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# The Boundaries, and Benefits, of 'Gross Negligence' Under Cayman Islands Law

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**For many years, it has been standard industry practice in the Cayman Islands, as in similar jurisdictions, for company directors, corporate service providers, and professional service providers, to apportion risk between themselves, and their client companies, by way of contractual indemnities and limitation of liability clauses.**

Indemnities and limitation of liability clauses are often found in standard terms and conditions of engagement, director's service contracts and in corporate Articles of Association. They are also, less frequently, the product of careful negotiation and drafting between the parties and their lawyers, depending on the nature and value of the transaction in question.

Such clauses usually provide a variety of benefits or protections to the director or service provider, including an exclusion or limitation of liability, an indemnity against loss or liability and provision for payment of the indemnified party's legal fees.

Such clauses are ordinarily subject to exceptions for wilful neglect or default, dishonesty and fraud. Indeed, as a matter of Cayman Islands law, fiduciaries are not ordinarily capable of being indemnified, or excluding liability, for their own wilful neglect or default, dishonesty or fraud, since honesty and good faith have been held to form part of the "*irreducible core of fiduciary obligations*".[1]

There is often scope for debate, however, as to whether or not it is possible, or commercially beneficial and appropriate, for a director or service provider to seek to exclude or limit liability for their own 'gross negligence', and if so, what that concept actually means legally and in practice.

In particular, to what extent does 'gross negligence' overlap with the concepts of 'wilful neglect or default', on the one hand, or simple negligence, on the other?

**The boundaries of 'gross negligence'**

As a matter of English common law, the legal test for wilful default, which is derived from *Re City Equitable Fire Insurance*,[2] provides that an act, or an omission to do an act, is wilful where a person intends to commit a breach of his duty, or is recklessly careless in the sense of simply not caring whether or not his act or omission is or is not a breach of duty. Recklessness is tantamount to dishonesty in this context.

This common law standard has been applied by the Cayman Islands courts in a number of different cases, including *Peterson v Weavering Macro Fixed Income Fund Ltd.*,[3] and *Primeo v Bank of Bermuda and HSBC*.[4]

In *Weavering*, the Cayman Islands Court of Appeal addressed the distinction between 'wilful neglect or default' and 'gross negligence', on the basis that wilful neglect or default requires an element of deliberate wrongdoing, and a conscious decision to act (or to fail to act) in knowing breach of duty: "*negligence, however gross, is not enough*". Put another way, the Court of Appeal described wilful neglect and default as *"the antithesis of negligence [which is] an inadvertent falling short of a duty to take reasonable care."*

In *Primeo v Bank of Bermuda*, the Cayman Islands Court of Appeal separately addressed the distinction between mere negligence and gross negligence. The Court of Appeal followed the guidance of the Privy Council in *Spread Trustee Co. Ltd. v. Hutcheson*,[5] in holding that "*On the plain meaning of the words, and as a matter of logic and common sense, the terms 'negligence' and 'gross negligence' differ only in the degree or seriousness of the want of due care they describe. It is a difference of degree, not of kind…"*

[1] *Renova Resources Private Equity Limited v Gilbertson and Four Others* [2009] CILR 268; *Re Bristol Fund Limited* [2008] CILR 317; *Cesar Hotelco v Ryan* [2012] CILR 164
[2] [1925] Ch. 407
[3] [2015] (1) CILR 45
[4] [2019] (2) CILR 1
[5] [2012] 2 A.C. 194

In a more topical development, the English High Court has considered the test for 'gross negligence', in a very recent decision in the case of Federal Republic of Nigeria v JP Morgan Chase Bank, NA,[6] a case in which a bank is alleged to have negligently failed to detect or prevent a fraud on its customer, in breach of an alleged Quincecare duty of care.

In her decision in that case, published on 14 June 2022, Mrs Justice Cockerill acknowledged that the test of 'gross negligence' is fact sensitive, and a "notoriously slippery concept".

The Court was clear, however, that 'gross negligence' requires something more than simple negligence, on the one hand, even if it does not require dishonesty or bad faith on the other hand. Indeed, the Court acknowledged that 'gross negligence' does not require any subjective mental element equivalent to a conscious appreciation of risk.

The Court and the parties agreed that the leading guidance on the subject was that of Mr Justice Mance in The Hellespont Ardent:[7]

*"'Gross' negligence is clearly intended to represent something more fundamental than failure to exercise proper skill and/or care constituting negligence. But, as a matter of ordinary language and general impression, the concept of gross negligence seems to me capable of embracing not only conduct undertaken with actual appreciation of the risks involved, but also serious disregard of or indifference to an obvious risk."*

In her judgment, Mrs Justice Cockerill held that "even a serious lapse is not likely to be enough to engage the concept of gross negligence". She concluded that the sort of mistakes that might justify a finding of "gross negligence" would be "mistakes which have a very serious and often a shocking or startling (cf. "jaw-dropping") quality to them"; in other words, "mistakes or defaults which are so serious that the word reckless may often come to mind, even if the test for recklessness is not met".

So, in summary, as the law currently stands,[8] "gross negligence" is negligence that is "very serious", "shocking or startling", "jaw-dropping", or virtually tantamount to recklessness (but without the same subjective element).

**The commercial purpose of 'gross negligence'**

Given the proximity, in practice, between 'gross negligence' and recklessness, what useful commercial purpose is to be served by including the concept of 'gross negligence' as an exception to an indemnity or limitation of liability clause?

It seems unlikely, in practice, that the quality of services provided by most directors or service providers changes materially, whether they are held to a 'gross negligence' standard, or a simple negligence standard, having regard to applicable regulatory and professional standards, in any event.

In practical terms, however, one of the main commercial benefits of preserving professional liability for acts of 'gross negligence' is for the purpose of accessing insurance cover under a D&O or professional liability insurance policy, and for promoting consensual resolution (and confidential settlement) of any substantial D&O or E&O liability claim.

Although the wording of every policy will be different, it is generally the case that D&O and professional liability policies exclude insurance coverage for wilful, dishonest and fraudulent acts (even if defence costs may be covered pending an actual finding of dishonesty).

It is often beneficial, therefore, for a claimant to be able to make allegations of 'gross negligence' against directors and service providers, without having to make positive allegations of fraud or dishonesty (which, in turn, can cause substantial reputational and regulatory damage, once those allegations are made public in a Court filing).

It may seem counter-intuitive, therefore, but provided that directors and service providers are appropriately insured for their D&O and E&O liabilities, it is generally beneficial for directors and service providers to seek to reduce the circumstances in which clients, or former clients, might consider it necessary to make allegations of fraud or dishonesty against them in support of any complaint, by agreeing to accept liability for 'gross negligence'.

Experience also suggests that clients are also more receptive to doing business with directors, corporate service providers and professional service providers that are willing to accept contractual liability for their own 'gross negligence', as opposed to seeking to exclude it in all cases.

In this respect, therefore, the "gross" (if not the grass) may actually be greener.

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[6] [2022] EWHC 1447 (Comm)

[7] *Red Sea Tankers Ltd v Papachristidis* [1997] 2 Lloyd's Rep. 547

[8] Mrs. Justice Cockerill refused permission to appeal by a subsequent judgment dated 4 July 2022, but it remains to be seen if the English Court of Appeal separately decides to grant permission to appeal.

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