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Litigation and Dispute Resolution

Review

Contents

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Arbitration

NO SOVEREIGN IMMUNITY FOR UKRAINE AGAINST INVESTMENT TREATY AWARD CREDITOR

PAO Tatneft v Ukraine [2018] EWHC 1797 (Comm), 13 July 2018

Ukraine's recent attempt to resist enforcement of an UNCITRAL award on sovereign immunity grounds has failed. Most importantly, the decision confirms the inherent value in any arbitration agreement
– a State may lose the right to claim immunity, as a basis for resisting enforcement, by agreeing to arbitrate "any dispute" in the underlying Bilateral Investment Treaty.

On 13 July 2018, Butcher J rejected an application by Ukraine based on sovereign immunity arguments to set aside an order made by Teare J *ex parte* in August 2017, which had granted leave to the claimant (**Tatneft**) to enforce an investment treaty award (**Award**) against Ukraine. Butcher J entered judgment against Ukraine for USD112 million, plus interest. In reaching this conclusion, Butcher J considered the interplay between the arbitration exception in s9 State Immunity Act 1978 (**SIA**) and the jurisdiction of the tribunal under the bilateral investment treaty between Russia and Ukraine (**BIT**).

Ukraine is entitled to sovereign immunity unless s9 SIA applies

Butcher J preliminarily explained that Ukraine is entitled, as it had argued, to sovereign immunity pursuant to s1SIA unless an exception applies. The exception in s9 provides that "[w]here a State has agreed in writing" to submit a dispute to arbitration, "the State is not immune as respects proceedings in the courts of the United Kingdom which relate to arbitration".

Tatneft contended that the relevant arbitration agreement for the purposes of s9 stemmed from the dispute provision in the BIT. Butcher J acknowledged that BITs can give rise to an "agreement in writing" between the state and an investor such that s9 is satisfied, since the provision effectively operates as a "unilateral offer" to an investor to arbitrate. This offer is accepted by the investor when it commences arbitration. Moreover, enforcement proceedings – such as in the present case – "relate to arbitration" as required by s9.

Ukraine is not precluded from raising jurisdictional points before the English courts

The crux of Ukraine's sovereign immunity argument was that it "did not agree to submit to arbitration" two of the successful claims that had been determined by the tribunal in the Award. One of these concerned whether Ukraine could be found to have breached the fair and equitable treatment standard (**FET**) in circumstances where there was no express FET provision in the BIT; the other was whether Tatneft had made a valid "investment" under the BIT.

Tatneft argued that Ukraine's 'no agreement to arbitrate' arguments went to whether the tribunal had jurisdiction. As such, these should all have been raised before the arbitral tribunal and, if they were not, Ukraine could not later raise them before the English court. It argued that a State effectively waived the right to raise such new jurisdictional arguments at the enforcement stage. If the contrary were true, Tatneft argued, states could "chop and change" their positions – which was unacceptable given that they would already have participated in a sophisticated arbitral process.

Butcher J disagreed with Tatneft. He emphasised that s1(1) SIA provides that states are immune from the jurisdiction of the court *unless* an SIA exception applies. As such, the court must be satisfied that, in this instance,

the s9 exception applies to remove immunity.
He explained that nothing in the SIA suggested Ukraine is "precluded by what occurred before the Tribunal from raising the points which it has at this hearing". He also stated that the 'chopping and changing' of positions by states was likely overstated.

In light of Butcher J's findings then, it seems that there is scope for states to argue revised or even new jurisdictional objections at the enforcement stage of treaty proceedings, notwithstanding what was presented before the arbitral tribunal.

However, a state's right to claim sovereign immunity will, in many cases, be limited where there is an agreement in writing to arbitrate

Art. 9 of the BIT – the disputes clause – provided that "[a]ny dispute" between a contracting party and an investor of the other contracting party "in connection with investments" shall be referred to a competent court or arbitration.

In respect of Tatneft's successful FET claim, Ukraine argued that as a jurisdictional matter, it had not agreed to the FET standard being incorporated into the BIT; therefore, it had not agreed to a claim of that type being arbitrated (It followed, therefore, that the s9 exception of the SIA didn't apply).

Tatneft argued, however, that the only jurisdictional issue was whether the dispute as to the existence or otherwise of an FET obligation fell within the arbitration agreement. Tatneft submitted it plainly did since it was a "dispute in connection with" a qualifying investment as required by Art. 9 of the BIT (As such, there was an agreement to arbitrate for the purposes of s9 of the SIA).

In Butcher J's view, Tatneft was correct. The FET issue was not a jurisdictional issue, but rather a question of construction of Art. 9 of the BIT. Art. 9, he observed, was drafted in broad terms. Giving proper effect to those terms, Ukraine agreed to arbitrate "any dispute" in connection with the relevant investments, and not particular types of dispute. Butcher J was therefore unwilling to adopt Ukraine's narrow interpretation.

Indeed, he remarked, if Ukraine's position were adopted, then the logical consequence would be that a state could simply say it had not agreed to confer a particular protection on an investor, and therefore that it had not agreed to arbitrate claims alleging a breach of the obligation to provide that protection. Butcher J said such an interpretation would be contrary to the broad intention behind BITs.

COMMENT

The case shows that a state will not be precluded from raising, before an English court, jurisdictional issues not raised before an UNCITRAL arbitration tribunal, and further that the court will carefully consider arguments of sovereign immunity. While this might be considered a second bite of the cherry for a state that has been unsuccessful before an UNCITRAL tribunal, the reality is that it may be difficult for a state to establish it has not submitted in writing to arbitrate a dispute where, as here, the dispute provision is broadly worded (ie an agreement to arbitrate "any dispute").

Although, overall, this case may be construed as a positive development for investors, Tatneft must still execute its award against Ukraine, a process which requires surmounting many more immunity-related hurdles. Ukraine has also reserved its right to raise other grounds against enforcement under s103 Arbitration Act 1996 should its claim for sovereign immunity fail.

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Conflicts of law

ENGLISH COURT'S JURISDICTION OVER ITALIAN SWAPS DISPUTE CONFIRMED

Deutsche Bank AG v Comune di Savona [2018] EWCA Civ 1740, 27 July 2018

The Court of Appeal dismissed an Italian local authority's challenge to the English court's jurisdiction over declarations sought by a bank pursuant to an English law governed swaps contract. In this important decision concerning potentially conflicting jurisdiction clauses, the Court of Appeal provided clear guidance in the face of recent differing approaches at first instance. The decision has therefore brought clarity and welcome market certainty to the interpretation of jurisdiction clauses, particularly when one of them is in an ISDA Master Agreement. Allen & Overy acted for the successful respondent bank.

Deutsche Bank AG (the **Bank**) and Comune di Savona (**Savona**) entered into two interest rate swaps in June 2007 under a 1992 ISDA Master Agreement, Schedule and two swap confirmations (the **Swaps**). The Swaps were governed by English law and contained an exclusive jurisdiction clause in favour of the English courts (the **English Jurisdiction Clause**). Previously, in March 2007, the Bank and Savona had entered into a separate agreement for the Bank to provide certain unpaid assistance with the management of Savona's indebtedness (the **Convention**). The Convention was governed by Italian law and contained an exclusive jurisdiction clause in favour of the Courts of Milan (the **Italian Jurisdiction Clause**).

