amount of loss suffered by individual complainants. It was for the purpose of setting against the GAR loss the amount by which the Society's investment performance may have exceeded the average performance of with profits funds. Our thinking was that there might have been various benefits attaching to investment with the Society not shared by investing with other with profits funds. A possible example might be the avoidance of commissions and costs of financial intermediaries. An investor with some, or most, with profits funds would be subject to

such intermediaries' commissions and costs. A complaint of misrepresentation is analogous to a claim in tort rather than for breach of contract or warranty. The measure of damages is therefore directed to losses suffered rather than gains and profits foregone. In modern terminology, the interests to be protected are the reliance and restitution interests rather than the expectation interest. In those circumstances, it seemed (and still seems) to us to be appropriate to set off against the actual GAR loss itself any benefit that the investor with the Society may have gained (when compared to other with profits funds), whether in the form of a saving of commissions and charges or, indeed, in any other form. To that extent, it seemed (and still seems) to us appropriate in principle (and subject to the availability of reliable data) to take the average performance of with profits funds as a proxy or measure of such benefits and as a means of capturing them. But that is a very far cry from treating the average performance of with profits funds as a primary component in the calculation of the loss suffered by the investor.

103. The central point we would wish to make is that there is no legal basis for including in the recoverable damages any loss suffered as a result of the Society's (assumed) relative under performance in comparison with other with profits funds. But the secondary point is that the computation of loss by reference to the performance of other with profits funds entails a statistical exercise which does not reflect any actual loss suffered by any particular individual. It is in that sense artificial. The fact that the implementation of the principle proposed by Mr. Hirst entails an artificial method of assessment is a further (though secondary) reason why the adoption of that principle requires reconsideration.

104. It would be helpful to take stock at this stage. The essential propositions for which we have so far argued and as to which we have expressed our opinion are as follows:

> "(i) The clearest and most authoritative modern articulation of law relating to problems of causation and of the relation between breach of duty and recoverable loss is to be found in SAAMCO.
>
> (ii) SAAMCO embodies a general approach to such problems applicable to cases of breach of contract, tort and breach of statutory duty.
>
> (iii) SAAMCO requires that attention be paid to the scope of the duty that has been broken and to the extent of the risk of loss which the person subject to the duty undertook.
>
> (iv) A person liable for negligent misstatement should not necessarily be responsible for all of the consequences of the transaction entered into in reliance on his statement. In particular, he should not be responsible for losses which would have been suffered even if the facts had been in accordance with the representation.
>
> (v) The application of the approach in SAAMCO to the facts of the lead cases would preclude recovery for any (assumed) relative underperformance by the Society. This is because investors with the Society would still have suffered those losses even if the facts concerning the GAR risk had been as represented.
>
> (vi) The approach formulated in SAAMCO may be subject to exceptions. Cases of fraud may be one such exception.
>
> (vii) The present cases are not cases of fraud. The legal policy which underlies the approach to cases of fraud has no application to cases of negligent misrepresentation.
>
> (viii) Royscot held that the measure of damages for negligent misrepresentation (under Section 2(1) of the

Misrepresentation Act 1967) is the same as that for fraud.

(ix) But the discussion in Royscot was concerned with the difference between foreseeable and unforeseeable damage rather than the case of damage which falls outside the scope of the duty in question. The damage in that case was in fact found to be foreseeable (so that the references to the fraud measure of damages were not necessary to the decision).

(x) But even if Royscot was correctly decided and requires the full measure of damages for fraud to be applied to a case of negligent misrepresentation, Lord Steyn's speech in Smith New Court confirms that damages are not recoverable for loss resulting from falls in asset values occurring *after* the transaction in question was entered into. Loss associated with the Society's relative underperformance is loss of this character.

(xi) Losses resulting from the Society's relative underperformance are, therefore, not recoverable either under the principle of SAAMCO or if the full measure of damages in fraud were to be applied.

(xii) With respect to Mr. Hirst, his opinion to the contrary is wrong.

V. METHODOLOGY OF ASSESSMENT OF DAMAGES

105. The error in the Opinion of Mr. Hirst is of more than marginal significance. His proposed method of assessment of damages is an unusual one but is one geared to reflect his view that damages are recoverable for relative underperformance by the Society. If that latter view is unsustainable, it follows that his proposed method of assessing damages is also unsustainable. In the following paragraphs, we explain this in more detail.

106. Mr. Hirst suggests that the damages recoverable for negligent misrepresentation in the lead cases should be the difference between (a) the amount which an hypothetical

investment in the average of with-profits funds would be worth today if that investment had been made at the same time and for the same amount as the investor's actual investment with the Society; and (b) the amount which an hypothetical investment in the average of with-profits funds would be worth today if the proceeds of surrender or transfer of the investor's actual investment with the Society had immediately been invested in such an average of with-profits funds.

