a
JEB Fasteners Ltd v Marks, Bloom & Co (a firm)

QUEEN'S BENCH DIVISION
WOOLF J
20th, 21st, 22nd, 23rd, 24th, 27th, 28th, 29th OCTOBER, 19th DECEMBER 1980

b

Negligence – Information or advice – Knowledge third party might rely on information – Auditor – Preparation of company's accounts – Duty to prospective investor – Auditor negligent in preparing accounts – Auditor aware when preparing accounts that company requiring outside financial support – Accounts made available to plaintiffs – Plaintiffs taking over company – Whether auditor owing duty of care to plaintiffs in preparation of accounts.

c
In April 1975 the defendants, a firm of accountants, prepared an audited set of accounts for a manufacturing company for the year ended 31st October 1974. The company's stock, which had been purchased for some £11,000, was shown as being worth £23,080, that figure being based on the company's own valuation of the net realisable value of the stock. The defendants nevertheless described the stock in the accounts as being 'valued
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at lower of cost and net realisable value'. On the basis of the inflated stock figure the accounts showed a net profit of £11·25, whereas if the stock had been included at cost with a discount for possible errors the accounts would have shown a loss of over £13,000. The defendants were aware when they prepared the accounts that the company faced liquidity problems and was seeking outside financial support from, inter alios, the plaintiffs, who manufactured similar products and were anxious to expand their
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business. The accounts prepared by the defendants were made available to the plaintiffs, who, although they had reservations about the stock valuation, decided to take over the company in June 1975 for a nominal amount, because they would thereby obtain the services of the company's two directors who had considerable experience in the type of manufacturing carried on by the plaintiffs. In discussions between the plaintiffs and the defendants during the take-over the defendants failed to inform the plaintiffs that the
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stock had been put in the accounts at an inflated value. The plaintiffs' take-over of the company proved to be less successful than they had anticipated and they brought an action for damages against the defendants alleging that the defendants had been negligent in preparing the company's accounts, that they had relied on the accounts when purchasing the company, and that they would not have purchased the company had they been aware of its true financial position. The plaintiffs contended that an auditor when
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preparing a set of accounts owed a duty of care to all persons whom he ought reasonably to have foreseen would rely on the accounts. The defendants contended that if a duty of care existed it was only owed to persons who made a specific request for information.

Held – (1) Whether the defendants owed a duty of care to the plaintiffs in regard to their preparation of the accounts of the company depended on whether they knew or ought reasonably to have foreseen at the time the accounts were prepared that persons
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such as the plaintiffs might rely on the accounts for the purpose of deciding whether to take over the company and might suffer loss if the accounts were inaccurate. Since the defendants knew at the time the accounts were prepared that the company needed outside financial support and ought reasonably to have foreseen that a take-over was a possible means of obtaining finance and that a person effecting a take-over might rely on those accounts, it followed that the defendants owed the plaintiffs a duty of care in the
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preparation of the accounts. The defendants were in breach of that duty by negligently including in the accounts stock at a value of some £13,000 over the discounted cost without appending a note in the accounts to that effect (see p 296 *h j*, p 300 *j* to p 301 *d* and *g* to p 302 *c* and *j* to p 303 *a* and *f* to p 304 *a*, post); dicta of Lord Wilberforce and of Lord Salmon in *Anns v London Borough of Merton* [1977] 2 All ER at 498–499, 512–513, *Scott Group Ltd v McFarlane* [1978] 1 NZLR 553 and *Ross v Caunters* (a firm) [1979] 3 All ER 580 applied.

(2) However, even though the plaintiffs had relied on the accounts, they would not have acted differently had they known the true position, since they knew the company was in financial difficulties, their reason for taking over the company was to obtain the services of its directors and the consideration paid for the company was only nominal. Accordingly, the defendants' negligence in preparing the accounts was not a cause of any loss suffered by the plaintiffs as a result of taking over the company. The plaintiffs' action would therefore be dismissed (see p 305 *e* to *h*, post).

Note

For damages for negligent statements in precontractual negotiations, see 31 Halsbury's Laws (4th Edn) paras 1099–1102.

Cases referred to in judgment

Anns v London Borough of Merton [1977] 2 All ER 492, [1978] AC 728, [1977] 2 WLR 1024, 191 JP 526, 75 LGR 555, HL, Digest (Cont Vol E) 449, *99b*.

Barton v Armstrong (1973) [1975] 2 All ER 465, [1976] AC 104, [1975] 2 WLR 1050, 3 ALR 355, PC, 12 Digest (Reissue) 117, **486a*.

Candler v Crane, Christmas & Co [1951] 1 All ER 426, [1951] 2 KB 164, CA, 36(1) Digest (Reissue) 22, *75*.

Derry v Peek (1889) 14 App Cas 337, [1886–90] All ER Rep 1, 58 LJ Ch 864, 61 LT 265, 54 JP 148, 1 Meg 292, HL, 9 Digest (Reissue) 123, *650*.

Donoghue (or M'Alister) v Stevenson [1932] AC 562, [1932] All ER Rep 1, 101 LJPC 119, 37 Com Cas 350, 1932 SC (HL) 31, 1932 SLT 317, HL, 36(1) Digest (Reissue) 144, *562*.

Everett v Griffiths [1920] 3 KB 163, 89 LJKB 929, 123 LT 280, 84 JP 161, CA; *affd* [1921] 1 AC 631, 90 LJKB 737, 125 LT 230, 85 JP 149, 19 LGR 283, HL, 33 Digest (Repl) 709, *1659*.

Grover Industrial Holdings Ltd v Newman Harris & Co (12th January 1976, unreported).

Haig v Bamford, Hagan, Wicken and Gibson [1976] WWR 331.

Hedley Byrne & Co Ltd v Heller & Partners Ltd [1963] 2 All ER 575, [1964] AC 465, [1963] 3 WLR 101, [1963] 1 Lloyd's Rep 485, HL, 36(1) Digest (Reissue) 24, *84*.

Le Lievre v Gould [1893] 1 QB 491, 62 LJQB 353, 68 LT 626, 57 JP 484, CA, 36(1) Digest (Reissue) 9, *27*.

Low v Bouverie [1891] 3 Ch 82, [1891–4] All ER Rep 348, 60 LJ Ch 594, 65 LT 533, CA, 35 Digest (Repl) 34, *258*.

Home Office v Dorset Yacht Co Ltd [1970] 2 All ER 294, [1970] AC 1004, [1970] 2 WLR 1140, [1970] 1 Lloyd's Rep 453, HL, 36(1) Digest (Reissue) 27, *93*.

Rhode Island Hospital Trust National Bank v Swartz, Bresenoff, Yavner & Jacobs (1972) 455 F 2d 847.

Ross v Caunters (a firm) [1979] 3 All ER 580, [1980] Ch 297, [1979] 3 WLR 605, Digest (Cont Vol E) 451, *158b*.

SCM (UK) Ltd v W J Whittall & Son Ltd [1970] 3 All ER 245, [1971] 1 QB 337, [1970] 3 WLR 494, CA, 36(1) Digest (Reissue) 28, *94*.

Scott Group Ltd v McFarlane [1978] 1 NZLR 553.

Spartan Steel & Alloys Ltd v Martin & Co (Contractors) Ltd [1972] 3 All ER 557, [1973] QB 27, [1972] 3 WLR 502, CA, 17 Digest (Reissue) 149, *403*.

Sykes v Midland Bank Executor & Trustee Co Ltd [1970] 2 All ER 471, [1971] 1 QB 113, [1970] 3 WLR 273, CA, Digest (Cont Vol C) 897, *862a*.

Ultramares Corpn v Touche (1931) 174 NE 441.

