Caytons
Changing Perceptions

Conveyancing Solicitors in Buyer-Funded Developments: an SRA Prosecution Falls Flat

INTRODUCTION

Those involved in defending buyer-funded development claims will be wearily familiar with the Agreed Outcomes between the SRA and David Hayhurst and David Sewell, arising principally from the stalled North Point Global projects. These are routinely presented by claimant firms as indicative of the approach a court would take to a solicitor's duties.

They were never anything of the sort but, in any event, can now be ignored. In the case of Amie Tsang who also acted for a number of buyers in North Point projects (and for whose practice we acted in related civil actions) substantially similar allegations crumbled on exposure to contested proceedings. The SRA was reduced to trying to persuade the Tribunal that the proceedings had not been a shambles from start to finish. Not only did Ms Tsang comprehensively defeat the allegations, but she also secured a rare adverse costs order against the SRA on the basis that the prosecution was wholly unmeritorious.

The judgment introduces a welcome measure of level-headedness to this topic and is of wider interest in demonstrating the tribunal's willingness to take a robust stance on misconceived prosecutions.

We have, therefore, prepared the following note.

BACKGROUND

A: Fractional sales

After the Credit Crunch, property developers adopted a funding model known as 'fractional sales'. The essence of this was that investors bought units off-plan and advanced a significant proportion of the purchase price on exchange on terms that the developer could use the monies to fund the project. In consideration for this, they were offered a discounted sale price as against the market value of the finished unit and other incentives such as a guaranteed rental income for a period after completion.

This funding model has been used with success on a significant number of projects and there is evidence that it largely became the norm at one stage in parts of the Northwest. However, confidence in the model was shaken by three high profile corporate failures from mid-2016.

B: The failed developers

Absolute Living Developments was wound up in April 2016. It was revealed soon afterwards that buyers' monies had been diverted to connected companies instead of being spent on the projects. There were protests in Hong Kong, where the projects has been marketed. Hong Kong investors thereafter took a jaundiced view of off-plan developments in the UK.

A knock-on effect of this was that sales quickly petered out of units in North Point Global's projects, which were being marketed through the same Hong Kong selling agent and had until then sold well. The developer continued to build out its projects until the end of that year but eventually ran out of money. Buyers found themselves out of pocket. The experience with ALD led some to infer that they had again been defrauded.

Pinnacle ran into difficulties around the same time. It had a track record of about eight successful student accommodation developments but its Angelgate project ground to a halt when the contractor walked off site and it was found that construction costs had been catastrophically underestimated. In circumstances where about £28m had been invested and there was little to show for it but a hole in the ground, there were again murmurings of a suspected fraud. These increased in volume when it emerged that the developer's controlling mind had previously served a prison sentence for fraud.

There were features in the *Times, Guardian* and *Daily Mail*, as well as an episode of *Panorama* and any number of online conspiracies, which made it all appear very murky. Nevertheless, a number of factors had to be explained away to maintain the theory that fraud was involved, and there were less sinister alternative explanations. Ultimately, the Serious Fraud Office conducted a lengthy investigation into the North Point projects and Angelgate but closed its file for want of evidence.

C: Regulatory response

The SRA initially appeared to conclude that projects funded on the fractional sales model were inherently dubious. It produced a warning notice in June 2017 ('the Warning Notice') which lumped them together with land-banking and self-storage schemes. The Warning Notice is now in its third iteration, each toned down from the previous version, but remains in force at time of writing. The regulator also began investigations into numerous solicitors who had acted in failed projects. It would appear that it elected to take no action in most cases, but there were a handful of prosecutions.

D: Previous prosecutions and Agreed Outcomes

Timothy Ackrel, who was a director of certain SPVs set up by ALD and its in-house solicitor, was unsurprisingly struck off. His case was something of a one off, however.