In light of the threat of potential legal action by Savona in Italy, the Bank issued a protective claim against Savona in the English High Court seeking 12 declarations concerning the entry into, validity, enforceability, interpretation and performance of the Swaps.

Parties disagree on which court has jurisdiction – England or Italy?

Savona acknowledged that half of the declarations fell within the jurisdiction of the English court but challenged the English court's jurisdiction over the other six declarations (even though, with one exception, the declarations closely tracked the wording of contractual representations in the ISDA Master Agreement). After conceding that the declaration tracking the entire agreement clause fell within the English court's jurisdiction, the five declarations challenged by Savona broadly concerned its understanding of the Swaps and the nature and extent of any advice provided by the Bank in relation to Savona's entry into them. Basing its challenge on Article 25 of the Recast Brussels Regulation (which provides that parties may agree to refer disputes in connection with a "particular legal relationship" to the courts of a Member State and that the courts of the contractually agreed Member State will have jurisdiction to hear the dispute), Savona argued that the challenged declarations fell within the scope of the Italian Jurisdiction Clause in the Convention.

At the time of Savona's jurisdiction challenge there were no Italian proceedings on foot. However, shortly before the first instance hearing, Savona commenced proceedings in Milan claiming, among other things, breaches of the Convention based on advice allegedly provided by the Bank concerning the Swaps.

At first instance, HHJ Waksman QC upheld Savona's jurisdiction challenge as, in his view, the Bank's claims in the challenged declarations fell "more naturally" within the Italian Jurisdiction Clause in the Convention. Acknowledging that his decision could lead to fragmentation with some issues to be determined in England and others in Italy, and notwithstanding that most of the declarations mirrored the terms of the

Swaps, it followed from the Judge's finding that the Convention was concerned with the Bank's role as adviser while the Swaps simply concerned the Bank as counterparty.

Court of Appeal

The Court of Appeal overturned the judgment at first instance and returned to the established position that disputes regarding declarations derived from an English law contract with an exclusive jurisdiction clause in favour of the English courts are likely to be determined by the English courts. The Court of Appeal's unanimous decision accordingly provides welcome certainty for contracting parties. In particular, the judgment provides helpful guidance on determining the "particular legal relationship" to which a dispute relates for the purposes of Article 25.

How to determine which 'particular legal relationship' the dispute relates to

Giving the leading judgment, Longmore LJ stated that the correct demarcation between the two relationships was between: (i) the generic relationship set out in the Convention; and (ii) the specific interest rate swap relationship set out in the Swaps.

The Convention made it clear that if a particular transaction was subsequently proposed it would have to be approved by Savona and would be the subject matter of a separate contract. That separate contract (ie the Swaps) would be the "particular legal relationship" relating to the proposed transaction envisaged in Article 25. Longmore LJ held that the existence of an entire agreement clause in the Swaps was strong confirmation of this delineation but that he would have reached the same conclusion without it.

With this approach the Court of Appeal gave the exclusive jurisdiction clauses in each of the Swaps and the Convention a mutually exclusive construction, in line with earlier authority (see *Monde Petroleum v Western Zagroz* [2015] 1 Lloyds Rep. 330).

Declarations raised disputes in relation to the Swaps

Concluding in general terms that disputes relating to the Swaps had to be determined by the English courts, Longmore LJ then considered whether the challenged declarations in fact raised disputes relating to the Swaps.

In all cases it was held that they did: all of the declarations which closely tracked the Swaps' wording "self-evidently" raised a dispute concerning the Swaps and fell within the English Jurisdiction Clause. In relation to the declaration which did not track the wording of the Swaps (a declaration of non-liability), the court concluded that it did no more than make explicit the alleged consequences of the other declarations and therefore also fell within English Jurisdiction Clause.

Noting that all questions of construction will ultimately depend on the terms of the relevant contracts, the Court of Appeal did not expressly approve or disapprove recent first instance jurisdiction decisions in the Italian swaps context, namely *Dexia Crediop SpA v. Provincia Di Brescia* [2016] EWHC 3261 (Comm) and *BNP Paribas SA v Trattamento Rifiuti Metropolitani SpA* [2018] EWHC 1670 (Comm). However, Longmore LJ agreed in principle with the approach of Knowles J in *BNPP v TRM*, which was to focus on whether the English court has jurisdiction rather than to try to predict whether the declarations if made would act as defences in Italy (as the Judge had done at first instance in this case).

Expert evidence in jurisdiction disputes

In their judgments both Lord Justices Longmore and Gross took the opportunity to express unease at the proliferation of expert evidence on foreign law in jurisdiction applications. Although Savona did not obtain permission from the court for its lengthy expert evidence, it was accepted by the Judge at first instance.

However, the Court of Appeal considered that the only relevance of foreign law was to questions of construction of jurisdiction clauses – namely whether there was any difference between the relevant principles under English law and the potentially competing foreign law. They recommended that this point be considered by the Commercial Court Users Committee with a view to expressly stating in the court rules that the court's permission was required to adduce expert evidence in interlocutory applications.

COMMENT

The Court of Appeal's decision marks a return to predictability in the interpretation of potentially competing jurisdiction clauses. In particular, Lord Justice Gross acknowledged the need to preserve market certainty in the ISDA context, stating that it would be "startling" if the bank's claims falling squarely within the terms of the swap contracts could not be brought in the forum expressly chosen by the parties.

Notwithstanding this helpful judgment, the decision is a reminder to parties to ensure there are consistent governing law and jurisdiction clauses across suites of documents if that is intended; if that is not possible or required, explicit reference should be made to the relative scope of any potentially competing jurisdiction clauses.

If a jurisdiction dispute did arise, parties would also be well advised to consider at an early stage whether expert evidence on foreign law is required and to seek permission from the court if it is.

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Contract

CONTRACTING WITH A FOREIGN SOVEREIGN: CAPACITY AND AUTHORITY

Ukraine v The Law Debenture Trust Corporation PLC [2018] EWCA Civ 2026, 14 September 2018

The second round of the legal battle between Russia and Ukraine over repayment of Eurobonds issued by Ukraine has ended with a victory for Ukraine: it can defend Russia's claim for repayment on the grounds it entered into the Eurobond under unlawful duress exerted by Russia. The Court of Appeal unanimously found that foreign sovereign states have unlimited capacity to contract which cannot be constrained by domestic law restrictions (constitutional or otherwise). Any lack of compliance with internal restrictions is properly characterised as a question of authority, rather than capacity counterparties will need to continue to be careful to ensure that they do not, and should not, have known of any lack of authority. The court also refused to imply terms into the Eurobonds on the basis that they were transferable financial instruments.

Ukraine issues USD3 billion Eurobonds

In late 2013, Ukraine was on the verge of signing an Association Agreement with the European Union. It did not ultimately do so: Ukraine contended that Russia applied "massive, unlawful and illegitimate" economic and political pressure to force the Ukraine administration into accepting Russian financial support instead.

The financial support was structured as a standard Eurobond note issue by the State of Ukraine for USD3 billion with Russia as the sole subscriber. The transaction documentation was otherwise as usual for Eurobonds: documents governed by English law, with the Law Debenture Trust Corporation (the **Trustee**) appointed as trustee. The notes were listed on the Irish stock exchange and fully tradeable instruments, although Russia never in fact sold them.