Weller & Co v Foot and Mouth Disease Research Institute [1965] 3 All ER 560, [1966] 1 QB 569, [1965] 3 WLR 1082, [1965] Lloyd's Rep 414, 36(1) Digest (Reissue) 45, *143*.

Action

By a writ issued on 31st May 1978, the plaintiffs, JEB Fasteners Ltd, claimed against the defendants, Marks, Bloom & Co (a firm), damages for loss suffered by the plaintiffs

following the acquisition of the issued share capital of a company, BG Fasteners Ltd,
a which the plaintiffs claimed to have done in reliance on the accounts of the company negligently prepared by the defendants as accountants and auditors of the company. The facts are set out in the judgment.

Murray Pickering for the plaintiffs.
Quintin J Iwi and *Andrew Jordan* for the defendants.

b

Cur adv vult

19th December. **WOOLF J** read the following judgment: In this action the plaintiffs are claiming damages from the defendants who are a firm of chartered accountants, in respect of the alleged negligence of the defendants in preparing the audited accounts of
c a company called BG Fasteners Ltd.

In June 1975 the plaintiffs acquired the entire share capital of that company. They contend that they would not have purchased the company if they had known its true financial position, but that they did so relying on its audited accounts for the year ending 31st October 1974, prepared by the defendants, which did not give a true and fair view of the state of the company. The plaintiffs allege that they have suffered substantial loss
d and damage as a result of the purchase of the company.

Before going into the facts in great detail it is desirable if I indicate my views as to the legal issues involved which have been in dispute before me.

In order to succeed in this case, the plaintiffs have to establish as a matter of law that the defendants owed them a duty of care so as to give rise to liability if they were negligent in the preparation of the accounts. It is not alleged that at the time the
e accounts were audited the defendants knew that the accounts would be relied on by the plaintiffs. Indeed, no takeover was then contemplated, and counsel for both the plaintiffs and the defendants agree that there is no direct English authority on the question whether the defendants owe such a duty in those circumstances.

The plaintiffs contend that an auditor, in preparing the audited accounts of a company, owes a duty of care to all persons who he ought to know could rely on the accounts, and
f the test is one of reasonable foresight or contemplation based on status and proximity. Furthermore, the duty is not limited by the absence of a request for information by the person relying on the accounts, or the fact that at the time of the audit the person is unidentified, or the fact that that person only suffers financial loss.

Before the decision of the House of Lords in *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1963] 2 All ER 575, [1964] AC 465 it could not have been argued before a judge of
g first instance that there was any possible liability in such circumstances. However, in that case the House of Lords overruled the majority judgment of the Court of Appeal in *Candler v Crane, Christmas & Co* [1951] 1 All ER 426, [1951] 2 KB 164 and approved the dissenting judgment of Denning LJ, expressly in the case of Lord Devlin (see [1963] 2 All ER 575 at 611, [1964] AC 465 at 530).

In his judgment in *Candler v Crane, Christmas & Co* Denning LJ dealt with the question
h of whether or not accountants owed a duty. First he said ([1951] 1 All ER 426 at 433, [1951] 2 KB 164 at 179–180):

> 'Let me now be constructive and suggest the circumstances in which I say that a duty to use care in making a statement does exist apart from a contract in that behalf. First, what persons are under such duty? My answer is those persons, such as accountants, surveyors, valuers and analysts, whose profession and occupation it
> j is to examine books, accounts, and other things, and to make reports on which other people—other than their clients—rely in the ordinary course of business. Their duty is not merely a duty to use care in their reports. They have also a duty to use care in their work which results in their reports. Herein lies the difference between these professional men and other persons who have been held to be under no duty

to use care in their statements, such as promoters who issue a prospectus: *Derry* v. *Peek* ((1889) 14 App Cas 337, [1886–90] All ER Rep 1) (now altered by statute [Companies Act 1948, s. 43]), and trustees who answer inquiries about the trust funds: *Low* v. *Bouverie* ([1891] 3 Ch 82, [1891–4] All ER Rep 348). Those persons do not bring, and are not expected to bring, any professional knowledge or skill into the preparation of their statements. They can only be made responsible by the law affecting persons generally, such as contract, estoppel, innocent misrepresentation or fraud. It is, however, very different with persons who engage in a calling which requires special knowledge and skill. From very early times it has been held that they owe a duty of care to those who are closely and directly affected by their work apart altogether from any contract or undertaking in that behalf.'

Further on Denning LJ continued as follows ([1951] 1 All ER 426 at 433–434, [1951] 2 KB 164 at 180–181):

'The same reasoning has been applied to medical men who make reports on the sanity of others: see *Everett* v. *Griffiths* ([1920] 3 KB 163 at 182, 217). It is, I think, also applicable to professional accountants. They are not liable, of course, for casual remarks made in the course of conversation, nor for other statements made outside their work, or not made in their capacity as accountants . . . but they are, in my opinion, in proper cases, apart from any contract in the matter, under a duty to use reasonable care in the preparation of their accounts and in the making of their reports. Secondly, to whom do these professional people owe this duty? I will take accountants, but the same reasoning applies to the others. They owe the duty, of course, to their employer or client, and also, I think, to any third person to whom they themselves show the accounts, or to whom they know their employer is going to show the accounts so as to induce him to invest money or take some other action on them. I do not think, however, the duty can be extended still further so as to include strangers of whom they have heard nothing and to whom their employer without their knowledge may choose to show their accounts. Once the accountants have handed their accounts to their employer, they are not, as a rule, responsible for what he does with them without their knowledge or consent.'

Denning LJ then referred to *Le Lievre v Gould* [1893] 1 QB 491 and then continued ([1951] 1 All ER 426 at 434, [1951] 2 KB 164 at 181):

'Excluding such cases as those, however, there are some cases—of which the present is one—where the accountants know all the time, even before they present their accounts, that their employer requires the accounts to show to a third person so as to induce him to act on them, and then they themselves, or their employers, present the accounts to him for the purpose. In such cases I am of opinion that the accountants owe a duty of care to the third person. The test of proximity in these cases is: Did the accountants know that the accounts were required for submission to the plaintiff and use by him?'

Denning LJ continued ([1951] 1 All ER 426 at 436, [1951] 2 KB 164 at 184–185):

'One final word. I think the law would fail to serve the best interests of the community if it should hold that accountants and auditors owe a duty to no one but their client. Its influence would be most marked in cases where the client is a company or firm controlled by one man. It would encourage accountants to accept the information which the one man gives them without verifying it, and to prepare and present the accounts rather as a lawyer prepares and presents a case, putting the best appearance on the accounts they can without expressing their personal opinion of them. This is, to my way of thinking, an entirely wrong approach. There is a great difference between the lawyer and the accountant. The lawyer is never called on to express his personal belief in the truth of his client's case, whereas the accountant, who certifies the accounts of his client, is always called on to express his personal opinion whether the accounts exhibit a true and correct view of his client's *a* affairs, and he is required to do this, not so much for the satisfaction of his own client, but more for the guidance of shareholders, investors, revenue authorities, and others who may have to rely on the accounts in serious matters of business. If we should decide this case in favour of the defendants, there will be no reason why accountants should ever verify the word of the one man in a one-man company, because there will be no one to complain about it. The one man who gives them *b* wrong information will not complain if they do not verify it. He wants their backing for the misleading information he gives them, and he can only get it if they accept his word without verification. It is just what he wants so as to gain his own ends. And the persons who are misled cannot complain because the accountants owe no duty to them. If such be the law, I think it is to be regretted, for it means that the accountants' certificate, which should be a safeguard, becomes a snare for *c* those who rely on it. I do not myself think that it is the law. In my opinion, accountants owe a duty of care not only to their own clients, but also to all those whom they know will rely on their accounts in the transactions for which those accounts are prepared.'