107. As is often the case with such formulae, a concrete example may give a clearer illustration. Let it be assumed that on 1 October 1998, a person invested £100 in the Society's with-profits fund and that on 1 January 2002 (after the Society's policy value reductions of July 2001 and any applicable market value adjuster), he surrendered his policy and received £80. Assume he then immediately re-invested the £80 proceeds into a notional with-profits fund whose investment performance was that of the average of with-profits funds and that today his investment is worth £70. This figure of £70 is then to be compared with what would have happened if the investor had initially (on 1 October 1998) invested his £100 in the notional with-profits fund representing the average of with-profits funds. Suppose that today that investment would be worth £78. On those figures, according to Mr. Hirst's proposed method of assessing damages, the damage would be £8 (£78 less £70).

108. We commented above that such a method of assessing damages is unusual. What makes it particularly unusual is that it measures loss by reference to events that have occurred not only after the transaction in question was entered into (which is permissible in appropriate cases such as where there is delay in discovering the falsity of the representation or the claimant is "locked in") but also by reference to events which have

occurred after the transaction was terminated by surrender (which we believe to be unprecedented). The fact that a particular formula or method for assessing loss is unusual, or even unprecedented, is not necessarily fatal, provided it captures correctly the components of loss for which damages ought to be awarded. This is the critical question. What are the implications of Mr. Hirst's method of assessment for that question?

109. What Mr. Hirst's method entails is that every factor which affected the Society's returns is taken into account. Any factor which produced a relatively adverse return (compared with the average with-profits fund) becomes the subject of an award of damages.

110. In the example we have given, the surrender value of the policy taken out with the Society was £80 at the time of surrender on 1 January 2002. Suppose the initial investment of £100 invested with the notional average with-profits fund over the same period (1 October 1998 to 1 January 2002) would have produced a surrender value of £83. Mr. Hirst's method requires us to take two steps. First, we are to take notice of that difference in return of £3. Secondly, we are to take notice of the continuing effects of investment of £80 and £83 respectively in the notional average with-profits fund over the period from 1 January 2002 until today (or the date by reference to which damages are to be assessed). If the average fund has done well (i.e. produced positive returns), the gap between £80 and £83 will have widened during the period. If it has done badly (i.e. produced negative returns), the gap will have narrowed during that period. This second step is the unusual feature of Mr. Hirst's method. But our principal concern is with his first step. This requires us to notice the difference in returns as between the Society and the notional average over the period of investment with the Society.

111. Such differences in returns may be due to any number of factors. One such factor is obviously likely to be the GAR cost. Another may be the relative investment performance. But there may be many others. The Society may have incurred a range of different costs and liabilities during the period which are reflected in its returns but are not paralleled by the average fund. Mr. Hirst's method does not merely bring into account differential investment performance. It brings into account the whole of the business outcome.

112. We do not know whether such other (i.e. other than investment performance) business considerations are significant. A method which "captures" them in the award of damages in any event without regard to their significance is, in our view, suspect.

113. But the most important feature of Mr. Hirst's method is likely to be its propensity to capture differential investment performance. We have already explained in some detail that we can see no justifiable legal basis for awarding damages to compensate for the Society's relative investment performance in a case of misrepresentation concerning the GAR risk and without a finding that the Society's investment performance was itself culpable. That is so whether damages are assessed on the fraud basis (and, in our opinion, they should not be) or on the more conventional SAAMCO basis. The critical point is that Mr. Hirst's proposed method of assessing damages would award damages for inferior investment performance. This cannot be supported either by reference to the fraud measure of damages (as explained in Smith New Court) or by reference to the measure of damages for negligent misstatement (as analysed in SAAMCO). If Mr. Hirst is correct in suggesting that the Society's investment performance has been inferior when compared to the average, his method of assessing damages will capture that inferiority

and will award damages in respect of it. In our view, this would be a clear mistake. If we are right in thinking that no damages for inferior investment performance should or can be awarded (absent an appropriate finding of liability for negligent investment performance), then Mr. Hirst's method of assessing damages cannot properly be applied.

114. In summary, Mr. Hirst has suggested that the (assumed) inferior investment performance of the Society is a compensable item in a claim for damages for negligent misrepresentation (concerning GAR) inducing a contract. He has then applied a method of awarding damages which incorporates the effects of that relative investment performance. (His method incidentally also incorporates the effect of any other factor bearing on relative returns, whether or not related to investment performance). But since the deterioration in asset values that occurred after the policy was taken out is excluded from the set of compensable items even in a case of fraud (by the clear observations of Lord Steyn in Smith New Court), it follows that a method of calculating damages which incorporates it is erroneous and cannot be accepted. It would subject continuing members of the Society to losses which they ought not to have to bear.