Ukraine defaults on bonds

In early 2014, Russia invaded the Crimea, impeding Ukraine's ability to meet its obligations under the notes due to adverse effects on tax revenues. Following Ukraine's failure to repay the Eurobond at maturity, the Trustee (acting on the direction of Russia) brought

proceedings against Ukraine in England. Ukraine's defence was threefold:

- Capacity and authority: The Eurobond transaction is void because, as a matter of Ukrainian law, Ukraine had no capacity to enter into it due to restrictions in its Constitution and Budget laws, and the Minister of Finance had no authority to sign the agreements and issue the bonds.
- Breach of implied terms: Russia, by invading the Crimea, was in breach of implied terms not to demand repayment if it: (a) deliberately interfered with Ukraine's capacity to repay; or (b) breached its obligations to Ukraine under public international law.
- Duress: Wrongful and illegitimate acts by Russia constitute duress under English law, such that the transaction documents were voidable.

At first instance before Blair J, all of Ukraine's arguments were unsuccessful. Ukraine appealed.

Unlimited capacity of a sovereign state to contract

The Court of Appeal ruled that, despite a lack of compliance with its own domestic law, Ukraine did not lack the capacity to issue the Eurobonds, although the court's reasoning differed from Blair J's.

The Court of Appeal found that a sovereign state derives legal personality, as a matter of English common law, from its recognition as a state by the British government. Its legal personality is *sui generis*: it is neither a person, nor a corporation, but rather a third category, a sovereign state. There is no analogy to be drawn to foreign corporations, whose capacity to contract is determined as a matter of local law.

Capacity flows from legal personality. The consequence of possessing legal personality in English law is that the person can do any of the things for which legal personality is required: owning property, becoming subject to liabilities and entering into contracts. English law imposes no restriction on the capacity of those who have legal personality except as imposed by statute. There is no prerogative or statutory authority for limiting the capacity of a foreign state, and there are no restrictions under common law, so a foreign sovereign state enjoys unlimited capacity as a matter of English law.

Authority to contract: Did the Minister of Finance have authority to bind Ukraine by executing the documents?

The Court of Appeal agreed with Blair J that the Minister did have ostensible authority, although for different reasons.

Actual authority is determined by local law (in this case, Ukrainian law). The parties agreed for summary judgment purpose that the Minister of Finance had no actual authority under Ukrainian law to sign the various agreements and issue the Eurobonds. However, the question of ostensible authority is governed by English law, as the governing law of the agreements. Ostensible authority arises where there has been some direct representation as to the authority of the person acting.

The Court of Appeal agreed that the Minister and cabinet had ostensible authority to issue the Eurobonds. This ostensible authority of the Minister and cabinet (who purported to authorise the Minister) to borrow on behalf of Ukraine was derived from their powers set out in the publicly available Ukrainian legislation.

However, an agent could not have ostensible authority where it conflicted with the express terms of the actual authority granted to the agent, of which the counterparty has notice (that is, in this case, the Ukrainian budget code and constitution). So if the Minister took steps to issue loan notes where it was known (or should have been known) to the Trustee as counterparty that the necessary steps to comply with the Ukrainian budget code (being the document which effectively authorised the Minister) had not been satisfied, the Trustee would have knowledge or notice that the Minister acted beyond his authority, and could not have relied on the Minister's ostensible authority.

The budget legislation was publicly available, and anyone lending to Ukraine was taken to know of its effect, albeit they would have required assistance from local Ukrainian counsel. There was evidence that Ukraine's external borrowings, if aggregated with the Eurobonds, would have exceeded its external borrowing limit for 2013. However, Ukraine could point to nothing

contemporaneous which informed, or could be reasonably taken as informing, the Trustee that the external borrowing limit would be breached by the issue of the Notes. In fact, Ukraine had issued a public statement prior to the Eurobond issue stating that all state debt indicators were within the budgetary limits.

The Court of Appeal concluded that it was impossible to find that the Trustee knew of or should have known, prior to the Eurobond issuance, that Ukraine's external borrowing limit would be exceeded. Ukraine did not therefore have an arguable defence that the Minister and cabinet lacked ostensible authority to issue the notes.

Unusual/suspicious circumstances

The Court said that a third party (in this case, the Trustee) cannot rely on ostensible authority if the terms of the transaction are unusual, or there are suspicious circumstances or abnormalities. The third party should make reasonable enquiries to ensure the agent's authority is sufficient to bind the principal. In this case, there were no terms that self-evidently stood out as abnormal.

Cabinet had no actual authority to make representation as to Minister's authority

The Court of Appeal disagreed with Blair J's supplementary finding that the Ukrainian Cabinet had usual authority to hold out the Minister of Finance as Ukraine's authorised representative in the transaction, such that the Minister also had ostensible authority to enter into it. This is because the person who holds out another as agent (so as to bestow them with ostensible authority) must have actual authority to do so on behalf of the principle, or ostensible authority derived from someone with actual authority.

No implied terms in transferable financial instruments

The Court of Appeal agreed that terms could not be implied into the Eurobonds. Although courts have been willing to imply terms that one party would not seek to prevent a counterparty's performance of a contract (as the Crimea invasion may be said to have done), there is no general rule that such a term will be implied, and it will depend on the relevant contract, particularly its express terms.

The implied terms contended for by Ukraine were not necessary in the context of the overall transaction and its express terms. They were not necessary for the operation of the agreement, which otherwise functioned clearly, they were not so obvious as to go without saying (particularly to subsequent purchasers of the Eurobond), and were not capable of clear expression.

Most importantly, the structure of Ukraine's debt obligation took the form of a tradeable financial instrument listed on the Irish stock exchange. This gave rise to strong arguments against the implication of terms:

- Any implied term would need to be derived from the contractual documentation available to subsequent holders of the Eurobonds (not just the initial subscriber). It could not be derived from the background or matrix of facts in which the initial subscriber had purchased the Eurobonds, in particular the state of Russia/Ukraine relations at the time of initial issuance.
- Although the initial subscriber, Russia, was not a counterparty to the relevant contractual documentation, it was contrary to principle and common sense to imply terms relevant to the relationship between Russia and Ukraine into a contract between Ukraine and the Trustee.
- The implication of Ukraine's suggested terms would effectively render the Eurobond unworkable and untradeable and therefore conflict with their express terms, as it would mean that future purchasers of the Eurobonds would have to agree to accept that Ukraine's payment obligations were contingent on the conduct of Russia *vis-à-vis* Ukraine. This was incompatible with the commercial purpose of the agreements.

Duress applied by a foreign state

The Court of Appeal found that the defence of duress was available to Ukraine. Unlike the trial judge, the Court of Appeal concluded that although the acts allegedly constituting the duress were foreign acts of state involving violations of norms of international law,

they were justiciable before an English court as a matter of public policy. This was because the loan relationship between the parties had been structured in the form of a Eurobond, governed by English law with choice of English court as the forum. Russia therefore accepted the risk that an English court would apply the English law of duress.

As such, overall, Ukraine succeeded on its appeal. The claim will proceed to trial on the issue of duress although the Trustee was granted leave to appeal to the Supreme Court.

Implications for dealings with sovereigns

The unanimous Court of Appeal support for the conclusions (if not the reasoning) of the trial judge on sovereign capacity and authority provides welcome clarity given the lack of prior case law on this topic. It confirms that a foreign state recognised in the UK has unlimited capacity to contract as a matter of English law, irrespective of any foreign domestic law provisions to the contrary. Consideration of questions of capacity remain important in the context of assessing the commercial risk of a transaction, particularly in emerging markets.