In *Candler*, although the facts are in some respects similar to those in the present case, it was clear that the accountants concerned had knowledge that the accounts were to be *d* supplied to the plaintiffs, and of the specific purpose for which they were required. It is therefore understandable that Denning LJ, having dealt with liability of accountants who had such knowledge and the position of strangers to the accountants to whom their employer without their knowledge chose to show their accounts, did not deal specifically with the position where the accountants had no actual knowledge that the accounts would be shown to a particular person, but should reasonably have foreseen that the *e* accounts could be shown to a third person who would rely on them.

However, in *Grover Industrial Holdings Ltd v Newman Harris & Co* (12th January 1976, unreported) (a transcript of which was placed before me), Stocker J makes it clear that he could see no good reason in principle why negligent accountants should not owe a duty of care 'to those who can be foreseen as likely to sustain damage if carelessness existed'. However, having examined the authorities, including the judgment of Cardozo CJ in the *f* American case of *Ultramares Corpn v Touche* (1931) 174 NE 441, he felt he was precluded from confirming there was such a duty, though on the facts of that case he was able to come to the conclusion that a duty existed.

In the *Ultramares* case the accountants had no prior knowledge of the plaintiffs and were held not liable in negligence to a company which had extended credit in reliance on certified accounts prepared by the accountants. The situation was one where the *g* range of the transactions in which the certificate of audit might be expected to play a part was not confined in any way, and it was in that situation that Cardozo CJ (at 444) made his important statement of principle that—

> 'If liability for negligence exists, a thoughtless slip or blunder, the failure to detect a theft or forgery beneath the cover of deceptive entries, may expose accountants to *h* a liability in an indeterminate amount for an indeterminate time to an indeterminate class. The hazards of a business conducted on these terms are so extreme as to enkindle doubt whether a flaw may not exist in the implication of a duty that exposes to these consequences.'

If there had been no further decisions of the courts since the judgment of Stocker J *j* I would have felt equally constrained from finding that there was any general duty based on foreseeability. However, since the decision of Stocker J, there have been three further authorities which throw more light on the subject.

The first is *Anns v London Borough of Merton* [1977] 2 All ER 492, [1978] AC 728. The facts of that case bear no relation to the facts under consideration. However, in the course of his speech Lord Wilberforce dealt in general terms with the circumstances in which a duty of care can arise. He said ([1977] 2 All ER 492 at 498–499, [1978] AC 728 at 751): a

> 'Through the trilogy of cases in this House, *Donoghue v Stevenson* [1932] AC 562, [1932] All ER Rep 1, *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1963] 2 All ER 575, [1964] AC 465 and *Home Office v Dorset Yacht Co Ltd* [1970] 2 All ER 294, [1970] AC 1004, the position has now been reached that in order to establish that a duty of care arises in a particular situation, it is not necessary to bring the facts of that situation within those of previous situations in which a duty of care has been held b
> to exist. Rather the question has to be approached in two stages. First one has to ask whether, as between the alleged wrongdoer and the person who has suffered damage there is a sufficient relationship of proximity or neighbourhood such that, in the reasonable contemplation of the former, carelessness on his part may be likely to cause damage to the latter, in which case a prima facie duty of care arises. Secondly, if the first question is answered affirmatively, it is necessary to consider whether c
> there are any considerations which ought to negative, or to reduce or limit the scope of the duty or the class of person to whom it is owed or the damages to which a breach of it may give rise (see the *Dorset Yacht* case [1970] 2 All ER 294 at 297–298, [1970] AC 1004 at 1027, per Lord Reid). Examples of this are *Hedley Byrne & Co Ltd v Heller & Partners Ltd* where the class of potential plaintiffs was reduced to those shown to have relied on the correctness of statements made, and *Weller & Co v Foot* d
> *and Mouth Disease Research Institute* [1965] 3 All ER 560, [1966] 1 QB 569 and (I cite these merely as illustrations, without discussion) cases about 'economic loss' where, a duty having been held to exist, the nature of the recoverable damages was limited (see *SCM (United Kingdom) Ltd v W J Whittall & Son Ltd* [1970] 3 All ER 245, [1971] 1 QB 337, *Spartan Steel and Alloys Ltd v Martin & Co (Contractors) Ltd* [1972] 3 All ER 557, [1973] QB 27).' e

And Lord Salmon, in the course of his speech, said ([1977] 2 All ER 492 at 512–513, [1978] AC 728 at 769):

> 'There are a wide variety of instances in which a statement is negligently made by a professional man which he knows will be relied on by many people besides his client, eg a well-known firm of accountants certifies in a prospectus the annual f
> profits of the company issuing it and unfortunately, due to negligence on the part of the accountants, the profits are seriously overstated. Those persons who invested in the company in reliance on the accuracy of the accountants' certificate would have a claim for damages against the accountants for any money they might have lost as a result of the accountants' negligence: see the *Hedley Byrne* case.' g

The second case is a decision of the New Zealand Court of Appeal, *Scott Group Ltd v McFarlane* [1978] 1 NZLR 553. As is apparent from the headnote, the facts of that case were similar to this case. Richmond P thought the maker of a statement would not owe a duty unless the maker of the statement was or ought to have been aware that his advice or information would in fact be made available to and would be relied on by a particular person or class of persons for the purpose of the particular transaction or type of h
transaction. I stress the reference to a particular person and a particular transaction, because on the facts in this case the plaintiffs could not comply with this requirement.

In his examination of the authorities Richmond P referred to a Canadian decision, *Haig v Bamford, Hagan, Wicken and Gibson* [1976] WWR 331. Richmond P pointed out that in that case the court held it was sufficient that the accountants were aware when they prepared the statements that they were intended to be used by a limited class of j
potential investors. It was unnecessary to show that they had actual knowledge of the specific plaintiff who would use and rely on the statements. Richmond P added (at 562):

> 'With this conclusion I unhesitatingly and respectfully agree. But in the *Haig* case it was not necessary to decide whether something less than actual knowledge of the

purpose for which the statement was required would be sufficient. In particular it was not necessary to decide whether it would have been sufficient if the accountants ought reasonably to have foreseen, in a general way, that the statement might be used for the purpose of attracting investors.'

The second judgment in the New Zealand case was a dissenting judgment given by Woodhouse J, who relied on the passage from the speech of Lord Wilberforce in *Anns v London Borough of Merton*, which I have cited, and stated that it was his opinion that the problem was to be approached 'by the comprehensible straightforward test of foreseeability'. With regard to Lord Wilberforce's second stage Woodhouse J stated (at 574):

> '... a need to establish knowledge of the very identity of those proposing to act upon advice would seem not merely an extremely stringent but an almost fortuitous test of responsibility.'

Woodhouse J however, thought it unwise to endeavour to lay down in advance precise rules as to when responsibility should be waived or modified and considered the facts of individual cases are likely to provide a far more reliable and equitable guide. When he examined the case before the court he came to the conclusion that a duty of care was owed notwithstanding the fact that the auditors had no direct knowledge of the plaintiffs or that a takeover from any quarter was contemplated.

The third judge, Cooke J, expressly agreed with Woodhouse J that in the circumstances of that case a duty of care was owed. Cooke J (at 584) also relied on the speech of Lord Wilberforce in *Anns v London Borough of Merton* and took the view that the evidence disclosed 'a plain risk of a takeover and the virtual certainty that in such an event the accounts would be relied upon by an offeror'. He therefore decided that, on the facts of the case as between the alleged wrongdoer and the person who had allegedly suffered damage, there was a sufficient relationship of proximity or neighbourhood such that it should have been in the reasonable contemplation of the former that carelessness on his part would be likely to cause damage to the latter. So, prima facie, a duty of care arose.