VI. MONEY MARKET ALTERNATIVES

115. A related difficulty of Mr. Hirst's Opinion arises out of paragraphs 30 and 47. It is necessary to set these paragraphs out in full.

> "The second starting point must surely be this: But for the misrepresentation none of the claimants would have entered into the contract with Equitable – that is clear from FOS's findings. What the claimants would have done with their money may be less certain. FOS may make findings on that. I expect in many cases, FOS will conclude that the claimants would probably have taken out a "with profits" pension

policy with another financial institution, but, save in some special cases, it may be quite unrealistic to reach a conclusion as to which institution would have been chosen. In other cases, FOS may conclude that the claimant would have placed the sums into a deposit style account." (paragraph 30).

"Where, however, FOS concludes that the claimant (but for the misrepresentation) would have not made a equity based investment, but kept the money in a deposit style account, in my opinion it would be wrong to have regard to market loss, to which, the claimants can fairly contend, he/she would not have been exposed." (paragraph 47)

116. Whether there are in fact cases in which the investor's next alternative preferred investment to an investment with the Society would have been a money market account we do not know. None of the lead cases is such a case. But, on the assumption that there are such cases, we have to say we disagree with Mr. Hirst's approach.

117. With respect to Mr. Hirst, the starting point which he identifies seems to be the wrong one in two respects. First, he observes that "but for the misrepresentation none of the claimants would have entered into the contract with Equitable". If the facts had been as represented, the claimants would certainly have entered into the contract with the Equitable. The point here is that there are two different ways of supposing that there was no misrepresentation. One of them is that the representation accurately reports the facts. The other is that the facts coincide with the representation. It is only in the former case that there can be any serious question of the claimants not entering into the contract. But, as Lord Hoffman pointed out in SAAMCO, if the loss would still have been suffered even if the facts were as represented, then, in general, damages for it are not recoverable. Secondly, even if the fraud measure of damages is adopted (rather than the principle of SAAMCO), it is still necessary to consider carefully the possibility that there is no

sufficient causal connection between the breach of duty in question and the loss complained of and still necessary to exclude from consideration those losses which result from changes in asset value *after* the transaction was entered into.

118. As we pointed out above, the compensatory principle precludes both recovery for loss which has not been suffered and recovery for loss, which though suffered, is not within the scope of the breach of duty. A comparison between the claimant's actual position and the position he would have been in if he had not entered into the transaction is important in determining whether any loss has been suffered; but it throws no light on the question whether any loss that has been suffered falls within the scope of the breach of duty.

119. In considering the decision of the Court of Appeal in SAAMCO, Lord Hoffmann (at pp. 217F-218A) said:

> "The other cases cited by the Court of Appeal and Counsel for the Respondent plaintiffs fall into two categories. The first comprises those cases concerned with the calculation of the loss which the plaintiff has suffered in consequence of having entered into the transaction. They do not address the question of the extent to which that loss is within the scope of the defendant's duty of care. The calculation of loss must of course involve comparing what the plaintiff has lost as a result of making the loan with what his position would have been if he had not made it. If for example the lender would have lost the same money on some other transaction, then the valuer's negligence has caused him no loss. Likewise if he has substantially overvalued the property so that the lender stands to make a loss if he has to sell the security at current values, but a rise in the property market enables him to realise enough to pay off the whole loan, the lender has suffered no loss. But the question of whether the lender has suffered a loss is not the same as the question of how one defines the kind of loss which falls within the scope of the duty of care."

120. In this passage, Lord Hoffmann is drawing attention to the distinction between the loss that the claimant has suffered on the transaction and the loss which falls within the scope of the duty which has been broken. The point he is making is that, where two phenomena affecting an outcome are in operation, it may be necessary initially to investigate whether the net effect of the operation of the two phenomena has prevented there being any loss at all. If it has prevented a loss, that is the end of the enquiry. If there is no loss, there is nothing in respect of which damages can be awarded. However, if the investigation of the comparison between what in fact happened and what would have happened if the transaction had not been entered into at all reveals that a loss was suffered, then an entirely different enquiry becomes necessary. As the latter portion of the above extract indicates, it is then necessary to consider what components of the loss fall within the scope of the duty that has been broken (or is appropriately causatively connected with the breach of duty). The fact that the first stage of the enquiry reveals that there has in fact been a loss throws no light on the second stage of determining what portion of that loss falls within the scope of the duty (or is appropriately causatively connected with the breach of duty).