The SRA prosecuted David Roberts, who acted as seller's solicitor on Angelgate and initially on some of the North Point projects, on various grounds. The Tribunal rejected the contention that the projects "*bore the hallmarks of dubious transactions*" and dismissed allegations of dishonesty. The prosecution succeeded on the lesser grounds of acting with a conflict of interest and in breach of undertaking. Mr Roberts was fined £10,000.

Alan Ma and Daniel Cheung of Maxwell Alves acted for a number of investors in Angelgate and ALD projects. They elected to admit that their advice was inadequate, apparently in an attempt to agree an outcome with the SRA. Given that, after *Baxendale-Walker v Law Society* [2007] EWCA Civ 233, the regulator will ordinarily not be liable for adverse costs, there is a strong commercial incentive for a solicitor whose integrity is not impugned to adopt such a course.

There were, however, complications in that case as monies had been released improperly (although, as was accepted by the date of the hearing, inadvertently) and former clients had been issued with a document called a *"frustration notice"* which was described as threatening and intimidating. The case proceeded to tribunal. The respondents were each fined £22,000 and had conditions placed on their practising certificates.

Oliver & Co was one of the preferred firms for buyers in Angelgate and some of the North Point projects. The partner in charge was not prosecuted but David Sewell, the senior (and by then retired) solicitor with day-to-day conduct elected to agree an outcome and pay a fine of £8,000. David

Hayhurst of 174 Law acted for buyers in some of the North Point projects and one of the ALD projects. He (also by then retired) agreed an outcome in similar terms to Mr Sewell's with a fine of £10,000.

E: The Outcomes

Both Agreed Outcomes ('the Outcomes') recited that the SRA did not (any longer) consider development projects funded on the fractional sales model to be inherently dubious, although it considered them inherently risky. Mr Hayhurst's Agreed Outcome also acknowledged that, although the ALD project in which he acted may have been a fraud, there was no evidence that he could have been aware of this.

The analysis in the Outcomes is otherwise problematic. They contain what is said to be a summary of the common law principles relating to solicitors' duties, but it is one-sided and incomplete. We established that it had been put together by copy-typing (without attribution) certain selected sentences from *Jackson & Powell on Professional Liability*.

It was acknowledged in the Outcomes that the transactions under consideration predated the Warning Notice but suggested that this document merely reflected the existing common law. If this were the case, it might well be asked why it was thought necessary to issue it at all. But, be that as it may, the Warning Notice departs from the common law in material respects, at least if it is to be applied with the rigour of an Act of Parliament, as it is often suggested it should be.

It is now forty-five years since Oliver J made the well-known observation in *Midland Bank Trust Co Ltd v Hett Stubbs & Kemp (a firm)* [1979] Ch 384 that there is no such thing as a general retainer and that the extent of a solicitor's duties depends on the terms and limits of the retainer. This has been repeatedly endorsed by the Court of Appeal, most recently in *Spire Property v Withers* [2022] EWCA Civ 1193.

On a strict reading, by contrast, the Warning Notice suggests that it is improper for a solicitor to limit its retainer. There is potentially a looser but uncontroversial reading to the effect that a solicitor cannot avoid warning a client of its suspicions about a dubious transaction by placing limits on its retainer. In Sewell and Hayhurst, however, a strict reading was adopted. It was suggested that attempts by the solicitors to limit their retainers were of no effect or, alternatively, represented regulatory issues in themselves. No weight was, therefore, placed on disclaimers to the effect that the solicitors could not give financial advice or advice on the wisdom of the transactions. This notwithstanding that they merely reflected the established position at common law. The Privy Council made clear in *Clarke Boyce v Mouat* [1994] 1 AC 428 that:

> *When a client in full command of his faculties and apparently aware of what he is doing seeks the assistance of a solicitor in the carrying out of a particular transaction, that solicitor is under no duty whether before or after accepting instructions to go beyond those instructions by proffering unsought advice on the wisdom of the transaction. To hold otherwise could impose intolerable burdens on solicitors.*

It is also well-established at common law that a solicitor acting in a transactional matter should give advice reasonably incidental to the transaction, and that what is reasonably incidental will depend on all the circumstances, including the characteristics of each client. More extensive advice may need to be given to a vulnerable client than to a more sophisticated one. Again if it is to be read strictly, the Warning Notice appears to say that the same warnings must be given to every client, regardless of their knowledge, understanding and sophistication.