Cooke J went on to consider whether there were any considerations which ought to negative or to reduce or limit the scope of the duty or the class of persons to whom it was owed or the damages to which a breach of it may give rise, and concluded that the class was narrowly limited; and liability to even that limited class could have been excluded by disclaimer.

It follows that, although Woodhouse J dissented, on the question which is important here both he and Cooke J were of the opinion that a duty of care could arise even though the auditor was not aware that his information would be made available to a particular person for the purpose of a particular transaction, and, on this point, it was Richmond P who was in the minority.

The third of the three cases is *Ross v Caunters* [1979] 3 All ER 580, [1980] Ch 297, a decision of Sir Robert Megarry V-C. That was a case concerning solicitors' negligence in which the Vice-Chancellor, in considering the question of whether or not a solicitor owed a duty to a named beneficiary in a will of his client, also adopted the test laid down by Lord Wilberforce in *Anns v London Borough of Merton*, and decided that a duty was owed. The issues were very different from those in this case, but having examined the authorities the Vice-Chancellor summarised his conclusions, inter alia, as follows ([1979] 3 All ER 580 at 599–600, [1980] Ch 279 at 322–323):

> 'The basis of the solicitor's liability to others is either an extension of the *Hedley Byrne* principle or, more probably, a direct application of the principle of *Donoghue v Stevenson* ... A solicitor who is instructed by his client to carry out a transaction that will confer a benefit on an identified third party owes a duty of care towards that third party in carrying out that transaction, in that the third party is a person within his direct contemplation as someone who is likely to be so closely and directly affected by his acts or omissions that he can reasonably foresee that the third

party is likely to be injured by those acts or omissions . . . The mere fact that the loss to such a third party caused by the negligence is purely financial, and is in no way *a* a physical injury to person or property, is no bar to the claim against the solicitor . . . In such circumstances there are no considerations which suffice to negative or limit the scope of the solicitor's duty to the beneficiary.'

If foreseeability of risk of causing injury plays a part in establishing the liability of a solicitor, it must also play a part in establishing the liability of an accountant, and for this reason alone the judgment of Sir Robert Megarry V-C is of help. However, he said *b* ([1979] 3 All ER 580 at 592, [1980] Ch 279 at 313–314), with regard to *Hedley Byrne*:

'*Hedley Byrne* is important, of course, as opening the door to the recovery of damages for negligence to at least some cases where the negligence has caused purely financial loss, without any injury to person or property . . . But for present purposes its importance is that the House of Lords rejected pure *Donoghue v Stevenson* *c* principles as forming the basis of liability for negligent mis-statements and instead based liability on the plaintiff having trusted the defendant to exercise due care in giving information on a matter in which the defendant had a special skill, and knew or ought to have known of the plaintiff's reliance on his skill and judgment. In this type of case, reliance forms part of the test of liability, as well as part of the chain of causation: and the effect of such a test of liability is to confine the extent of liability *d* far more closely than would an application of pure *Donoghue v Stevenson* principles. If liability for negligently putting into circulation some innocent misrepresentation were to be imposed on the same basis as negligently putting into circulation some dangerous chattel, the resulting liability might be for enormous sums to a great multiplicity of plaintiffs. One way of preventing any such liability being imposed is to make the test of liability more strict: and that was the way adopted in *Hedley* *e* *Byrne*. But that does not affect those cases in which the principles of *Donoghue v Stevenson* apply. If I am right in thinking that the case before me falls within those principles, then there is no need to consider questions of reliance.'

The importance of this passage is that if Sir Robert Megarry V-C is right, as with respect I think he is, the fact of reliance on the statement is sufficient limitation on liability to overcome the danger raised by Cardozo CJ. In view of Stocker J's statement *f* that he regarded it as—

'paradoxical that no duty of care should be owed to those who can be foreseen as likely to sustain damage if carelessness existed, but that a duty of care should be owed to those, their clients, in respect of whom there is no foreseeable risk of damage,' *g*

I have little doubt that if the three cases to which I have made reference were available to him, Stocker J would not have felt the same constraint. Particularly as the law in the United States appears also to have advanced as a result of *Hedley Byrne* (see the Second Restatement of the Law of Torts (1977), § 552, and *Rhode Island Hospital Trust National Bank v Swartz, Bresenoff, Yavner & Jacobs* (1972) 455 F 2d 847). *h*

Without laying down any principle which is intended to be of general application, on the basis of the authorities which I have cited, the appropriate test for establishing whether a duty of care exists appears in this case to be whether the defendants knew or reasonably should have foreseen at the time the accounts were audited that a person might rely on those accounts for the purpose of deciding whether or not to take over the company and therefore could suffer loss if the accounts were inaccurate. Such an *j* approach does place a limitation on those entitled to contend that there has been a breach of duty owed to them. First of all, they must have relied on the accounts and, second, they must have done so in circumstances where the auditors either knew that they would or ought to have known that they might. If the situation is one where it would not be reasonable for the accounts to be relied on, then, in the absence of express knowledge, the auditor would be under no duty. This places a limit on the circumstances in which the audited accounts can be relied on and the period for which they can be relied on. The longer the period which elapses prior to the accounts being relied on, from the date on which the auditor gave his certificate, the more difficult it will be to establish that the auditor ought to have foreseen that his certificate would, in those circumstances, be relied on.

It was argued on behalf of the defendants in this case that, if contrary to their primary contention they were under any liability to the plaintiffs, then the plaintiffs were guilty of contributory negligence. The plaintiffs contended that the Law Reform (Contributory Negligence) Act 1945 did not apply to actions founded on an allegation of negligent misrepresentation. It was submitted on behalf of the plaintiffs that there was no precedent for a defence based on contributory negligence. In support of this contention the plaintiffs relied on *Sykes v Midland Bank Executor Co* [1970] 2 All ER 471, [1971] 1 QB 113 and *Barton v Armstrong* [1975] 2 All ER 465, [1976] AC 104. In neither of those cases was the court considering the question of the application of the Law Reform (Contributory Negligence) Act 1945, and I do not consider that they are of any assistance on this issue.

It is true that in the latter case Lord Cross said ([1975] 2 All ER 465 at 474, [1976] AC 104 at 118):

> 'If on the other hand Barton relied on the misrepresentation Armstrong could not have defeated his claim to relief by showing that there were other more weighty causes which contributed to his decision to execute the deed, for in this field the court does not allow an examination into the relative importance of contributory causes.'

That statement of Lord Cross is of great assistance in deciding whether or not there liability is owed by the representor to the representee, but it does not help as to whether the representor is entitled to have his damages reduced under the provisions of the Law Reform (Contributory Negligence) Act 1945. The words of s 1(1) of that Act are in very wide terms and I can see no reason why those terms are not sufficiently wide to cover a case involving a negligent misrepresentation.

In the course of argument, counsel for the plaintiffs also referred me to 31 Halsbury's Laws (4th Edn) paras 1066–1069. I am afraid that I deterred him from citing additional authorities in support of the statements in those paragraphs. I did not consider that they would assist me because, again, in my view, they were not considering the question which I have to consider, which is the application of the 1945 Act.

I do, however, recognise that it may well be that in the case of negligent misrepresentation the scope for contributory negligence is limited since an auditor will only be liable if he should foresee that someone might rely on his accounts and, as I have sought to indicate, this involves it being reasonable for the person concerned to rely on the accounts. If it is reasonable to rely on the accounts, it is difficult to envisage circumstances where as a matter of fact it would be negligent to do so without taking further steps to protect yourself from the consequence of relying on the auditor's certificate.

