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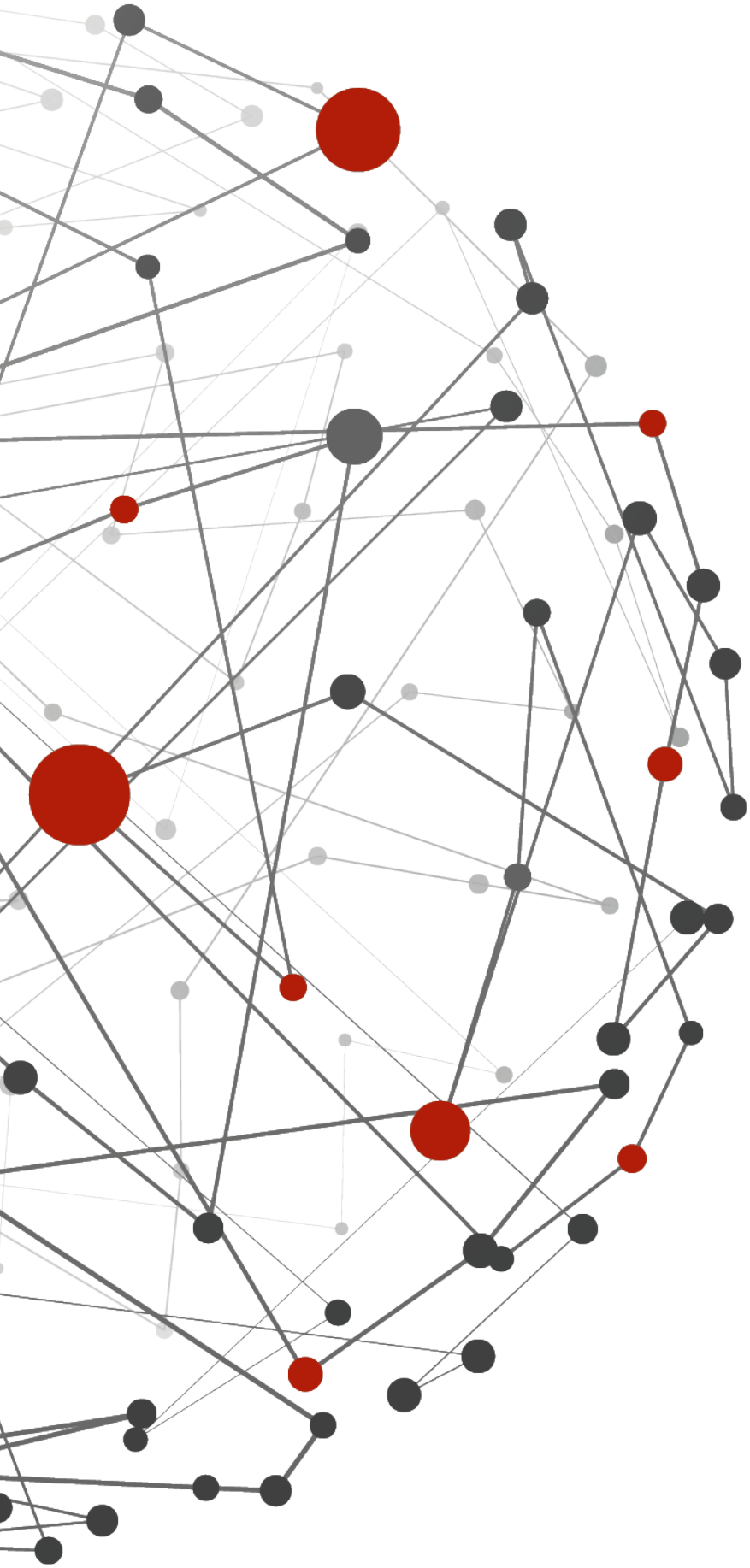

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Class actions

Oil spill representative action attempt fails to meet "same interest" threshold

Harrison Jalla & Ors v (1) Royal Dutch Shell Plc (2) Shell International Trading & Shipping Co Ltd (3) Shell Nigeria Exploration & Production Co Ltd [2020] EWHC 2211 (TCC), 14 August 2020

Representative elements of a claim by individuals and communities arising out of an oil spill off the coast of Nigeria have been struck out by the English High Court. Although there were some common issues of law and fact, they were not sufficient to satisfy the requirement that the multiple parties had "the same interest" within the meaning of CPR r.19.6. This was because of individual differences regarding damage suffered and limitation issues.