Although the principle that the advice required will depend on the characteristics of the individual client was mentioned in the Outcomes, it was ignored in the analysis. This proceeded on the apparent assumption that all 379 of Mr Sewell's clients and all 118 of Mr Hayhurst's were naïfs who did not know what they were getting into and needed rescuing from themselves. It is hard to see how such an assumption can safely be made.

This was particularly so in the case of Mr Sewell, whose report on title clearly stated that the monies paid on exchange would be released to the developer and explained in some detail what the money would be spent on. He also warned that there was a risk that the developer might not finish the development and deliver the unit. It was not explored with any degree of precision how and why this advice was said to fall short of what was required.

It was suggested in the Outcomes that the solicitors should have advised their clients that the projects did not have various safeguards which it was alleged a commercial lender would ordinarily insist on, that the investments were worthless unless the projects were carried to completion and that it would be difficult to recover monies if they stalled.

In the appropriate case, a solicitor will be under a duty to warn of something which is obvious to them, as a solicitor, but unlikely to occur to the lay client. This principle has been invoked in cases involving leases with onerous and unusual clauses. By contrast, in *Pickersgill v Riley* [2004] PNLR 606, the court concluded that the fact that the counterparty might turn out to lack substance did not arise out of any legal complexity and was not a hidden pitfall which a solicitor was required to warn the client about. This case was cited in the Outcomes but no attempt was made to distinguish it. The risks inherent in buyer-funded developments were repeatedly described as obvious but no case was made out as to why they might be thought to be uniquely obvious to a lawyer. It is hard to see how this could credibly be maintained.

The suggestion that these conveyancing solicitors should have given buyers of units detailed advice about what safeguards a commercial lender would ordinarily insist on when lending money to a developer was an odd one. None of the various legal teams acting for claimants in related civil proceedings echoed this argument, despite one of them conjuring up over ten pages of alleged breaches of duty by Mr Sewell's firm. As Leading Counsel for Ms Tsang submitted, it would have been laughed out of court.

Moreover, it is again contrary to principle, to determine in the abstract what advice ought to have been given to a combined cohort of almost 500 different individuals without enquiry into the knowledge, understanding and experience of any of them.

From a professional liability standpoint, therefore, the most that could be said was that there might be a *prima facie* case of professional negligence against Mr Sewell and Mr Hayhurst. Professional negligence will give rise to a civil claim in damages, assuming that the claimants could establish the other elements of their case; but it will not ordinarily amount to professional misconduct attracting a regulatory sanction. The conduct in question would need to cross the line into what is often described as manifest incompetence.

In *Re a Solicitor* [1972] 2 All ER 811, Lord Denning MR said that *"negligence in a solicitor may amount to professional misconduct if it is inexcusable and is such as to be regarded as deplorable by his fellows in the profession"*. It is not easy to see how anything Mr Hayhurst or Mr Sewell did or did not do could properly be regarded as deplorable.

In the case of Mr Hayhurst, it was suggested, but not explained why, that the advice which he gave was so inadequate as to be incompetent. That does not seem a fair characterisation. Moreover, it is difficult to reconcile with the modest fine of £10,000 it was agreed he should pay. In *Iqbal v SRA* [2012] EWHC 3251, (Admin), Sir John Thomas (P) (with whom Silber J agreed) made clear that:

> *If in a course of conduct a person manifests incompetence as, in my judgment, the Appellant did, then he is not fit to be a solicitor. The only appropriate remedy is to remove him from the roll.*

It was not even suggested that Mr Sewell had been manifestly incompetent. Why his conduct was thought to attract a regulatory sanction, therefore, remains something of a mystery.