Having expressed my views as to the matters of law which are in dispute, the issues between the parties can be summarised as follows.

1. The foreseeability issue: that is, ought the defendants to have realised, when auditing BG Fasteners Ltd's accounts for the year ending 31st October 1974, that those accounts could be relied on in the circumstances in which they were allegedly relied on by the plaintiffs for the purpose of taking over BG Fasteners Ltd?

2. The reliance issue: in coming to their decision to take over BG Fasteners Ltd, did the plaintiffs rely on the accounts audited by the defendants?

3. The negligence issue: were the defendants negligent in the preparation of those accounts?

4. The causation issue: that is, did the plaintiffs suffer any loss in consequence of the alleged negligence?

5. The contributory negligence issue: that is, did the plaintiffs contribute to their alleged loss by their own negligence?

6. The quantum issue: the assessment of the plaintiffs' alleged loss.

Before considering each issue in turn, it is necessary to say something more about the facts of the case. The defendants are a small firm of chartered accountants. The membership of the firm has changed from time to time but the one constant feature has been Mr Marks, who is a chartered accountant of many years' standing. He qualified before the last war and has been continuously in practice since that time.

The plaintiffs are well-established suppliers of industrial fasteners, fasteners coming in many sorts from screws upwards. The company is a family one run by the Bufton family. There were two principal directors at the times with which this case was mainly concerned, John Bufton and his brother Eric Bufton. Eric Bufton has unfortunately since died, and it is to John Bufton I will mainly refer in the course of this judgment. John Bufton has some accounting training and spent some time in Shell before becoming involved with the plaintiffs' business.

By 1974 the plaintiffs were in a position where they had finance available for the expansion of their business, and the Buftons were anxious to make use of this finance by extending the area of their operations. They became aware of another fastener business, namely, that of BG Fasteners Ltd which carried on similar activities to the plaintiffs, but in an adjacent area. The business of BG Fasteners Ltd had been initially commenced by Mr George Godridge under the name BG Fasteners. Mr Godridge had previously been employed by a large public company which, among other things, manufactured fasteners, and in about August 1972 he set up in business on his own account under the style BG Fasteners. Subsequently he was joined by Mr Wigg and in due course, on the 20th September 1973, the company BG Fasteners Ltd, was incorporated to take over the business which had previously been carried on by Mr Godridge and Mr Wigg.

On 1st November 1973 BG Fasteners Ltd started trading with Mr Godridge and Mr Wigg acting as its directors.

From the time that Mr Godridge had started trading on his own account in 1972, Mr Marks acted as his accountant, giving general financial advice. In due course the defendants became auditors of the company and ultimately they prepared the first audited accounts of the company for the year ended 31st October 1974, which were dated 14th April 1975. BG Fasteners Ltd's turnover expanded satisfactorily but, as often happens with new companies, liquidity proved a problem and from an early stage the defendants were well aware that financial support was being sought in various forms. Although Mr Marks was not very happy about this, resort was had to factoring. Loans had to be obtained from the company's bankers, and in 1974 the question arose of some sort of arrangement being come to between the plaintiffs and BG Fasteners Ltd whereby the plaintiffs would invest money in that company. At that time, however, there was no question of a take-over.

As early as 2nd August 1974, Mr Marks was writing to Mr Godridge enclosing copies of the draft trading and profit and loss account, covering the period 1st November 1973 to 17th July 1974, which he indicated the company required for their dealing with the plaintiff company. Mr Marks said that he was of the opinion that the plaintiffs would want further information and that, if he could be of any assistance, not to hesitate to let him know.

On 14th April 1975 Mr Marks, who was undoubtedly aware of the financial problems of BG Fasteners Ltd, wrote to Mr Godridge and Mr Wigg enclosing a fair copy of the accounts for the year ended 31st October 1974, indicating that he was anxious that the accounts should be received at that stage in order that those gentlemen could visit the bank manager with the figures. He also stated that he had forwarded a copy of the accounts to the bank manager although they had not been signed by him or certified. Subsequently the accounts were certified by the defendants and dated 14th April 1975.

The certificate was in these terms:

'REPORT OF THE AUDITORS TO THE MEMBERS OF B. G. FASTENERS LTD.

'In our opinion the above Balance Sheet and Trading and Profit and Loss Account gives a true and fair view of the state of the Company's affairs as at the 31st October, 1974 and of its Profit at that date and complies with the Companies Acts 1948 and 1967.'

The trading and profit and loss account showed a net profit of £11·25. The account also showed stock, as at 1st November 1973, of £5,051·96, purchases of £54,251·65, and a gross profit of £23,262·78. Sales were indicated as being £59,486·03 and stock, as at 31st October 1974, of £23,080·36. In the balance sheet under 'current assets' it was stated, 'Stock as valued at lower of cost and net realisable value £23,080·36'.

After the accounts had been certified there was first canvassed a proposal by the plaintiffs to take over BG Fasteners Ltd. Mr Marks was fully aware of the progress of the negotiations on which he advised Mr Godridge and Mr Wigg. He also supplied information to the plaintiffs at the request of Mr Bufton.

On 23rd June 1975 the plaintiffs acquired the share capital of BG Fasteners Ltd from Mr Godridge and Mr Wigg. In exchange for the 500 £1 shares in BG Fasteners Ltd, Mr Godridge and Mr Wigg each received 50 £1 ordinary shares in the plaintiffs. In addition, Mr Godridge and Mr Wigg were appointed directors of the plaintiffs and loans which they had made to BG Fasteners Ltd were repaid.

On 24th June the defendants submitted their account in connection with advising relative to the take-over, including correspondence with the plaintiffs and telephone conversations with Mr Bufton in the sum of £68·26.

On 8th July Mr Bufton wrote to the defendants asking them if they would provide a schedule giving details of debtors and creditors as at 31st October 1974, so that double entry accounts for the period 1st November 1974 to 30th June 1975, in respect of BG Fasteners Ltd, could be produced. That schedule was forwarded on 10th July 1975.

By 23rd July Mr Bufton had prepared elementary accounts relating to BG Fasteners Ltd for the period up to 30th June 1975, which showed a net loss before tax of £910 based on an estimated gross profit of 36% on sales. The figure for sales for that period shown in that account was £59,839, approximately the same figure as the sales shown in the audited accounts for the previous 12 months.

On 22nd July Mr Bufton was already unhappy about the accounts for the 12 months' period and he wrote to the defendants indicating that the accounts failed to show sales amounting to £5,040·59, that certain purchases had not been taken up in the accounts and that an error had been made in arriving at trade debtors. He also indicated that he thought there was difficulty in verifying the cash on hand and indicating his view that it would be prudent for the accounts already failed to be withdrawn. Mr Marks did not agree to this.

In the proceedings before me, Mr Godridge and Mr Wigg did not give evidence, but certain serious criticisms were made of them by Mr Bufton and it appeared that those criticisms could well have substance. As I have not heard the answer which those gentlemen may have to the allegations, I do not propose to say any more about their shortcomings in this judgment, although I should make it clear that, in my consideration of these issues, I am going to assume that the criticisms were justified. The results during the period which is relevant to these proceedings make it quite clear that Mr Godridge and Mr Wigg were a great disappointment to the plaintiffs. Mr Bufton, in the course of his evidence, made no secret of the fact that he and his brother had been influenced to take over BG Fasteners Ltd because of the high regard they had for Mr Godridge and Mr Wigg, and their belief that they would, with the plaintiffs' backing, be able to build BG Fasteners Ltd into a flourishing business.