Given a foreign sovereign's status as a *sui generis* creature, it should be noted that the ruling does not change the position on capacity of a foreign public body (rather than the state itself): it will remain the law of the jurisdiction of the public body which determines capacity.

Instead, any restrictions on a foreign state's ability to contract under domestic law go to the question of whether those purporting to bind the state had authority to do so. Even if there is clearly no express actual authority under local law, there may still be ostensible authority established as a matter of English law where transaction documents are governed by English law.

Parties contracting with states must carefully consider the authority of the individual (or individuals) purporting to bind the state before transacting. The Court of Appeal was clearly of the view that a state representative's ostensible authority could be defeated in circumstances where a counterparty knew, or should have known, that the representative lacked authority to bind the state (including by acting in breach of relevant publicly available domestic legislation). Obtaining robust legal opinions as to authority will therefore remain the best protection for counterparties hoping to satisfy themselves of the enforceability of their transactions.

Finally, the court was firmly against implying terms into transferable financial instruments. Its reasoning resonates beyond Eurobonds into a wider field of instruments, and it is reassuring to see the regard given to the position of potential subsequent investors in such products.

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NO OBLIGATION IMPOSED BY USE OF "SHALL" IN COMMERCIAL REFERRAL AGREEMENT

PM Law Ltd v Motorplus Ltd [2018] EWCA CIV 1730, 26 July 2018

Commercial parties often use the word "shall" to impose a contractual obligation. This Court of Appeal decision is an illustration of how the surrounding circumstances, including prior dealings, can mean that "shall" is merely an expression of the parties' intention at the time of contracting.

In 2006 a law firm (**PML**) and an insurance intermediary (**Motorplus**) entered into an agreement recorded in an email (the **2006 Agreement**) in which Motorplus agreed to refer road traffic accident claims to PML. The email stated: "*We intend to send approx.. 100 claims a month*". PML and Motorplus then entered

into a written contract (the **2007 Agreement**) which stated at clause 1:

"*In consideration of the payment of referral fees by PM Law Ltd Solicitors…Motorplus Ltd shall refer a quantity of road traffic accident, accident at work, public or private liability and product liability PI & Non PI claims for compensation*".

A dispute arose concerning the meaning and effect of clause 1. Motorplus argued that the 2007 Agreement did not impose an obligation on it to refer any claims to PML. PML argued that Motorplus was in fact obliged to refer some claims to PML, and that in return PML would handle the claims and pay a referral fee.

The Court of Appeal concluded that despite the use of the word "shall" in clause 1, the agreement did not oblige Motorplus to refer claims to PML. "Shall", in light of the 2007 Agreement as a whole and the relevant factual matrix, was interpreted as an expression of the parties' present intention rather than a promise or obligation. The court relied on the fact that clause 1 did not refer to a specific or minimum number of claims. The court rejected the argument that "business common sense" required clause 1 to be read as requiring a "reasonable" quantity of claims to be referred. It endorsed the reasoning of the judge, who pointed out that the business efficacy of the agreement did not depend on there being a minimum number of referrals. The possibility that the other party would fail to deliver any referrals was a risk which businesses often took. The court considered the fact that the pricing structure in the 2007 Agreement dealt with referrals on an individual basis rather than setting a price for a bulk amount, or minimum amount, of referrals. This was more consistent, said the court, with a unilateral contract (where PML would pay a referral fee **if** Motorplus referred a claim) rather than a bilateral exchange of obligations (referred to by the court as a "synallagmatic contract").

The court was also persuaded by the fact that the parties' 2006 Agreement by email had not required Motorplus to guarantee a minimum number of referrals. The intention of the parties was to place the 2006 Agreement on a more formal footing in order to comply with the then new Solicitors' Code of Conduct of 2007. This pointed against construing clause 1 in a manner which would require Motorplus to refer a minimum quantity of claims to PML.

COMMENT

"Shall" is, potentially, an ambiguous term which is capable of: (i) expressing a future intention; and (ii) expressing an obligation. The court decided, in this case, that that the former was the preferred interpretation by using the "documentary, factual and commercial context" of the parties' agreement to construe the word.

The case arrives at a time when the courts are tasked with balancing the natural meaning of language used between the parties (emphasised by the Supreme Court in *Arnold v Britton* [2015] UKSC 36) with a construction that aligns with "business common sense" (as per the guidance set out in *Rainy Sky*). The implication of the Supreme Court decision in *Wood v Capita Insurance Services Ltd* [2017] UKSC 24 is that these are not to be seen as rival approaches to interpretation, but considerations to be balanced. The Court in *PML v Motorplus* expressly stated that where the language used is clear, it cannot "*seek out differences of meaning in order to enable it to re-write the bargain in accordance with what it considers to be fair or to be business common sense*". It did, however, consider whether interpreting clause 1 of the 2007 Agreement as an obligation to refer a minimum number of claims was necessary for the arrangement to make commercial sense (the answer was no).

Following *Wood v Capita*, we can expect the courts to continue to balance an interpretation which is faithful to the natural meaning of the words used by the parties whilst not offending business common sense. Clearly drafted contracts will largely avoid having to predict the outcome of this balancing act.

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Crime

ENRC V SFO APPEAL: INTERNAL CORPORATE INVESTIGATION DOCUMENTS WERE PROTECTED BY PRIVILEGE

SFO v ENRC [2018] EWCA Civ 2006, 5 September 2018

Documents, including interview notes, generated by mining company ENRC during an internal corruption investigation were protected by privilege and therefore did not have to be disclosed to the Serious Fraud Office (**SFO)**. This unanimous Court of Appeal decision overturns the controversial High Court ruling last year which threw into question how businesses could investigate possible wrongdoing without creating material, including potentially incriminating documents, that would have to be handed over to investigators. The decision will be welcomed by businesses and their lawyers as it increases the likelihood of a successful claim to litigation privilege in England when entities are facing the prospect of a criminal prosecution or regulatory enforcement action. The Court also expressed helpful, but non-binding, views on the question of who is the "client" for the purposes of legal advice privilege – ie which individuals within a corporation can communicate with the corporation's lawyers on a privileged basis. The SFO has announced that it will not be appealing to the Supreme Court.

ENRC conducts internal investigation

In December 2010, ENRC received an email from an apparent whistleblower containing allegations of bribery and financial wrongdoing in relation to its Kazakh subsidiary. This led ENRC to instruct lawyers and to carry out an internal fact-finding investigation. In April 2011, following press reports suggesting that the SFO had been asked to investigate ENRC on the matter, forensic accountants were also instructed.

In August 2011, the SFO became directly involved. It contacted ENRC, drew its attention to the SFO's self-reporting guidelines and suggested a meeting. There followed a lengthy period of dialogue between ENRC and the SFO, including a series of meetings in which ENRC updated the SFO on the progress of its internal investigation.

SFO starts criminal investigation of ENRC and demands documents

The SFO formally commenced a criminal investigation in April 2013 and compelled ENRC to produce a range of documents including:

(1) notes taken by lawyers of the evidence given to them by ENRC's employees, former employees, subsidiaries, suppliers and other third parties; and

(2) materials generated by forensic accountants, as part of a "books and records" review, with a focus on identifying controls and systems weaknesses and potential improvements (together, the **Documents**).