121. Mr. Hirst has omitted to consider this second stage. He implies (without stating expressly) that the fact that the claimant would not have invested with the Society if he had known the truth and would instead have placed his funds in a money market account resolves the enquiry and that the difference between the returns on the two forms of investment is the measure of the recoverable damages. In our opinion, he is in error.

122. It may be that what Mr. Hirst has in mind is that the observations in SAAMCO should not be regarded as controlling because it was a case of negligence and he is applying the fraud measure of damages. But even allowing for this, he still faces the difficulty that, in fraud cases, changes in asset values that occur *after* the date of the transaction are to be disregarded; and the difference in respective returns between an investment with the Society and an investment in a money market account fall within this category. In our opinion, Mr. Hirst is in error in suggesting that money market returns might form the basis of the assessment of damages.

123. When a person invests in an equity-based investment, he accepts the risk of fluctuations in equity prices. If the GAR risk had been immaterial (as was represented), the claimants would still have suffered the effects of the fall in equity values. In fact, the GAR risk *was* material and the representation was (we assume) false. The claimants are entitled to be compensated accordingly. But they are not entitled to be compensated for the risk of a fall in equity values for that is the very risk they assumed. To compensate for that would be to penalise continuing members of the Society unjustifiably. They would shoulder the burden of the decline in equity values affecting their own investment as well as that of the claimants.

VIII. THE DATE OF ASSESSMENT OF DAMAGES

124. The problem of determining an appropriate date by which to assess the loss and damages suffered by claimants is a significant one in applying Mr. Hirst's methodology. This is because he treats the loss resulting from the Society's relative under performance as compensable. On that approach, it becomes necessary to compare the performance of

the Society with that of other providers over a period of time and to decide how long a period of time should be taken for that purpose.

125. Once it is appreciated that relative under performance is not compensable (either on the fraud or the negligence measure of damages), this problem largely disappears. The appropriate measure of damages is essentially the loss caused to policyholders as a result of their policy values being reduced by the need to fund the GAR costs. Performance over time is irrelevant.

126. There is, however, a residual problem of determining the date of assessment. If the representation made to the claimants had been true, they would obviously still have invested with the Society. Their contributions and resulting policy values would then not have been reduced in order to fund the GAR costs. But the effects of general market falls and any special under performance by the Society would then have operated on their full (unreduced by GAR) proportionate share of the fund. For example, suppose that a particular investor's proportionate share of the fund has been reduced by £10 as a result of the need to fund GAR costs. If that £10 had remained part of the investor's proportionate share, assume it would have fallen to £9 as a result of market declines. This fall in value affecting the value of the policy would have been suffered even if the representation had been true. If it is disregarded and damages are awarded simply by reference to the reduction in policy values resulting from funding the GAR costs, the claimants will be over compensated at the expense of continuing members of the Society. The correct measure of the compensable loss in this example is £9 and not £10. To make such a calculation requires a date of assessment to be determined.

127. In our opinion of 19 September 2002, we concluded that the measure of damages should the lower of

(i) The sum needed to bring the return of a former non-GAR policyholder up to the level of return he would have enjoyed with a comparable group of life houses; and

(ii) The loss of return suffered by a former non-GAR policyholder as a result of the Society's inability to satisfy the rights of GAR policyholders through the application of differential bonuses or ring fencing.

128. The former of these alternatives is directed to pointing out that if, despite the misrepresentation, policyholders have not in fact suffered loss at all (because of other beneficial features of investing with the Society), then no damages should be awarded. Or, if a lesser loss had been suffered than might have been expected based only on the GAR loss, then a lesser sum by way of damages should be awarded.

129. Putting aside those possibilities (as one would in all likelihood have to do if Mr. Hirst is right in supposing that the Society's performance compared unfavourably with that of other with profits funds), one then focuses upon the second of the above alternatives.

130. If the representation had been true, the investor would unfortunately have continued to suffer the effects of falls in equity values and reductions in policy values right up until the moment when he surrendered or transferred his policy. On this second alternative, the correct measure of damages is the loss of return caused by GAR costs. But this entails reducing the actual GAR cost by reference to any other relevant reduction in

policy values that may have occurred during the period of the investment. The reason is, quite simply, that if the representation had been true and the notional portion of the investor's investment that had to be applied to fund the GAR costs had not had to be so applied and still enured to the benefit of the investor, that notional portion of his investment would still have suffered from declining equity values and consequent policy reductions.