On 3rd May 1976 Mr Godridge wrote resigning from both companies, and Mr Wigg did likewise on 5th December 1976. If by that time the plaintiffs had not advanced substantial funds to BG Fasteners Ltd it is quite clear that that company would have had to go into liquidation owing substantial sums, and I am quite satisfied that in the short term the plaintiffs would have been substantially better off if they had not acquired the company. a

Within a relatively short time of the acquisition, the plaintiffs were well aware of the mistake which they had made, and as early as 23rd August 1976 their solicitors were writing to Mr Marks pointing out that they had been asked to advise the plaintiffs with regard to the affairs of BG Fasteners Ltd, and that the plaintiffs' auditors had drawn their attention to certain aspects of the 1974 accounts which gave rise to serious concern. The letter set out in some detail matters which were canvassed in detail before me. b

Having completed an investigation, on 3rd December 1976, the plaintiffs' then auditors, Turquands, Barton, Mayhew & Co, submitted their report as to the accounts prepared and certified by the defendants for the year ended October 1974, and these proceedings were commenced by a writ issued on 31st May 1978.

The majority of the eight days during which the trial lasted were taken up with the evidence of four witnesses, Mr Bufton and Mr Morphitis on behalf of the plaintiffs and Mr Marks and Mr Bolton on behalf of the defendants. Mr Morphitis was employed at the material time by Turquands and was responsible for carrying out the audit of the plaintiffs' accounts and the investigation into the October 1974 accounts of BG Fasteners Ltd, prepared by the defendants. Mr Bolton is a partner in the firm of Viney Merretts, a well-known firm of chartered accountants now incorporated in Binder Hamlyn. c

I am satisfied that all the witnesses who gave evidence before me were doing their best to assist me. So far as Mr Bufton and Mr Marks were concerned they had the difficulty that they were dealing with what occurred as long ago as 1975. Fortunately, what had happened is documented and the facts can be substantially ascertained from the documents. However, in critical matters Mr Bufton's evidence was vital and it is therefore necessary for me to indicate my assessment of him. Quite clearly he is an honest and careful man. Perhaps because of his partial training as an accountant he has a very high regard for the professional qualification of a chartered accountant and the certificate of an auditor who holds the qualification of chartered accountant is one which is of significance to him. He feels very strongly indeed about what has happened in consequence of the take-over of BG Fasteners Ltd. Indeed, at one stage in his evidence he associated the death of his brother with the results of that take-over. Because of the intensity of his feeling, I came to the conclusion that it was necessary to look at Mr Bufton's evidence with a degree of caution because his recollection could be coloured by the firm belief which he has now that all the troubles which followed the take-over could properly be put at Mr Marks's door. d e f

So far as Mr Morphitis is concerned, I was impressed by his undoubted skill, intelligence and ingenuity as an accountant. I did, however, feel that in certain respects, no doubt influenced by his own very high standards, he was apt to be unduly harsh in his criticism of the standards adopted by others. g

Mr Marks was an amiable witness and I have no doubt he is an accountant who in general provides very sound service and advice to his clients. He was in the unenviable position in this case of at times being embarrassed into seeking to defend the undefendable. However, in general I felt his evidence was more reliable than that of Mr Bufton's and, in so far as hereafter my conclusions are inconsistent with the evidence given by Mr Bufton, I have not accepted that evidence. h

Mr Bolton is clearly a competent accountant. In giving his opinion as to the propriety of accountants' conduct I considered that his standards were more in accord with those which should be required of the profession as a matter of law than Mr Morphitis. I did, however, regard Mr Morphitis as being more authoritative in respect of the calculations which he made and in relation to the investigation which he had carried out. j

I will now turn to the issues I adumbrated earlier.

1. The foreseeability issue

As Mr Marks was aware of the financial difficulties of BG Fasteners Ltd and the fact

that they were going to need financial support from outside of some sort, I am satisfied
a that Mr Marks, whom I can treat as being synonomous with the defendants, ought to have realised the accounts could be relied on up till the time that a further audit was carried out by the commercial concerns to whom BG Fasteners Ltd were bound to look for financial assistance. When he audited the accounts, Mr Marks would not know precisely who would provide the financial support, or what form the financial support would take, and he certainly had no reason to know that it would be by way of takeover
b by the plaintiffs. However, this was certainly one foreseeable method and it does not seem to me that it would be right to exclude the duty of care merely because it was not possible to say with precision what machinery would be used to achieve the necessary financial support. Clearly any form of loan would have been foreseeable including the raising of money by way of debenture, and, while some methods of raising money were more obvious than others and a take-over was not the most obvious method, it was
c certainly one method which was within the contemplation of Mr Marks.

I have little doubt that if Mr Marks had asked himself, before the accounts were certified by him, whether those accounts would be used by BG Fasteners Ltd for the purpose of raising money during the coming year he would have answered Yes, and if he had then been asked whether one method of raising money which could be used would be a take-over he would also have answered Yes, although a take-over is not strictly
d speaking a method of raising finance. He would not know that the financial support would be provided by the plaintiffs, but certainly by the time the accounts were certified they were sufficiently on the scene to be a possible source of finance.

I would therefore answer the first issue in favour of the plaintiffs.

2. The reliance issue

e As I have partially anticipated in outlining the facts, it is my view that the predominant motive for the plaintiffs deciding to take over BG Fasteners Ltd was the fact that they thought that Mr Godridge and Mr Wigg, in the form of BG Fasteners Ltd, would be the ideal vehicle to complement their existing business. I do not think that the plaintiffs were particularly concerned about the progress that BG Fasteners Ltd had made up to that time, as the plaintiffs, through their directors, took the view that, allied to the
f plaintiffs, BG Fasteners Ltd would be in a much better position to achieve sales and profits than they had been previously. In this they were right, but, as I have indicated, they were not right about the value of Mr Godridge's and Mr Wigg's services. Therefore, I do not think that the accounts up to October 1974 were of critical importance to the plaintiffs, but this does not mean that they did not rely on them. I have no doubt that they were studied by Mr Bufton with care and they would indicate to him, as he said in
g evidence, that if they were correct the company, during its first year, had done reasonably well and was in a position of balance where it was making neither profits nor losses. Such a picture would certainly encourage him to take over the company, and in that sense I think the plaintiffs relied on the accounts, although as will appear hereafter I think that before the take-over Mr Bufton had reservations as to the accuracy of the accounts and their limited influence would be the importance which he attached to the auditors'
h certificate.

3. The negligence issue

There were various allegations of negligence with which I must deal in turn.

First, because it can be easily dealt with, there was the question of sales omitted. The revised figure in respect of the value of sales omitted, set out in the report prepared by Mr
j Morphitis, shows the figure as being £4,667. Mr Marks did not dispute that a figure in respect of sales in that region was omitted. He took a serious view of the error and it resulted in the member of his staff who was responsible, Mr Ahmed, being dismissed. While it was quite proper to employ Mr Ahmed to extract the figures, there was no justification for the error, and this was due to negligence for which the defendants were responsible. It was, however, an error, the effect of which was to make the accounts

appear less favourable rather than more favourable to BG Fasteners Ltd. It did, however,
mean that the certificate was wrong. It also cancelled out two other alleged errors to a
which I must refer.

One is the alleged omission of purchases amounting to £2,606. On the evidence
before me I find that purchases of approximately this amount were omitted. The
explanation for the omission was not the failure to make a request to the bank for
information. This was done in a satisfactory form, but not until 9th April 1975, so that
the reply from the bank was only received on 18th April 1975, after the accounts had b
been certified. However, the reply, when it was received, would not have helped since
it did not refer to the invoices which were being held by the bank awaiting payment, as,
Mr Bolton says in his report, perhaps it should have done. This does not exonerate the
defendants since I am satisfied that if the inquiry to the bank had not been delayed to the
extent which it was, or if more exhaustive investigations had been made of the company's
directors, these omitted purchases would have been discovered. There was, therefore, a c
default by the defendants which amounts to negligence in not ascertaining this.

