Duties to third party investors in tax avoidance schemes following *McClean*

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The Court of Appeal's recent decision in *David McLean and others v Andrew Thornhill KC* considered the circumstances in which duties are owed to non-clients in the context of legal advice made available to investors in tax schemes.

The Court of Appeal dismissed the investors' appeal against the decision of Mr Justice Zacaroli[1]. It applied the test set out by the Supreme Court in *Steel v NRAM Ltd*[2] and held that no duty was owed. This was because it would have been unreasonable for the investors to rely on the advice without obtaining independent advice and Mr Thornhill could not reasonably have foreseen that they would have relied on his advice in this way.

Background to Appeal

The claimants invested in tax avoidance schemes that were marketed on the basis that their efficacy had been endorsed by an eminent tax silk. The promoters and sponsors were Scotts Atlantic Management Limited ('Scotts'). They instructed the barrister to advise on whether the intended tax strategy of the schemes was effective. He gave robust and unequivocal advice that it was. He expressly consented to copies of his opinions being made available to prospective investors on request and did not include any disclaimer of liability.

His endorsement of the schemes was also referred to in the relevant Information Memorandums describing the schemes to prospective investors. He consented to that and approved the contents of them.

Nick Bird
Partner
+44 20 3060 6548
nick.bird@rpc.co.uk

Laura Stocks
Partner
+44 20 3060 6389
laura.stocks@rpc.co.uk

Natalia Jeremiah
Of Counsel
+44 20 3060 7432
natalia.jeremiah@rpc.co.uk

Notes

1. [2022] EWHC 457 (Ch)
2. [2018] UKSC 13 – where solicitors acting for a borrower in the context of a property sale were held not to owe any duty, in respect of incorrect statements made as to the discharge of charges secured on the property, to a commercial lender on the other side of the transaction.

The Information Memorandums included various warnings about the risks (including tax risks) of the schemes. Investors were also required to give warranties (amongst other things) to the effect that they were experienced investors, had taken *"appropriate professional advice"* and had relied solely on the advice of their own professional advisers *"with regard to the tax, legal, currency and other economic considerations"* relating to the schemes.

The intended tax benefits of the schemes unravelled when they were investigated by HMRC. It contended that the intended tax benefits failed because LLPs into which the investments were made were not carrying on a trade or business on a commercial basis with a view to profit. A closure notice was served in relation to one of the schemes in September 2016 and the investors entered into settlement agreements with HMRC in relation to all of the schemes in 2017.

The investors subsequently brought over one hundred claims against Mr Thornhill. Ten of these were selected to be tried first as sample claims. The remainder were stayed pending judgment on the binding common issues. Zacaroli J dismissed those claims in 2021 in a judgment that the Court of Appeal later referred to as *"conspicuously clear and careful"*. He held that no duty was owed by Mr Thornhill to the investors and that, even if a duty had been owed, the advice given by him had not been negligent (whether on the efficacy of the schemes or the absence of warnings of the risks). He further held that it had not been established that the investors relied on his advice.

The Appeal

The investors challenged each of these findings on appeal relying in particular on the House of Lords decision in *Hedley Byrne v Heller*[3]. They said that Mr Thornhill

- was an eminent tax silk possessing a special skill;
- had voluntarily and for a fee consented to his name and his opinions being used, without any disclaimer, to promote the investment schemes;
- was providing unusual services in that marketing function rather than acting simply as a barrister advising on the promoter's side of the transaction; and
- made unequivocal and incorrect statements about the schemes' efficacy, recognising that this this efficacy was of critical importance to the investors.

They said that the statements in the Information Memorandums telling investors to obtain their own advice and/or the warranties given by investors that they had done so were not a material consideration because they were directed at the investors' own tax position rather than the efficacy of the schemes themselves.