The SFO cannot compel the production of documents which a corporation would be entitled to refuse to disclose on grounds of legal privilege in proceedings in the English court. ENRC claimed the Documents were privileged and refused to produce them. The SFO then commenced these proceedings disputing that claim and seeking production of the Documents.

Court of Appeal rules that litigation privilege applies

Litigation privilege applies to communications between clients or their lawyers and third parties for the purpose of obtaining information or advice in connection with existing or contemplated litigation when, at the time of the communication in question:

(1) litigation is in progress or reasonably in contemplation;

(2) the communications are made with the sole or dominant purpose of conducting that litigation or anticipated litigation; and

(3) the litigation is adversarial, not investigative or inquisitorial.

At first instance, Andrews J denied a claim for litigation privilege for the Documents. This was on the basis that:

(1) ENRC needed to have a criminal prosecution in contemplation at the time the Documents were created and, on the facts, Andrews J concluded that ENRC did not contemplate criminal prosecution at that time;

(2) even if a prosecution had been reasonably in contemplation, none of the documents had been created with the dominant purpose of being used in such litigation; and

(3) litigation privilege does not extend to documents created in order to obtain legal advice as to how to best avoid contemplated litigation, or a future regulatory or criminal investigation.

The Court of Appeal unanimously disagreed with these conclusions and upheld ENRC's claim that the Documents were protected by litigation privilege.

Criminal proceedings against ENRC were reasonably in contemplation

The Court held that a criminal prosecution was reasonably in contemplation when ENRC initiated its investigation and was certainly in contemplation from when ENRC was contacted by the SFO.

Ultimately, this was a question of fact (and the Court noted that it was not sure that "*every SFO manifestation of concern would properly be regarded as adversarial litigation*"). However, the Court stated that, when the SFO specifically makes the prospect of its criminal prosecution clear to a corporation (over and above the general principles set out in the SFO's Guidelines), and legal advisers are engaged to deal with that situation, there was "*clear ground*" to contend that a criminal prosecution was in reasonable contemplation. This was the case for ENRC.

Indeed, the Court held that "*the whole sub-text of the relationship between ENRC and the SFO was the possibility, if not the likelihood, of prosecution if the self-reporting process did not result in a civil settlement*".

The Court diverged from the views of Andrews J on some important points of general principle, finding that:

(1) whilst a party anticipating possible prosecution will often need to make further investigations before it can say with certainty that proceedings are likely, that uncertainty does not of itself prevent proceedings being in reasonable contemplation;

(2) Andrews J was wrong that litigation privilege cannot attach until either: (a) the defendant knows the full details of what is likely to be unearthed; or (b) a decision to prosecute has been taken; and

(3) the fact that a formal criminal investigation has not yet been commenced will be a part of the factual matrix when determining whether litigation is reasonably in contemplation, but it will not necessarily be determinative.

Documents were generated by ENRC for the dominant purpose of resisting or avoiding criminal proceedings

At first instance, Andrews J concluded that ENRC's dominant purpose was to investigate the facts to see what had happened and deal with compliance and governance, rather than defend contemplated criminal proceedings. Andrews J also concluded that there was overwhelming evidence that the interview notes were created for the specific purpose of being shown to the SFO.

The Court disagreed, taking a more pragmatic approach. The Court found that:

(1) the fact that solicitors prepare a document with the ultimate intention of showing it to the other side (which, in any event, the Court found was not supported by the evidence in this case) does not automatically deprive the preparatory legal work of litigation privilege;

(2) legal advice given to head off, avoid or even settle reasonably contemplated legal proceedings remains protected by litigation privilege as much as advice on defending or contesting such proceedings would be; and

(3) whilst reputable corporations will certainly want to ensure high ethical standards for their own sake in their business, realistically, the legal sanction used to enforce appropriate standards in business is the criminal or civil law. As such, where a corporation is facing a clear threat of criminal investigation and prosecution, the reason the corporation is investigating whistleblowing allegations must be "brought into the zone" where the dominant purpose is to prevent or deal with litigation.

In addition, the Court found on the facts that, whilst ENRC had indicated to the SFO it would make "*full and frank disclosure*", it did not in fact do so and it had never gone so far as to agree to disclose all of the materials it created in the course of its investigation to the SFO.

The Court noted that, had it been asked to approve a deferred prosecution agreement between ENRC and the SFO, ENRC's failure to make good on its promises to be full and frank would undoubtedly have counted against it. However, the Court was clear that this would not affect whether the Documents were covered by litigation privilege in the first place.

The Court found that the Documents were brought into existence for the dominant purpose of resisting or avoiding proceedings and so were protected by litigation privilege.

Legal advice privilege – *Three Rivers 5* criticised

Legal advice privilege attaches to confidential communications between a client and its lawyers, acting in their professional capacity, in connection with the provision of legal advice.

The Court declined to determine whether the Documents were protected by legal advice privilege, in part because there was no need to do so, given its conclusions on litigation privilege, and in part because the Court took the view that in light of previous Court of Appeal authority in *Three Rivers 5*, any change to the test for legal advice privilege would have to be determined by the Supreme Court.

However, the Court did express a non-binding view on how it would have decided the matter if it could have done so. The Court said that:

(1) *Three Rivers 5* decided that communications between an employee of a corporation and the corporation's lawyers could not attract legal advice privilege unless that employee was tasked with seeking and receiving such advice on behalf of the client; and

(2) it would have departed from *Three Rivers 5* if it had the choice.

In particular, the Court noted that in the modern world, the law needs to cater for legal advice sought by large national and multi-national corporations. It recognised that, where small corporations are concerned, the relevant information will normally be held by members of the corporation's board (who will almost always be authorised to seek and receive legal advice on the corporation's behalf), whereas this is less likely to be the case for multi-nationals. The Court's view was that, if "*a multi-national corporation cannot ask its lawyers to obtain the information it needs to advise that corporation from the corporation's employees with relevant first-hand knowledge under the protection of legal advice privilege, that corporation will be in a less advantageous position than a smaller entity seeking such advice*." The Court said that, whatever the rule is, it should be equally applicable to all clients, whatever their size or reach.

The Court also noted that English law was out of step with the common law in other jurisdictions on this question, referring specifically to decisions of the Singapore and Hong Kong Courts of Appeal. The Court said that it was "*undoubtedly desirable*" for the common law to remain aligned in different countries where its development was not specifically affected by different commercial or cultural environments. In the Court's view, "*legal professional privilege is a classic example of an area where one might expect to see commonality between the laws of common law countries, particularly when so many multinational companies operate across*

borders and have subsidiaries in numerous common law countries".

As the Court felt unable to depart from *Three Rivers 5*, it concluded, however, that Andrews J was right in deciding that legal advice privilege did not apply.

Impact of *ENRC v SFO* Court of Appeal ruling

Lower bar for reasonable contemplation of criminal prosecution

Decisions of the English court which narrowed the scope of legal professional privilege available to businesses involved in regulatory and criminal investigations had become the unfortunate norm. That trend is now starting to reverse.

The decision is positive news for those facing criminal or regulatory investigation and strikes a sensible balance on when litigation privilege should be available in those circumstances. The Court recognised a clear public interest in encouraging companies to investigate allegations from whistleblowers or investigative journalists under the protection of legal professional privilege before approaching the authorities: otherwise, companies might be tempted not to investigate such allegations at all.