The two lead claimants sought to bring claims in negligence and nuisance against the defendants (three companies in the Shell group) on behalf of 27,830 individuals and 479 communities said to be affected by the oil spill. The case has raised a number of jurisdictional and procedural issues to date, there is an appeal outstanding and fresh, related proceedings have been issued. This decision, however, is focussed on representative action issues.

"Same interest" test must be satisfied

Under CPR r.19.6, a claim may be begun or continued by or against one or more persons as representatives of any others who have the "same interest" in the claim. This type of "representative" action proceeds on an opt-out basis, so there is no need for the represented class to be joined as parties to the action or even to be identified on an individual basis. It is the same type of claim that Mr Lloyd is trying to bring against Google.

A key question in this case was whether the lead claimants had the "same interest" as those they purported to represent. There was also a dispute over a connected issue of whether the class had been sufficiently ascertained.

"Same interest" claims do not need to be identical, but must be the same "in effect"

Stuart-Smith J agreed with earlier authority that, while the causes of action of the representing and represented parties do not need to be "congruent", they do need to be "in effect" the same for all practical purposes. The "same interest", which the represented parties must have, is a common interest, which is based upon a common grievance, in the obtaining of relief that is beneficial to all represented parties. It is not sufficient to identify that multiple claimants wish to bring claims that have some common question of fact or law.

In this case, while the claims raised common issues of law and fact in relation to the oil spill, the individual claimants and communities would each need, to complete their causes of action, to prove that the spill caused them damage (the claimants being potentially affected at different times and to differing degrees). The "individualised claims" regarding damage were just as important as the common issues of fact and law; they were not "subsidiary" as the claimants had tried to argue. There were also differences in how limitation defences were likely to be run by the defendants.

So, although there were some common issues of law and fact, there remained a high number of individual claims requiring individual consideration on proof of damage, and individual defences. This made the claim unsuitable for a representative action.

Ascertainment of class

As well as the common interest point, the defendants had also challenged the claimants' ascertainment of class, which is a requirement for a representative action. While the court examined these as separate questions, it noted that the question of "same interest" and "identification of the class" are closely connected. In order to bring a representative action, it must be possible to identify the members of the represented class at all stages of the proceedings (and not just at the end) and the represented cohort must be defined with a sufficient degree of certainty.

The court ruled obiter that it would not have struck out the claim on the basis of failure to ascertain the class because the individual and community claimants were listed in schedules to the Particulars of Claim, and solicitors had asserted that all had given authority to the lead claimants to act on their behalf.

Comment

This case demonstrates the very restricted circumstances in which a CPR r.19.6 representative action can be taken. The reality is that, in many cases, parties may have claims where there are common points of law or construction, but thereafter their interests and legal rights diverge. They may be in a different position with respect to the specific facts of their case, the loss they have suffered, and their claims may have additional issues, such as limitation issues.

In such situations, the representative action may establish, for example, the true construction of a clause in a standard form contract. Thereafter, individual claimants would have to bring their own case, bound by the common principles of construction already agreed in the representative action, to prove and recover their own loss.

Alternatively, if claimants do seek to recover their loss or damage collectively in CPR r.19.6 proceedings, they may have to abandon or leave to one side their individual claims for loss, and pursue only, as the judge put it, the "lowest common denominator" of claim as a representative action. For example, in previous representative actions referred to in the judgment, the claimants claimed based on breach of statutory rights, rather than for individual loss (*The Duke of Bedford v Ellis & ors*) or disavowed any claims based upon the particular facts related to an individual represented person's loss (*Lloyd v Google*).

The judgment also considered an estoppel argument run by the claimants, which submissions were ultimately held not to be relevant to the substance of the judgment, and which is not considered further here.