131. Before leaving this topic of the appropriate date of assessment, we feel we should state that we disagree with a number of features of Mr. Hirst's Opinion concerning it. In particular, we do not believe that it is generally correct to equate the date of assessment of damages with the date at which a failure to mitigate loss might be said to have occurred. The two concepts generally involve different enquiries. In addition, we do not accept that a different approach towards pension policies is necessary or appropriate (see paragraphs 52-59 of Mr. Hirst's Opinion). The basis of Mr. Hirst's differential treatment of pension policies is that the investment is "locked in," at least from the perspective of the Inland Revenue (paragraph 53). However, a pension policy may be transferred to another provider without difficulties with the Inland Revenue (barring attendance to formality).

132. However, we need not elaborate these concerns any further. The essential point is that (apart from the residual matter we have mentioned) once it is accepted that subsequent asset value movements are irrelevant both to the measure of damages in negligence and that in fraud, then the significance of the date of assessment disappears. The loss is, quite simply, the loss of return caused by the need to fund GAR costs. Differential or relative performance over time is irrelevant.

IX. MARKET VALUE ADJUSTERS

133. Mr. Hirst addressed the problem of market value adjusters (in paragraph 62-68 of his Opinion). His essential proposition was that "the sum realised on re-sale is a key component of the damages calculation in cases of misrepresentation" and a claimant who has transferred or surrendered his policy has, in effect, re-sold and has suffered the effects of market value adjusters. Mr. Hirst therefore concludes that the loss suffered by reason of the application of an MVA ought to be compensated for. His method of computing damages by reference to the relative performance of the Society and an average fund was, we imagine, intended in part to reflect his opinion.

134. In fact, the matter is more complex than this. Other with profits funds have also applied market value adjusters (as Mr. Hirst points out in paragraph 65), although the rates of adjustment they have applied and the timing at which they have applied them will differ. The application of an MVA by other providers will, of course, be reflected in the average performance of other with profits funds. So Mr. Hirst's methodology does not in fact compensate for the MVA imposed by the Society. It compensates for the difference between the MVA imposed by the Society and that imposed by the average with profits fund (unless Mr. Hirst intends that MVAs imposed by other with profits funds are to be ignored). But we need not dwell upon this somewhat recondite point. There are more fundamental difficulties with Mr. Hirst's opinion.

135. Mr. Hirst describes the reasons why MVAs are applied (in paragraph 63 of his Opinion). As he makes clear, the first reason for requiring an MVA is that, at any given moment in time, the policy values and bonus declarations provided to an investor may

overstate the actual value of his proportionate share in the fund. This is the phenomenon of "smoothing." When a policy matures at a moment of time at which the published statements of his policy value and bonuses exceeds the true value of his proportionate share of his fund, he nonetheless normally enjoys the benefit of the figures in the published statement. In a sense, his policy is allowed to mature on payment of too great an amount to him. But this is done because the returns are smoothed. His policy may be maturing at a time when the volatility of the market would work adversely against him if he received precisely the proportionate value of his share in the fund.

136. But this policy of smoothing only applies to policyholders whose policies mature. A person who surrenders or transfers his policy prior to its maturity date has no contractual right to any particular return. An MVA is intended, amongst other things, to ensure that a person surrendering or transferring in advance of maturity receives only his proportionate share of the fund.

137. It is obvious from this that the imposition of an MVA does not cause loss. It operates to adjust the value of a policy to the actual value of the policyholder's proportionate share of the fund on the occasion of early surrender or transfer. The only sense in which the policyholder suffers loss is that he gives up the reasonable expectation that, if he continued in membership, the future performance of the fund would bring it more closely into line with declared policy values and bonuses and, on maturity, he will receive the full value of his published statement of policy value and bonus declarations.

138. In short, an MVA is not a loss at all if it is referable to the need to protect continuing members from excessive payments being made to those who surrender early.

But, in any event, even if it were, it is one which has nothing whatever to do with GAR risk and cost.

139. In our opinion, Mr. Hirst was wrong to treat MVA as a component of loss. Even if it were a component of loss, he was wrong to treat it as recoverable (as long as it reflects the movement in the financial performance of the Society after the transaction was entered into, for which no damages are recoverable).

140. This last point can be further illustrated. Mr. Hirst accepts that general market value reductions ought not to be the subject of an award of damages. The imposition of an MVA reflects the fact that policy value and bonus statements are too generous in comparison with the policyholder's actual proportionate share of the fund. The reason this has come about is due to factors which include falls in equity values. They may in part consist of falls which have affected with profits funds generally and in part as a result of relative under performance by the Society. To award damages in respect of the MVA would amount to awarding damages not just for relative under performance by the

Society but market falls generally affecting all with profits funds. Mr. Hirst does not explore the implications of his belief that the MVA should be recovered but that general market falls should not, although the former reflects the latter.