The other alleged error relates to the expenses which are said to be understated, and
which are scheduled as appendix 3 to Mr Morphitis's report. The individual items are
not in themselves significant, apart from the ones which I shall deal with shortly
hereafter. Their significance, the plaintiffs contend, is their number. I have reservations
about this approach because there can be some small errors even in the most carefully d
audited accounts which will be revealed by a later investigation when the investigators
often have information available to them which was not available at the time of the
audit. In this respect I accept Mr Bolton's evidence that any subsequent examination of
a set of accounts is likely to disclose variations from the figures set out in the accounts,
some of which are dependent on estimations which have to be made at the audit date,
and that the minor differences do not warrant detailed comment. e

The first of the significant amounts is the £700 in respect of directors' remuneration,
which it is alleged was negligently omitted. Twelve salary payments were charged for
the year to October 1974, but Mr Morphitis is right in contending that cheques for salary
were probably drawn before the year-end, which were omitted from the accounts
because they were not debited in the bank account until after the year-end. Certain post
year-end debits in the bank account were written into the expenses of the year up to f
October 1974 in the accounts; and so it appears cheques drawn before the year-end but
debited after the year-end were investigated and a conscious decision taken not to include
this £700. Such a decision would not be taken without reason and I am not satisfied, on
the balance of probability, that there is not some explanation for this of which the
witnesses who gave evidence before me would not be aware, such as while the cheques
were drawn earlier they were not delivered to the directors until after the year-end when
the salary became due. I am therefore not prepared to draw any inference of negligence g
in respect of the non-inclusion of this sum in the accounts.

The other significant item is interest. The amount here is £366. As the defendants
were well aware that the company was overdrawn, they should have appreciated that
there must be some interest referable to the year in question, and in so far as it is relevant
to do so I do think that the defendants were at fault in not making some provision for this h
in the accounts.

Before moving on to the last item, I should emphasise that the negligence to which I
have already made reference has little significance because the sums involved would be
set off by the omission of sales.

Finally there is the allegation that the stock was wrongly described in the accounts.
The criticism which can properly be made is not that the stock could not possibly have j
properly been valued at the figure shown in the accounts but that it was wrongly
described as being the lower of cost and net realisable value. (It is not in dispute that that
means lower of cost or net realisable value.) Quite clearly it was known by the defendants
that in the figures supplied to them by the directors of BG Fasteners Ltd, there was a sum
for stock included which was put at a value which was in excess of cost because it was

contended that its net realisable value was higher than cost. Normally it is not proper practice to include in the accounts, as the valuation of stock, an item at a figure higher than cost. This is a matter of which Mr Marks was fully aware and in fact had commented on in the correspondence which is before me. Apparently a substantial part of the stock had been obtained at less than its normal selling price from Torrington Co Ltd; there is a letter of 11th October 1974 confirming this fact. On 17th October 1974 Mr Marks wrote to Mr Godridge and to Mr Wigg in respect of this, and the relevant parts of the letter read as follows:

> 'With regard to the valuation of the parcel of stock as shown on the aforementioned invoice of the Torrington Co. Ltd., as was explained to you previously it is not in accordance with good accountancy practice to bring in a value of stock other than the cost or market price whichever be the lower at the date of stock as taken and in a general way it is wrong to increase profits on an inflated stock figure. On the other hand if a separate valuation of the stock in question could be obtained to reflect the value as proposed this would be most useful and whilst I realise that the stock in question does run into a considerable number of items, you can of course appreciate the reason for having a third party valuation but in view of your agreement that the figure could be taken as £11,000 then subject to the note on any Balance Sheet as audited by myself or in any communication to a third party then I am prepared to deal with this point along these lines. I do of course appreciate your reasons for wanting this stock position to be clarified as far as H. & H. Factors are concerned and I will communicate with them along the lines of this letter but I would be much happier if sales could be made at the current prices or at a special price which would show a value of not less than 150% more than invoiced cost to you by the Torrington Co. Ltd. of any particular item as included on their invoice. This accordingly means that the minimum value of the prices to be received from the Torrington stock must exceed £11,000 after taking VAT at 8% into consideration.'

When the accounts were prepared, they included the items referred to in the letter which I have just read, at an inflated value, but there was no note to indicate that this is what had happened. The entry was clearly wrong and, furthermore, in my view there was negligence in not including a note to make the position clear in the way envisaged by Mr Marks in the letter to which I have just referred. This was, I am afraid, a case where, no doubt because of the very many pressures that were on Mr Marks, he fell short of the standards no doubt he normally adopts. To aggravate the difficulty Mr Bufton spoke to Mr Marks on about 19th June about stock and Mr Marks omitted to tell him on that occasion of what he should have been aware about the inflated value, but told him instead how the stock had been valued for the purpose of the audit in a manner which was misleading in that it stated that a figure of £29,000 had been the starting point of the valuation, from which had been deducted 20% for obsolescence and slow movers, and a further 2½% for possible errors in stock casting. (It seems that the latter figure was probably 2·8%.) On this matter I accept the evidence of Mr Bufton in preference to that of Mr Marks. I was not clear whether Mr Marks was conceding that he appreciated at the time that stock had been valued at a higher figure than cost, but if he was in any doubt about the matter he should not have been because a proper audit would have revealed what he knew previously, namely that the directors were intending to uplift the value of certain stock. The precise extent to which stock was wrongly shown, as the lower of cost or net realisable value, is difficult to ascertain with precision. It is not important for the present purposes that it should be. However, on the evidence before me, on the balance of probability, I accept the figures given by Mr Morphitis set out in appendix 3 of his report. That figure in the account is £12,097 in excess of cost, and an additional provision of £1,483 is needed to reduce cost to net realisable value, the result being that there is an overstatement of approximately £13,500 as to the figure for value of stock. This is an important matter in respect of which the defendants were negligent because, if the stock value is wrong, so is the profit figure wrong, and instead of a profit of £11 the accounts should have shown a loss in excess of £13,000.

4. The causation issue

Where a representation is made and it is relied on, there is a strong inference, in the absence of evidence to the contrary, that the results which follow were brought about by the representation. In addition, in this case, Mr Bufton gave evidence that if the accounts had shown what the defendants had represented them as showing, namely a true and fair view of the financial state of BG Fasteners Ltd, the plaintiffs would not have purchased that company. If he is right, then the loss which the plaintiffs suffered as a result of so doing came about because of a misrepresentation by the defendants. The issue is whether Mr Bufton is right.

In considering this issue, the important wrong entry is that as to the stock. The other errors in total, as I have already pointed out, approximately cancel themselves out, and, in any event, I do not accept that either individually or cumulatively they have affected the plaintiffs' decision in any way.

With regard to the stock, the plaintiffs had carried out their own stock check in June, prior to the take-over. This had thrown up a value of £13,500 which was increased to £15,000 to cover the cost of plating which the company had carried out on certain items. This figure apparently did not cover a large number of shoe heel nails at anything like the same value as had been attributed to them by BG Fasteners Ltd as the plaintiffs regarded them as being valueless. In addition, in the course of his evidence, Mr Bufton gave a picture of the stock generally which showed that it was in a very poor state indeed. Part could be described as 'slow moving', if it was at all saleable. It had not been stored in anything like ideal conditions, and I conclude from the evidence that a figure of £15,000 was well below its net realisable value.