It is relevant to note that both individuals subsequently gave evidence at length in related civil proceedings in *Various NPPM Purchasers v 174 Law v Key Manchester* [2022] EWHC 4. HHJ Judge Hodge KC (sitting as a High Court Judge), who was aware of the Outcomes, found that *"Mr Sewell was a competent and honest solicitor*" and Mr Hayhurst *"a competent solicitor who was doing his best to assist the court".*

F: The prosecution of Ms Tsang

Amie Tsang & Co (subsequently Key Manchester Limited) was based in Manchester's Chinatown. It acted for Chinese clients in the Northwest of England and in Hong Kong. Ms Tsang was one of its principals. The practice was a preferred firm for buyers in the North Point projects. It also acted for a single Angelgate buyer and a handful of buyers in an ALD project. Its terms of business recited that it did not comment on the financial viability of transactions. Its reports warned, among other things, that there was a risk that the seller might not finish the project and that the value of the rental guarantee depended on the solvency of the developer. It went on to say that the practice could not comment on the viability of the business plan or the developer's ability to deliver the project.

Ms Tsang also gave evidence in the *174 Law* proceedings and was found by the Judge to be *"a competent, thoughtful, open, careful and honest solicitor".*

After a sporadic investigation over six years, the SRA brought a prosecution. On paper, its case closely mirrored the case against Mr Sewell (it again did not appear to be argued that this was a case of manifest incompetence). But it deviated from this in oral submissions. Its case was difficult to follow but the thrust was that it did not say that Ms Tsang was in breach of any individual retainer but of a professional duty which was said to transcend the retainers, arising from the fact that she acted for a large number of clients across the projects who collectively paid about £27m into the client account.

In analysing the SRA's arguments at the hearing, the Tribunal sought clarification on its case as to the safeguards ordinarily required by a lender, but Counsel was forced to concede that he could do little more than read out from a guidance note printed off from Thomson Reuters Practical Law some seven or eight years after Ms Tsang had contracted with her clients.

THE JUDGMENT

The Tribunal was satisfied that the SRA's approach was flawed. It began by making the elementary but important point that the burden of proof lay entirely with the SRA. It likened the case it advanced to one of *res ipsa loquitur* (the thing speaks for itself) in the clinical negligence field, where negligence can be said to be obvious from the nature of the injury. It considered that such an approach was misconceived in this context.

It accepted submissions made on behalf of Ms Tsang that the proper starting point is to determine the scope of the retainer. It directed itself to Carr LJ's judgment in *Spire Property* and, in particular, to the guidance based on existing caselaw on the requirement to give advice reasonably incidental to the retainer.

The SRA was criticised for not calling evidence from any clients and falling back on stereotypes about foreigners. It noted that, even if there were assumed to be some kind of language barrier, this was removed because Ms Tsang met with the clients and was able to take them through the documents in Cantonese. Absent evidence to the contrary, the Tribunal was unable to conclude that Ms Tsang's clients were "*anything other than commercially minded investors, who wanted high returns on their investments and were prepared to take upon themselves the risks in achieving that objective and who did not want to pay a large amount in legal fees to obtain any more advice than they had received".*

The Tribunal gave effect to the limitations contained in the client care letter, terms of business and report and placed weight on the warnings which were given in the report. It considered it important that Ms Tsang had left communication with clients open by inviting them to email her if they had any further queries.

Of the Warning Notice, it said:

> *Whilst the Tribunal accepted that the Warning Notice was an important source of guidance for the profession and not something to be ignored, there was no evidence which proved to the requisite standard that Ms Tsang had not followed the Warning Notice's admonition that "[you should] ensure that clients fully understand the risks they are taking …". Clearly it could not be complied with retrospectively after it had been amended subsequent to the relevant events.*

In conclusion, the Tribunal considered that Ms Tsang had gone as far as she was reasonably able under the terms of her retainer to outline the wider risks. She had not, it found, been required as a matter of law to explain the commercial risks faced by her clients if the developments failed and had not been required to conduct investigative tasks beyond the scope of her retainer. Indeed, she had gone beyond what was strictly required of her.