X. FINAL BONUS REDUCTIONS

141. The position concerning final bonus reductions resulting from the July 2001 policy value cuts is, in our opinion, the same as in the case of the MVA. Mr. Hirst thinks that it ought to be brought into account in assessing damages if surrender reasonably occurred after the imposition of the final bonus reduction. In fact, his methodology fails to reflect

this because it is based upon a comparison with average with profits performance. As he observes (in paragraph 69) other with profits funds have made similar adjustments. Mr. Hirst's method of assessing damages awards damages only in respect of the difference between the Society's final bonus reduction and the average reduction made by other with profits funds.

142. There is also a curious feature of Mr. Hirst's approach to the assessment of damages when applied to the problem of bonus or policy value reductions. It arises from the fact that Mr. Hirst's method of assessment takes into account events that occurred not only after the policy was entered into but also after it was surrendered. (We commented on this in paragraph 108 above.) Suppose a policyholder suffered a final bonus reduction whilst a member of the Society and subsequently surrendered his policy. Suppose he then invested the proceeds with another provider and was unfortunate enough to suffer another bonus or policy value reduction. This second reduction will tend to give him a worse outcome than the average and, hence, increase his damages under Mr. Hirst's methodology. In effect the Society is held liable for the effect of another provider's action after the surrender of the Society's policy has occurred. We could not accept this to be correct.

143. The fundamental point is, however, that final bonus reductions reflect the decline in equity values that has occurred. By definition, a policyholder who acquired his policy before the final bonus reduction and who has, therefore, been affected by it has also been affected by the decline in equity value that has occurred since he took out his policy. That cannot be taken into account either under the fraud or the negligence measure of damages (for the reasons summarised in paragraph 104 above).

XI. CONCLUSIONS ON MISREPRESENTATION CASES

144. We have felt obliged to comment on many points of detail in Mr. Hirst's Opinion. But running throughout all these matters of detail there are essentially two simple ideas. The first is that a proper application of legal policy is repelled by the application of the fraud measure of damages to cases of negligence. The second is that, even if there is no escape from the necessity to apply the fraud measure of damages to a case of negligence, still the fraud measure of damages does not compensate for losses and reductions in asset values that occur after the transaction was entered into. Most of the errors of Mr. Hirst's Opinion lie in his having overlooked these two ideas.

145. The only rational basis (consistent with legal policy) on which damages can be awarded is in respect of the consequences of the representation being false. But even if the fraud measure of damages has to be applied, this still entails the conclusion that the only loss for which damages may be awarded is the loss of return associated with the need to fund GAR policies.

146. In the end, it seems to us that Mr. Hirst has largely followed his own instinct of what seems right. He concludes that general market losses suffered by all with profits funds should be excluded from compensation. But his difficulty is that he has no principle or theory to justify the exclusion. He bases the exclusion on "common sense" (see paragraph 42). No doubt all lawyers need a healthy reminder of common sense and a sensitive instinct of what seems right. But we must also have resort to legal principle. Mr. Hirst needs the Twycross point (and its adoption in Smith New Court) to justify his exclusion of general market losses. But once he has it, his view that there should be an

award of damages for the assumed relative under performance of the Society cannot withstand it. The Twycross point rules it out.

XII. BREACH OF A DUTY TO ADVISE

147. We now consider the fifth lead case in which it was found by the adjudicator that the Society acted in breach of a duty to advise. The adjudicator's reasoning was that the Society assumed a duty to advise the claimant with reasonable care about the suitability of investing in the Society's with profits fund; this duty required the GAR risk to be explained; the Society failed to explain it; and this failure was negligent.

148. For present purposes, we are not concerned with the correctness of the findings of fact or the inference that they gave rise to a duty to advise with reasonable care or the conclusion that there was a breach of that duty. We assume the correctness of these matters. On the basis of these findings, it is Mr. Hirst's opinion that the measure of damages recoverable by the claimant is essentially the same as in the cases of negligent misrepresentation. More particularly, in his opinion, damages for the relative under performance by the Society are recoverable in such a case (just as in a case of negligent misrepresentation).

149. It is, in our view, of critical importance once more to examine carefully the cause of action, the scope of the duty and the cause of any loss suffered. We do not, of course, repeat the extracts quoted above from SAAMCO. But they are of equal significance when considering the question of a breach of a duty to advise with reasonable care.

150. The decision of the adjudicator in finding a breach of a duty to advise with reasonable care records the main features of the evidence and the facts. The adjudicator noted that the claimant's case was that she had been "advised" by one of the Society's representatives to take out a personal pension policy. The representative's own evidence was that he had recommended an investment in the with profits fund because it provided an appropriate balance of risk and reward which the client had agreed was acceptable. The representative maintained that this advice was correct and that the difficulty lay with "the ELAS situation". By this, he apparently meant the GAR problem.