They further contended that the case was distinguishable from *NRAM* because Mr Thornhill had performed an unusual role as a participant in the marketing process such that this was a prospectus case. Accordingly, so they said, Zacaroli J had been wrong to focus so heavily on the question of whether an adviser on one side of a commercial transaction owed a duty of care to a party on the other side of that transaction.

The Court of Appeal rejected those arguments. Simler LJ gave the judgment of the court and applied the following reasoning.

- He rejected the argument that Mr Thornhill had acted in an unusual capacity. He said that he had remained the adviser to Scotts throughout and that *"even if it is fair to regard him …as having become part of the sales team, he did nothing that could be regarded as stepping outside his role as a barrister advising on the scheme and the terms of the Information Memorandums. …He did not at any stage become a neutral or independent expert. Nor is there anything to suggest that he took on a role acting for all parties or as acting also for the investors."*
- He agreed with Zacaroli J that Scotts and the investors were commercial counterparties and the principle of caveat emptor applied so that the investors should have conducted their own assessment of the risks of entering into the transaction. He held that *"The starting point… was that it was presumptively inappropriate for investors to rely on anything said by Scotts' adviser, and not the reverse."*
- He placed considerable emphasis on the approach of the Supreme Court in *NRAM*, asking both (a) whether it was reasonable for the investors to rely on Mr Thornhill's representations and (b) whether Mr Thornhill ought reasonably to have foreseen this reliance. He held that the answer to both was 'no'.

Notes

3. [1964] AC 465 (HL)

- He acknowledged that the absence of any disclaimer was a *"fair point to make"* but said that it was *"a multifactorial analysis and the absence of an express disclaimer was but one factor in the mix. It was neither a trump factor nor fatal."*
- He ascribed greater significance to the facts that:
  - the investors were only able to invest in the schemes through authorised professionals and therefore had to have the benefit of their own independent financial advisers;
  - the investors could only subscribe to the schemes if they warranted that they had consulted with their professional advisers in relation to tax and other considerations; and
  - the Information Memorandums included warnings in relation to the risks of the schemes.
- The Court of Appeal also referred to the investors as high net worth individuals who (Zacaroli J had found) were largely sophisticated investors. As such, they would reasonably have been expected to understand the risk warnings in the Information Memorandums and be in the habit of obtaining specialist accountancy and/or taxation advice on a regular basis. Accordingly, they would have had easy and convenient access to independent advice on the contents of the Information Memorandums and the risks of the transaction. The court rejected the investors' argument that references in the Information Memorandums to obtaining their own tax advice did not refer to advice on the overall efficacy of the schemes.

The Court of Appeal also commented on breach of duty and causation.

It held that the tax advice given by Mr Thornhill on the efficacy of the schemes had been reasonable. However, the advice would have fallen short of the requisite standard in failing to acknowledge both that there was a risk of challenge by HMRC and that there was no binding authority covering the precise nature of these tax schemes.

It held, on causation, that the investors had failed to discharge their burden of showing that they would not have invested in the absence of Mr Thornhill's advice.

Comment

The decision will be welcome to professionals who permit their advice on the efficacy of tax schemes accessible to investors in the context of the promotion of such schemes. However, it is currently subject to an application for permission to appeal to the Supreme Court.

The key issue for the Court of Appeal was the extent to which is was reasonable for the investors *"act without making any independent check or inquiry"*. This was held to be an important factor in determining the reasonableness of their reliance. On the facts of this case it was particularly important given the warranty that each of the claimants gave about their obtaining of or relying on their own advice.

Irrespective of whether the appeal succeeds or fails, the decision is unlikely to alter a cautious approach by professional advisors. In particular, it will not result in the removal of disclaimers. The decision turned on the application of the legal principles to a very specific set of facts and professionals will inevitably continue to avail themselves of all the protections that they can.

Those giving opinions will also note the strength of the warranties to the independent inquiry check issue and think carefully about what precise warranty will maximise that particular argument. There was significant argument about the precise relevance of the independent inquiry criterion and the application of the precise terms of the warranty to it.