Businesses are now in a position where, on the right facts, they can make a successful claim for litigation privilege at a much earlier stage than the first instance judgment suggested, and therefore obtain the benefit of protection for communications with third parties including external expert advisers and employees (or ex-employees) who are not specifically tasked with seeking legal advice. The impact resonates beyond criminal proceedings: the Court's conclusions are relevant to internal investigations in anticipation of regulatory action by bodies such as the Financial Conduct Authority, Competition and Markets Authority or HMRC.

Businesses will still need to demonstrate, on the facts of each case, that civil litigation or criminal prosecution (or its equivalent) is reasonably in contemplation. But the fact that a corporation has not yet comprehensively established whether there is truth in claims of wrongdoing is no longer a bar to litigation being reasonably in contemplation.

Although the Court's conclusions of fact are specific to this case, they indicate the factors that might help in demonstrating a reasonable contemplation of adversarial litigation. The Court said that it was "not sure" that adversarial litigation would automatically be in contemplation whenever an entity is contacted by the SFO and noted that where an SFO investigation is reasonably in contemplation, it is not inevitable that an SFO prosecution can also be said to be reasonably in contemplation.

Here, however, ENRC was able to provide contemporaneous documents and witness evidence that the Court found pointed clearly towards contemplation of a criminal prosecution if the self-reporting process was not successful in heading it off. Being able to point to examples of similar evidence will be helpful in future cases when seeking to establish a claim to litigation privilege. Factors which the Court considered relevant included:

(1) ENRC's receipt of a whistleblower email and subsequent appointment of external lawyers to investigate the allegations;

(2) contemporaneous views of both ENRC's general counsel and head of compliance (expressed by email) that they expected an SFO investigation, and actions taken within the company which were consistent with this view (eg upgrading its dawn raid procedures);

(3) contemporaneous views of the firm's lawyers that privilege would attach to the documents and that litigation was reasonably in contemplation; and

(4) the fact that, when the SFO wrote to ENRC, it asked ENRC to consider the self-reporting guidelines carefully, which included express statements that "*no prosecutor can ever give an unconditional guarantee that there will not be a prosecution*", and the SFO's expression of similar views in later meetings.

One other practical consequence of the decision is that the SFO (and regulators) will have to confront the

question of how they will deal with privileged documents involuntarily produced under statutory compulsion based on the (now overturned) first instance decision. It also remains to be seen whether the SFO will modify the content of its communications with targets of new investigations in response to this decision.

Three Rivers 5 still with us for now

Parties will also have to consider whether the Court of Appeal's non-binding comments disagreeing with *Three Rivers 5* should affect their approach in relation to legal advice privilege, including on the key issue of whether notes of interviews with employees are disclosable when created in circumstances which do not attract litigation privilege. The Court's decision provides a strong indication that it believes *Three Rivers 5* should be overturned, but a party may need to be willing to take that issue to the Supreme Court for resolution.

The SFO has announced that it will not be appealing to the Supreme Court.

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SFO CAN REQUEST OVERSEAS DOCUMENTS FROM NON-UK COMPANIES

The Queen on the application of KBR Inc v The Director of the Serious Fraud Office [2018] EWHC 2368 (Admin), 6 September 2018

The Serious Fraud Office can validly issue a section 2 notice with extraterritorial application. It can compel production of documents held extraterritorially by a UK company, or issue a notice to foreign companies in respect of documents held outside the UK if there is a "sufficient connection" between that company and the UK. The ruling comes at a time when the SFO is testing the limits of its powers to seek disclosure of documents. Although unsuccessful in *SFO v ENRC* when contesting the ambit of legal professional privilege, the SFO will be pleased with the outcome of this ruling on its extraterritorial reach.

The SFO can issue a notice requiring a person or entity under investigation or any other person to produce documents which appear to the SFO to relate to any matter relevant to the investigation.[1] These are commonly called "section 2 notices". Failure to comply with a section 2 notice without reasonable excuse is a criminal offence.

The territorial scope of this power has been unclear: does it extend to documents held by UK companies overseas (including on an overseas server)? Does the SFO have power to issue a section 2 notice to a foreign corporation that has no business presence in the UK?

These questions were answered in this case dealing with the validity of section 2 notices issued to:

- **an English company**: *Kellogg Brown & Root Ltd* (**KBR Ltd**): KBR Ltd carried out business in the UK. In February 2017, the SFO commenced a criminal investigation into KBR Ltd for suspected offences of bribery and corruption relating to the Unaoil scandal; and
- **the U.S. parent company**: *KBR Inc*: the ultimate parent of a multinational group, including KBR Ltd, providing professional services and technologies. KBR Inc had no fixed place of business in the UK and did not independently carry on business in the UK; it only did so through its UK subsidiaries. KBR Inc was under investigation by the U.S. Department of Justice and Securities and Exchange Commission for its dealings with Unaoil.

SFO seeks documents held both in and outside the UK

The SFO issued a section 2 notice to KBR Ltd in April 2017. Initially, the KBR Group expressed an intention to cooperate expansively in its response. It provided: (i) UK-based responsive documents already under KBR Ltd's custody and control; (ii) documents located outside the UK and sent to KBR Ltd at KBR Inc's direction; and (iii) purely on a voluntary basis, documents which KBR Inc had previously disclosed to the DOJ and SEC.

However, the SFO became concerned that the KBR Group was drawing an inappropriate distinction between documents held by or under the control of KBR Ltd, and documents held outside the UK and beyond the control of KBR Ltd. It therefore issued a further, largely duplicative, section 2 notice in July 2017 (the **July Notice**) addressed directly to the U.S. entity, KBR Inc.

The U.S. entity, KBR Inc, challenged the lawfulness of the notice and refused to produce documents in response to it on the grounds that:

- the July Notice was *ultra vires* as it requested material held outside the UK from a foreign-incorporated company;
- it was an error of law for the SFO to exercise section 2 powers despite the power to seek Mutual Legal Assistance (**MLA**) from the U.S. authorities; and
- the July Notice had not been effectively served on KBR Inc when it was handed to an officer of KBR

Inc who had temporarily been present in the UK in order to, at the request of the SFO, attend a meeting with the SFO.

The court rejected all of these arguments and upheld the validity of the notice.

Section 2 notice capable of extending to documents held overseas by UK companies

There is a general principle that, absent contrary intention, statutes have only territorial (not extraterritorial) application: ie they are restricted in operation to the UK.

However, the court concluded that section 2 notices issued to UK companies had to have at least some extraterritorial reach. This was because it was "scarcely credible" that a UK-based company could refuse to provide documents solely because the documents were contained on a server abroad, as this would mean that a company could thwart an investigation by moving documents overseas. While section 2 had been drafted pre-internet, and had to be construed accordingly, the underlying policy behind section 2 was to prevent the "determination and ingenuity" of persons trying to obstruct investigations. Even in a pre-internet age, this would have required section 2 notices served on UK companies to have extraterritorial application.

Section 2 notice capable of extending to non-UK companies in respect of documents held outside the UK

There was no express statutory limitation on who could be a potential recipient of a section 2 notice. The court concluded that section 2 was directed at facilitating the investigation and prosecution of top end fraud, which by its nature would have an international dimension. While the international spread of documents has been amplified by technological developments since 1987, the court did not consider that an international dimension to such investigations was "unknown or not appreciated" when the Criminal Justice Act 1987 was drafted. Excluding any consideration of MLA, the court saw a "very real risk" that the section 2 power would be frustrated if the SFO was unable to seek documents located abroad from a foreign company. The court recognised the strong public interest in section 2 having an extraterritorial ambit, and concluded that section 2 notices could be validly issued to non-UK companies for documents held both in and outside of the UK.