I certainly accept Mr Bufton's view that the shoe heel nails, which were 1½ tons of stock, had a nil value. As Mr Bufton had been told by Mr Godridge that the stock was worth £25,000 at the time of the stock-taking, Mr Bufton must have been well aware that there was a very substantial difference between the view of the company as to the value of the stock and what had been found by the plaintiffs at stock-taking. Mr Bufton said (which is not surprising) that the question of stock valuation was discussed at great length with Mr Godridge and there were arguments about it. He says that Mr Godridge strongly disputed the plaintiffs' valuation and the plaintiffs' contention that lots of the stock was rubbish. However, despite what may have been said by Mr Godridge, I am sure that Mr Bufton must have appreciated it was being overvalued. Furthermore, he must also have known that if this was true in June 1975 it was also probably true in October 1974 since the condition of the stock was such that it indicated that it had been held a long time.

Mr Bufton was sufficiently knowledgeable about accounts to know that the question of the stock value was important, not only because of its significance in assessing the value of the assets of the company, but also because, if the stock value was wrong, other figures, and in particular the profit figure, in the accounts would be wrong.

It is true that, in addition to what his own stock valuation had shown, Mr Bufton had only limited information available. Mr Bufton said that the books were not made available to him and he had difficulty in getting information, and this I accept. However, he agreed that he did have figures which gave an indication as to creditors and trade debtors and was given sales figures and projections for the following six months. His recollection when he gave evidence was that the information which he was given created a picture very much in line with the previous accounts. The company was still making neither a profit nor a loss. However, in the course of his evidence the original copy of the accounts up to October 1974, with which he was supplied, was produced, and from that it could be seen that various figures had been inserted in different colours, presumably at different times. When asked about this, when initially giving evidence, Mr Bufton said that the pencilled figures were ones which he had written before the take-over.

a Against stock appeared in pencil £12,000 in the profit and loss account, though in the balance sheet the figure £15,000 plus or minus also appeared. Looking at the pencil figures, it became reasonably apparent that, when those pencil figures were written, Mr Bufton had tried to recast the accounts working backwards from the information he had, so as to get a correct view of the company's financial position as at the end of May 1975. While doing this, the fact that the company was not breaking even must have become clearly apparent although the figures which were being used were very b approximate and, to a large extent, estimated figures. If the exercise was carried out, then, even though, as Mr Bufton says, he was working on the worst position which could arise, I have no doubt that that is what would have caused him to talk to Mr Marks about stock valuation. It is interesting to note that the note which Mr Bufton prepared in respect of that conversation says against stock 'not up to valuation'. Mr Bufton said that Mr Marks could have told him that he was sure that the stock was valued at cost during c this conversation, but I do not accept that Mr Bufton's recollection is right as to this.

Subsequently, at my invitation, Mr Bufton set out in writing the dates on which he made the various annotations on the accounts. He said that, whereas certain of the entries were before acquisition, others, the critical ones, were made after acquisition. I find that I cannot accept the pencilled figures were made in two stages, some before and some after the take-over. I find that Mr Bufton's first recollection was correct and these d figures were all inserted before acquisition. If part of the figures were inserted at that time, it would only be sensible to insert all the information available since the exercise was purposeless unless as much information was put in as could be put in. I have therefore come to the conclusion that before the acquisition Mr Bufton knew that there was something seriously wrong with the stock valuation. He also had worked out figures which indicated that the company's position could be much less attractive than e was shown by the accounts. This did not mean that Mr Bufton did not rely on the accounts, but it does satisfy me that Mr Bufton was not so concerned about the position of the company as he now believes. He did say, in evidence, something to which I have already alluded, namely, what motivated the plaintiffs to take over the company was the two men, Mr Godridge and Mr Wigg, and it is my conclusion, on the balance of probabilities, that, even if the accounts up to October 1974 had shown the position which f they represented to show, the plaintiffs would have still acted in exactly the same way and taken over the company. The consideration payable for the company was nominal, and it is my view that the plaintiffs would have concluded that BG Fasteners Ltd, under their umbrella, could be made financially successful, as indeed it has ultimately become after a long and painful process. There is no dispute that the plaintiffs were aware that the company had financial difficulties, as it was those financial difficulties which had g brought the two companies together in the first place. Even though the condition of the stock in June 1975 was not necessarily the same as it had been in October 1974, stock in that condition, when contrasted with the valuation placed on it, would have made a director as careful as Mr Bufton unwilling to proceed unless, as I think was the case, he really was prepared to acquire the company if its financial position was that which should have been shown in the accounts at October 1974, if they had shown the true position.

h Accordingly, on this issue, I find in favour of the defendants and conclude that the negligence of the defendants was not causative of any loss which the plaintiffs may have suffered as a result of taking over this company.

At first sight my conclusion on causation may seem inconsistent with my finding that the plaintiffs relied on the accounts. The distinction, as I see it, is that you can be influenced by something even though if you had not been influenced you would have j acted in the same way. The plaintiffs relied on the accounts in deciding to take over BG Fasteners Ltd but they would have acted no differently even if they had known the true position as to the accounts. I therefore reject Mr Bufton's evidence on this issue. In doing so, I do not suggest that he deliberately lied. On the contrary, he gave evidence as to the position as he now believes it to be. His recollection is, however, tainted by how badly things went after the take-over.

Because of my decision on this issue it is not really necessary for me to consider the final two issues. However, in case of an appeal, I will express my views very shortly. a

5. Contributory negligence

The picture which was revealed before the take-over was certainly one which in my view required the plaintiffs to try to make further inquiries if they thought it was critical that the company should be in the position which the accounts purported to indicate. There were however limited steps which they could take and ultimately the best they b could do was to ask for access to more information. This was refused to the plaintiffs and so it does not seem to me that they can be held guilty of contributory negligence. If the position of the company had been important, the plaintiffs would have had to make a choice either to not go on or to go on with the information which was available to them. If I am wrong in taking the view that they were not really concerned with the precise financial position of the company, then the decision to go on is fully c understandable. If I am wrong in my finding, they were still entitled to make the business decision to proceed without being held guilty of contributory negligence.

6. Quantum

With regard to the alleged loss suffered by the plaintiffs, the defendants first of all contended that the proper course for the plaintiffs to have adopted when they realised the d true position of the company was to put it in liquidation and in that way cut down the losses. I do not consider that they can be said to have acted unreasonably or to have failed to mitigate their loss because they did not take such a course. Having decided to see the company through, they were forced to incur expenditure of a substantial nature. Two written schedules of that loss have been put before me which speak for themselves. One is based on the money introduced by the plaintiffs plus interest and notional interest; the e other is based on the losses for the period shown. I regard those schedules as giving an indication of the upper figure for the plaintiffs' loss. From that has to be deducted some allowance for the fact that, if the plaintiffs had not taken over the company, they themselves would have had the expenses of setting up their own operation in the area where the company was carrying on operations. I can only hazard a guess as to what allowance should be made for this. f

Doing the best that I can on the material before me, having taken into account the answers put forward by the defendants, both in argument and in writing, to the plaintiffs' quantification, I have come to the conclusion that an appropriate figure by way of damages if the plaintiffs had succeeded would have been £20,000.

I do not accept the major part of the defendants' criticisms of the plaintiffs' calculations because, in my view, it is not right to look at the position on the basis that this company g had been taken over but its financial position should have been as disclosed by the accounts. The correct initial approach is to calculate the loss on the basis that if the accounts had been correct the plaintiffs would not have acquired the company.

It only remains for me to thank counsel for the very considerable assistance they have given me in this case.

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Judgment for the defendants.

Solicitors: *Taylor & Humbert* (for the plaintiffs); *Hewitt, Woollacott & Chown* (for the defendants).

K Mydeen Esq Barrister.