151. The adjudicator's finding was that the representative had discussed with the claimant her attitude to risk and given his opinion as to the most appropriate course of action. The adjudicator observed:

> "It is my view that Equitable Life assumed a duty to provide [the claimant] with full and proper advice and to disclose all the material risks and benefits of the proposed course of action. In particular, Equitable Life did not disclose to [the claimant] the matters referred to below, namely the risks to her as a non GAR policyholder of the litigation which was proceeding through the courts and about which Equitable Life had been in receipt of relevant advice. It is my view that such failure to disclose amounted to a breach of duty of care."

152. It is of the utmost importance to notice that although the Society's representative had investigated the claimant's risk tolerance and advised that the with profits fund was appropriate to her risk tolerance, *that* advice was not found to have been negligent or to have involved a breach of duty.

153. If the representative had acted negligently in assessing the claimant's risk tolerance or in recommending a product suitable to her level of risk tolerance and, in

consequence, she invested in an unsuitable and volatile product and suffered loss, that loss would have been recoverable. But there was no such finding. The breach of duty lay in the failure to disclose the GAR risk; not in a failure to give careful advice about the suitability of the type of investment in question.

154. The claimant's loss resulted from two causes: the GAR cost and the fall in equity values. The loss caused by the GAR cost was caused by the breach of duty found by the adjudicator. The loss caused by the fall in equity values was not. Even if there had been no GAR risk at all (so that the representative would have committed no breach of duty in failing to disclose it), the loss caused by the fall in equity values would still have occurred.

155. It is, in our view, clear that if the SAAMCO approach is applied, there can be no liability either for general market falls or for falls in equity values that may have affected the Society more than the average with profits fund but that are unrelated to GAR. The question must, therefore, be whether there is any reason to depart from SAAMCO and to apply a different approach.

156. Mr. Hirst's view is that the claimant is entitled to recover damages for the relative underperformance by the Society though not for general market losses. The basis of his reasoning is that the duty in question in the claimant's case was a duty to advise; the claimant would not have entered into the transaction at all if accurate advice had been given; and the Society is, therefore, liable for all the consequences of the claimant entering into the transaction (less the general market falls which would have been suffered by investing in the average with profits fund).

157. In supporting his argument, Mr. Hirst refers to Aneco Reinsurance Underwriting Ltd. v. Johnson & Higgins [2002] Lloyd's Rep IR 90. He comments that that case:

> "confirms that the ordinary rule is that where a person agrees to advise generally, he is liable for all the foreseeable consequences of his negligence, including the adverse consequences of entering into the transaction provided such consequences can fairly be held to fall within the scope of his duty."

158. With respect to Mr. Hirst, he has misunderstood Aneco. We need not enter upon a detailed analysis of it. The basis of the decision was that the defendant should have advised the claimant that the contract of insurance the claimant was contemplating entering into involved unacceptable risks; not (as Mr. Hirst states) that the claimant would not have entered into the contract of insurance if he had not been negligently advised that reinsurance cover was available. The reasoning of the House of Lords was (a) the defendant was negligent in advising that reinsurance cover was available; (b) in truth it was not and the defendant should have so advised; (c) its lack of availability implied that the risks involved in the contract of insurance the claimant was contemplating were unacceptable risks; (d) in negligently failing to advise that reinsurance was unavailable, the defendant also negligently failed to advise that the risks of the contract of insurance contemplated by the defendant were unacceptable.

159. The proposition for which the decision is authority is that the loss suffered by the claimant on the contract of insurance was recoverable because the defendant negligently failed to advise accurately about *that contract of insurance*. In other words, the scope of the duty was not merely to advise about the availability of reinsurance. It extended to advising about the quality of the risks of the contract of insurance itself; and the

defendant negligently failed to perform that latter duty by failing to advise that reinsurance was unavailable.

160. Once this feature of Aneco is appreciated, it can then be seen that it gives no support to Mr. Hirst's conclusion. In that case there was a negligent breach of a duty to advise that the risks of the contract of insurance were unacceptable. In consequence, the losses suffered when *those* risks materialised were recoverable.

161. By contrast, in the present case, there was no negligent failure to advise upon the risks of investing in an equity-based product and no negligent failure to advise upon the suitability of the product to the claimant's risk tolerance. The only finding of breach of duty was the failure to warn of the GAR risk. That is the loss for which damages are recoverable.