Section 2 notice issued to non-UK company – must be a "sufficient connection" with the UK

The court applied a new limitation - a section 2 notice can only validly be given to a non-UK company in respect of documents held outside the UK where there is a "sufficient connection" between the company and the UK.

The court found a sufficient connection between KBR Inc and the UK for the July Notice to be valid. This was because the SFO's investigation focused on a large number of suspected corrupt payments made by KBR Inc's UK subsidiaries to Unaoil. The SFO had formed the view that those payments had required express approval by KBR Inc's U.S.-based compliance function and were processed by KBR Inc's U.S.-based treasury function. Further support arose from the fact that a corporate officer of KBR Inc was based in the group's UK office and appeared to carry out his functions from the UK.

The following factors, said the court, would not, without more, amount to a "sufficient connection" between a non-UK company and the UK:

- the non-UK company is the parent company of a company under UK investigation;
- the non-UK parent company cooperates to a degree with the SFO's request for documents and remains willing to do so voluntarily; or
- a senior officer of the non-UK parent company attends an in-person meeting with the SFO.

Mutual Legal Assistance (MLA) regime curtailed?

The court found that the MLA regime provides an additional, alternative route to obtain documents for the SFO: but its availability does not affect the lawfulness of the SFO's decision to issue a section 2 notice to a non-UK company with sufficient connection to the UK. Even when there is an available MLA regime, there may be good practical reasons for the SFO to proceed with a section 2 notice (as it had in this case). The SFO has

recently used the MLA regime to try to obtain documents in Monaco.

How is a section 2 notice served on a non-UK company?

A section 2 notice should be given to a person within the jurisdiction: there is no additional formality or traditional "service" required beyond the giving of the notice.

In this case, the July Notice was handed to an officer of KBR Inc voluntarily attending a meeting in the UK with the SFO, at the SFO's request. The officer was present in the UK for the purpose of representing KBR Inc, which was sufficient to establish KBR Inc was present in the jurisdiction at the time it (through its officer) was given the July Notice. Whilst the court found it unappealing that the SFO insisted on a KBR Inc representative attending the meeting with the intention to serve the July Notice, this did not affect its validity.

Safeguards/defences

The court pointed to statutory "safeguards" in place in the CJA: the SFO must decide whether to exercise the power to issue a section 2 notice, the issue of such a notice is subject to judicial review and a person may rely on a statutory defence of reasonable excuse if they do not comply. However, it is unclear what the practical value of these safeguards and defences would be to a foreign company facing a potential fishing expedition. The English court has traditionally been reluctant to interfere, by way of judicial review, with the SFO's decision-making powers, for example the 2016 failed attempt, via judicial review, by Soma Oil to stop an SFO investigation.

Comment

While the court was careful to note that it was not engaging in "impermissible judicial legislation", it is difficult to conclude that the decision involves anything else. The CJA imposes criminal penalties for failure to comply with a section 2 notice, which would not usually align with an extraterritorial reach without specific extraterritorial statutory provision (as in, for example, the Bribery Act 2010).

There is no suggestion in the CJA of the "sufficient connection" test, and in other similar contexts (for example, the Proceeds of Crime Act 2002), the Supreme Court has limited disclosure orders to having jurisdictional reach only. While similar tests have been generated in the insolvency context, the statutory safeguards surrounding exercise of such powers are quite different to those involved in questioning the SFO's power to issue a section 2 notice, which are limited to very narrow grounds.

The "sufficient connection" test for when a non-UK company may be issued with a section 2 notice involves considering the factual connection of the company to the UK, not in terms of (as might be expected) the strength of the business connections to the UK or storage of documents here, but rather its connection to the subject matter of the SFO's investigation (in this case, it was the U.S. company's role in the UK company making improper payments). As such, it is unclear what can be done by a non-UK company to insulate itself from the reach of a section 2 notice, barring avoiding receipt of such a notice by refraining from its officers entering the UK.

The court did not consider the practicalities of a non-UK company complying with a request for documents. For example, there was no discussion regarding data protection or other overseas laws or arrangements which may restrict a company's ability to comply, and the invidious position a non-UK company may then be put in of facing competing criminal or civil liability (a difficulty which may be overcome through appropriate use of the protections built into the MLA regimes). The practical ability of the SFO to enforce such a notice against a non-UK company without any UK presence may also be called into question, in particular where a foreign company may face domestic blocking statutes or other compelling local law prohibitions against compliance with a UK section 2 notice.

A strong pointer that the legislature itself views the SFO's section 2 power as not being intended for extraterritorial use is the proposed introduction of a new UK law that will allow law enforcement agencies (including the SFO) to apply for a UK court order to get stored electronic data directly from a company or person

based outside the UK. The Crime (Overseas Production Orders) Bill 2018 contains specific safeguards surrounding the extraterritorial use of production powers. The need for additional UK legislation governing extraterritorial production orders is consistent with the international approach taken in such cases. The Microsoft case in the U.S. (in which the U.S. government sought to compel Microsoft to disclose information stored on servers abroad) was based on unclear drafting in the U.S. Stored Communications Act. To clarify this ambiguity, the U.S. Clarifying Lawful Overseas Use of Data Act (the **CLOUD Act**) was passed. The CLOUD Act amends the SCA expressly to require a provider to provide data within its "possession, custody, or control, regardless of whether [such data] is located within or outside the United States".

While the Court did not consider that extending the jurisdiction of the SFO to issue section 2 notices extraterritorially would "raise eyebrows" in this case, it certainly does raise questions about international co-operation and comity, and (if the decision stands) the on-going use of MLA procedures by the SFO in the UK.

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[1] Section 2 Criminal Justice Act 1987.

Privilege

FINANCIAL REPORTING COUNCIL GRANTED ACCESS TO PRIVILEGED DOCUMENTS OF AUDITOR'S CLIENT

FRC v Sports Direct International Plc [2018] EWHC 2284 (Ch), 11 September 2018

The Financial Reporting Council (**FRC**), the regulatory body for accountants, auditors and actuaries in the UK, was allowed access to privileged material of a client of an auditor under investigation. Although the decision is subject to an appeal, at present companies may feel rightly concerned about losing control over their privileged documents by being forced to provide them to the regulator of one of their professional advisers.

Since 2016 the FRC has been investigating Grant Thornton in relation to its audit of the financial statements of Sports Direct International (**Sports Direct**). As part of its investigation, the FRC issued several statutory notices to Sports Direct. The FRC sought material Sports Direct had already provided to Grant Thornton during the course of its audit, as well as additional material that remained in the hands of Sports Direct but related to Grant Thornton. Sports Direct claimed privilege over some of this material and refused to produce it. The FRC applied to the court to compel production.

Client's privileged material disclosed to audit regulator does not infringe the privilege

The FRC submitted that disclosure by Sports Direct of its privileged material to the FRC, for the purpose of the FRC investigation of Grant Thornton's audit of Sports Direct, did not infringe Sports Direct's privilege. This was principally because the disclosure to the regulator did not result in that material being made publicly available. It was also not sought for the purpose of or used in such a way as to be relied upon against Sports Direct.