On costs, the Tribunal directed itself that the starting point, based on *Baxendale-Walker,* was that:

> *Unless a complaint was improperly brought or, for example, had proceeded as a "shambles from start to finish"… an order for costs should not ordinarily be made against* (the SRA) *on the basis that costs followed the event"*

It recorded that Counsel for the SRA had accepted when questioned by the Tribunal that a *"shambles from start to finish*" was just one example of where a Tribunal might depart from the ordinary position. It left open whether this prosecution could properly be characterised as a shambles from start to finish but concluded that it was questionable whether it had properly been brought. It was satisfied that the SRA had no basis in law for its allegations. The considerable delay by the SRA in taking the prosecution forward, and the stress caused to Ms Tsang, was, it concluded, an aggravating factor.

She was awarded her costs in full, save that Counsel's refresher fees were reduced to reflect the fact that the hearing had been concluded in two days rather than three.

DISCUSSION

This is a welcome decision. Unlike the Outcomes, it adopts an approach which can be readily reconciled with the established position at common law. It would be most odd, and entirely unsatisfactory, if the threshold for establishing a regulatory breach deserving of a sanction were lower than that for establishing professional negligence in the courts. It should surely only be in the most egregious, or at least exceptional, cases that conduct which might amount to professional negligence requires a regulatory response.

It is surely right that in the regulatory as in the professional liability field, the proper starting point in a failure to advise case is to determine what the solicitor agreed to do, rather than work backwards from what went wrong. As Laddie J memorably put it in *Credit Lyonnais v Russell Jones and Walker* (2022) EWHC 1310 (Ch), *"a solicitor is not a general insurer against his client's legal problems".*

It remains to be seen whether this decision prompts further refinement of the Warning Notice. The judgment confirmed that it should not be applied retrospectively but it left for a future Tribunal to determine how it might apply where the transactions under consideration happened after June 2017. It did, however, hint that a purposive approach might be called for and that the question would be whether in all the circumstances the solicitor took adequate steps to see that the client understood the risks they were taking.

The Tribunal was alive to the commercial realities underlying the transaction and that the clients had agency. This is too often glossed over, if not ignored altogether. It cannot be assumed without evidence that the clients are vulnerable individuals who did not know what they were getting themselves into; still less that they would have walked away if given the sort of warnings a solicitor

might reasonably be expected to give. Indeed, in our experience, investors in projects of this sort are very often highly educated professionals with surplus capital who are more than capable of making their own decisions.

The decision is a reminder that *Baxendale-Walker* allowed more flexibility than is sometimes appreciated. In the Divisional Court, Moses LJ said (emphasis added):

> ***Absent dishonesty or a lack of good faith***, *a costs order should not be made against such a regulator* ***unless there is good reason to do so.*** *That reason must be more than that the other party has succeeded. In considering an award of costs against a public regulator the court must consider on the one hand the financial prejudice to the particular complainant, weighed against the need to encourage public bodies to exercise their public function of* ***making reasonable and sound decisions*** *without fear of exposure to undue financial prejudice, if the decision is successfully challenged.*

In the Court of Appeal, Sir Igor Judge P said (emphasis added):

> ***Unless*** *the complaint is* ***improperly brought****, or,* ***for example****, proceeds…as a "****shambles from start to finish****", when the Law Society is discharging its responsibilities as a regulator of the profession, an order for costs should not* ***ordinarily*** *be made against it* ***on the basis that costs follow the event. The "event" is simply one factor for consideration****.*

It is an interesting example of a case where a Tribunal might depart from the ordinary rule.

Further Information

Given the generality of the note it should not be treated as specific advice in relation to a matter as other considerations may apply.

Therefore, no liability is accepted for reliance on this note. If specific advice is required, please contact one of the Partners at Caytons who will be happy to help.

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