162. This analysis is in fact implicit in the passage we have quoted above from Mr. Hirst's Opinion about the effect of Aneco. He there correctly limits the recoverable damages to those that "can fairly be held to fall within the scope of [the defendant's] duty". The duty in question was to "advise" the claimant. The breach of duty was not to give negligent advice about the suitability of the product. It was to fail to disclose the GAR loss. The damages that were suffered as a result of falls in equity values lay outside the scope of *that* duty. It is true that, on the findings of the adjudicator, there was also a duty to advise generally. That would include a duty to advise about the suitability of the product. But the critical point is that *there was no breach of that duty.*

163. If two duties are owed and one is satisfactorily performed and the other is negligently broken, the defendant is liable for the loss resulting from the breach of duty.

But it would be absurd to say that, because the defendant is liable for that loss, he is also liable for loss associated with the subject matter of the first duty even though he performed that duty. Yet that is what Mr. Hirst's Opinion holds. In our opinion, he is wrong. Aneco gives no support for his conclusion.

164. Mr. Hirst's reference to limiting damages by reference to the scope of the duty can, we believe, only be a reference to the duty that has been broken. A duty that has been *performed* is incidental. It can have no relevance to the assessment of damages. Where loss is suffered as a result of some cause which was the subject of a duty that has been performed satisfactorily, to hold the defendant liable for that loss is no different from holding him liable for loss which was not the subject of any duty at all. A defendant who performs his duty cannot be in a worse position than one who owes no duty at all. Yet that is the result of Mr. Hirst's conclusion .He accepts that no damages are recoverable for loss falling outside the scope of the duty. But he holds the defendant liable for loss even though the defendant has performed satisfactorily his duty relating to the cause of that loss.

165. There are real difficulties in the distinction between a duty to give advice and a duty to give information. Lord Millett drew attention to this in Aneco (though in a dissenting judgment). We believe that there is danger in generalisation or oversimplification.

166. The safest approach is, we think, to consider carefully the scope of the duty that has been broken and the consequences of *that* breach of duty. Aneco does not give support to any different approach.

167. In our opinion, a finding that there was a negligent failure to inform the claimant of the GAR risk (or, in the language of the adjudicator, a breach of a duty to advise) does not lead to the conclusion that the Society is liable for its (assumed) relative underperformance. Liability is confined to the loss caused by the breach of duty in question (or the loss falling within the scope of the duty that has been broken). This excludes loss flowing from relative underperformance.

XIII. REVISITING MISREPRESENTATION

168. In paragraph 87 of his Advice, Mr. Hirst revisited the lead cases concerning misrepresentation in the light of the conclusions he had arrived at in the lead case concerning a duty to advise. He observed that, even if the fraud measure of damages is put to one side, this would not affect his opinion. He reasoned that it was realistic to assume that the Society owed a duty to advise even in those cases where the only finding is misrepresentation; and based on such a duty the damages recoverable would be the same as in the fifth lead case i.e. they would include damages for the Society's relative underperformance.

169. We have to take issue with Mr. Hirst in the strongest possible terms.

170. The premise for his opinion is that it can realistically be assumed that the Society acted in breach of a duty to advise even though the only finding made by the adjudicator was that there had been a misrepresentation of the GAR risk.

171. In the fifth lead case (the one concerned with the duty to advise), the adjudicator observed:

> "It is a question of fact to be decided in each case whether the Equitable Life representative assumed a duty to provide information or a duty to advise generally."

172. The starkness of the contrast this passage supposes between a duty to provide information and a duty to advise generally may be too strong. Again, the question whether a duty to advise was assumed may also involve issues of law and legal policy. But the essential thrust of the adjudicator's observation is, with respect, correct. At the very lowest, the question whether a duty to advise was assumed certainly *includes* findings of fact.

173. This at once rules out Mr. Hirst's assumption that a duty to advise also existed in the 4 misrepresentation lead cases. No finding that such a duty exists was made in those 4 cases. It is impossible to assume the existence of facts when no finding that they exist has been made.

174. We appreciate that, in this part of his Opinion, Mr. Hirst was doing no more than considering the possible existence of an alternative analysis that did not entail the unpalatable aequiperation of negligence and fraud. But the alternative analysis fails because its premise is false. Mr. Hirst must, therefore, accept the necessity of basing himself upon that aequiperation. Even then, of course, damages for post-transaction falls in value are not recoverable (thus ruling out damages for the Society's relative underperformance).

175. Finally, even if Mr. Hirst's unwarranted assumption were to be made, the consequence is not as he supposes. Since a negligent breach of a duty to advise about GAR leads to liability for GAR loss and not for relative underperformance, it follows that,

if the same analysis as applies to the case of a breach of duty to advise were to be applied to the misrepresentation cases, in those latter cases too the liability could not extend beyond the GAR loss.

CHRISTOPHER CARR Q.C.

GABRIEL MOSS Q.C.

30th September 2003