The FRC went on to suggest that if there was an infringement, it was only a "technical" one – and thus permissible. It was technical in that while the privilege may have been infringed, such infringement was not prejudicial to the client in any way (as it was only being sought for the purposes of the FRC's investigation into Grant Thornton). The FRC argued that the statutory powers pursuant to which it had requested the material impliedly authorised a technical infringement of this nature.

Arnold J agreed with the FRC, finding that the same was true irrespective of whether the documents were held by an auditor or its client. Despite acknowledging he was not entirely comfortable with the conclusion reached in this case, Arnold J was nonetheless bound by an earlier House of Lords decision.[1]

No limited waiver by client relating to audit investigation

The FRC argued any privileged material Sports Direct had already provided to Grant Thornton in the course of its audit should also be provided to the FRC. In addition to the "no infringement" argument above, the FRC argued in the alternative that Sports Direct had impliedly granted a selective and limited waiver of privilege over the material it had already provided to Grant Thornton. The FRC argued that it was entitled to the privileged material on the basis that the waiver necessarily extended to the FRC for the purposes of regulating the auditor's conduct in respect of the same material in other words that regulatory oversight is a necessary extension of the audit function. Sports Direct submitted that this waiver did not extend beyond Grant Thornton, or beyond its use by Grant Thornton for the purposes of the audit.

Arnold J held that the FRC was not entitled to the privileged material merely because it had already been shared with Grant Thornton, over which the FRC had regulatory supervision. It was incorrect to suggest that the regulatory process and the audit process were part of a single continuum.

Attaching material to a privileged communication does not make it privileged

Sports Direct asserted privilege over certain material attached to emails between Sports Direct and its lawyers (which had been provided by Sports Direct to Grant Thornton). An example was a contract between a subsidiary of Sports Direct and a third party.

Arnold J confirmed that privilege does not extend to any material that was not privileged *per se* but that had been attached to privileged communications. Using the example of press cuttings[2] attached to a lawyer's email, Arnold J observed that a client who asks its lawyer for relevant press cuttings because it is convenient is not asking for legal advice. The act by the lawyer of attaching them to an email to its client does not convert what are pre-existing, non-privileged press cuttings to privileged ones.

COMMENTS

Companies may face increased disclosure requests for privileged material from the FRC as a result of this ruling, although it is being appealed. Such disclosure requests may cover both material already provided to auditors during the course of an audit as well as additional material not provided to the auditor but relating to it. Although the disclosure is limited to circumstances where the accountant or auditor itself is under investigation, companies may well share Arnold J's discomfort at the implications of his ruling and will want to consider carefully the basis on which they accede to such a request. They may want to seek reassurance about how the documents will be used and who they will be disclosed to so as to mitigate the risks of: (i) any inadvertent disclosure during enforcement proceedings against the regulated entity; and/or (ii) the documents being disclosed to another regulator or investigating authority.

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[1] *R (Morgan Grenfell & Co Ltd) v Special Commissioners of Income Tax* [2003] 1 AC 563.

[2] from *Property Alliance Group Ltd v Royal Bank of Scotland* [2015] EWHC 3187 (Ch), [2016] 1 WLR 992.

Procedure

WHO HAS ACCESS TO COURT DOCUMENTS? – THE RULES ON NON-PARTY ACCESS

Cape Intermediate Holdings Ltd v Mr Graham Dring (for and on behalf of the Asbestos Victims Support Group) [2018] EWCA Civ 1975, 31 July 2018

A recent court order caused alarm for one corporate litigant, Cape Intermediate Holdings (**CIH**), which was ordered to hand over a vast number of documents to a pressure group, the Asbestos Victims Support Group (**AVSG**). The documents had been used in mesothelioma litigation which CIH had settled previously and to which the AVSG had not been a party. On appeal, the Court of Appeal significantly reduced the pool of documents to which the AVSG was entitled. Litigation is generally public, which means that non-parties (including potential future claimants and journalists) are able to access many of the court documents. The Court of Appeal's judgment provides useful guidance about what non-parties are, and are not, able to see.

AVSG had not been a party to the original proceedings but had made a without notice application for access to all documents used at or disclosed for the trial. At first instance, the court allowed AVSG to obtain copies of the following documents from the records of the court:

(i) written submissions and skeleton arguments;

(ii) transcripts;

(iii) trial bundles;

(iv) statements of case (including requests for further information and answers if contained in the trial bundles);

(v) witness statements including exhibits; and

(vi) expert reports.

Non-party access – a reminder of the rules

CPR 5.4C provides that non-parties to proceedings may obtain copies of the following documents from the court:

- a statement of case, but not any documents filed with or attached to the statement of case, or intended by the party whose statement it is to be served with it;
- a judgment or order given or made in public (whether made at a hearing or without a hearing); and
- from the "records of the court", a copy of any other document filed by a party, or communication between the court and a party or another person.

Non-parties can see 'records of the court'

The key issue before the Court of Appeal was the definition of "records of the court". The court held that these were "documents kept by the court office as a record of the proceedings, many of which will be of a formal nature". Documents likely to fall within this definition include:

(i) a statement of case and any documents filed with or attached to a statement of case;

(ii) an application notice; and

(iii) any written evidence filed in relation to an application notice.

Whilst this list was not exhaustive, only documents analogous in nature to those in the list would fall within the definition of "records of the court". Examples include the list of documents (but not the disclosed documents themselves) and witness statements and exhibits filed in relation to an application notice.

Documents which are not 'records of the court'

Crucially, the court said that the following would not generally be considered "records of the court":

(i) witness statements and expert reports exchanged in relation to trial;

(ii) trial bundles;

(iii) trial skeleton arguments or opening or closing submissions; and

(iv) trial transcripts.

Trial documents

Aside from Rule 5.4C the court has an inherent jurisdiction to allow a non-party access to trial documents. The Court of Appeal stated however that non-parties cannot access documents purely because they have been referred to in a skeleton argument, witness statement, expert's report or in court.[1] The court's inherent jurisdiction allows non-parties inspection of the following trial documents:

(i) witness statements (including of experts), where they stand as evidence in chief and would have been available for inspection during trial;

(ii) documents in relation to which confidentiality has been lost due to the fact that they have been read in open court either by advocates or the judge, or the judge has been specifically invited to read them, or which it is clear that the judge has read;

(iii) skeleton arguments or submissions read by the court and which have been deployed at a public hearing; and

(iv) specific documents which it is necessary for a non-party to inspect in order to meet the principle of open justice.

COMMENT

It is not uncommon for a company's management to be concerned about who has access to litigation documents – particularly documents that have been disclosed to the other side, witness statements and expert reports. The concern may be about other future litigants, journalists or a combination of both. The concern may be focused on individual and/or corporate exposure.

This Court of Appeal ruling usefully clarifies what a non-party is entitled to see (and not entitled to see). It is not practical to manage litigation without producing or disclosing documents that may end up being accessed by a non-party. However, understanding the rules will ensure that non-parties are not provided access to documents which they are not entitled to see. It means that in the run up to trial, pre-preparation of press reports can avoid a company being caught off guard should damaging information come to light as a result of non-party access. Finally, it should be taken into account as part of any settlement strategy.

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[1] Upholding the Court of Appeal's decision in *GIO Personal Investment Services Ltd v Liverpool & London Steamship P&I Ass. Ltd* [1999] 1 WLR 984.

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Key contacts

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