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Landmark ruling on rule against recovery of reflective loss

Marex Financial Ltd v Sevilleja [2020] UKSC 31, 15 July 2020

The Supreme Court has significantly narrowed the scope of the rule against the recovery of "reflective loss". The rule now only applies to a claim by a shareholder that the value of shares, or of the distributions received as a shareholder, have been diminished by reason of actionable loss suffered by the company. The rule no longer applies to claims by creditors (whether they are also shareholders or not). The ruling will be welcomed by creditors.

The rule against recovery of reflective loss - a reminder

A shareholder cannot bring a claim for a loss suffered by the company, for example damages based on the diminution in the market value of shares or a likely diminution in dividend. A shareholder's loss is said to be merely a "reflection" of the loss suffered by the company, and the company (or its liquidator) is the proper claimant: *Prudential Assurance v Newman Industries (No 2)* [1982] 1 Ch 204. A notable exception to the rule was developed in *Giles v Rhind* [2003] Ch 618: the rule will not apply where the alleged wrongdoing means the company is unable to pursue the wrongdoer.

Several cases since Prudential have raised the possibility that the rule against reflective loss should extend beyond shareholders' claims. In *Johnson v Gore Wood* [2002] 2 AC 1, Lord Millett commented that the rule applied to claims brought by the claimant shareholder in his capacity as employee, rather than his capacity as shareholder. In *Garner v Parker* [2004] EWCA Civ 781, Neuberger LJ stated obiter that it was hard to see why the rule against reflective loss should not also apply to creditors other than employees.

Creditor tries to sue asset-stripper

In *Marex v Sevilleja*, the defendant allegedly asset-stripped two BVI companies ultimately owned and controlled by him so that they were unable to pay their judgment debt to Marex. The BVI companies are now in liquidation.

Marex started English court proceedings against the defendant to claim its judgment debt, interest and costs as damages. Marex's tort claims were that the defendant had knowingly induced and/or procured the BVI companies to act in wrongful violation of Marex's rights under the judgment and that he had intentionally caused loss by unlawful means. The defendant argued, inter alia, that the rule against reflective loss barred Marex's claims.

At first instance, the court held that the rule against reflective loss did not bar the claims of a non-shareholding creditor such as Marex. The court's decision turned on the view that the torts of knowing inducement and unlawful means had a principled part to play in allowing a claimant to hold a defendant to account in the case of deliberate asset-stripping.

Court of Appeal – rule bars claims by creditors

Overturning the decision at first instance, the Court of Appeal held that the rule against the recovery of reflective loss applied to Marex's claims against the defendant, even though Marex was a creditor and not a shareholder of the BVI companies. The Court of Appeal considered that seeking to distinguish between the position of shareholder creditors and non-shareholder creditors was artificial and anomalous, and therefore the rule against the recovery of reflective loss should apply equally to non-shareholder creditors. The rule therefore barred Marex's claim against the defendant.

Supreme Court – reframes and narrows the rule against recovery of reflective loss

The Supreme Court disagreed with the Court of Appeal. All seven members of the Supreme Court agreed that the rule does not bar claims by unsecured creditors of a company. The court was however divided on the reasoning, and split on whether any such rule should exist at all.

Majority - A bright-line rule of company law with no exceptions

The majority judgment was given by Lord Reed, with whom Lady Black, Lord Hodge and Lord Lloyd-Jones agreed. They all thought that the rule should be retained as a 'bright-line' rule of company law but its ambit confined to Prudential, i.e. to only bar claims by a shareholder in respect of loss suffered in that capacity for the diminished value of their shareholding or for the loss of distributions which the company would have paid to them in circumstances where an actionable wrong has been done both to the company and to the shareholder, even if the company does not pursue its own cause of action. The rule does not apply to other types of losses suffered by a shareholder or any claims by a non-shareholder, or to situations where the company has no cause of action.

They criticised the decision in *Johnson v Gore Wood* (except for Lord Brown-Wilkinson), and overruled the exception in *Giles v Rhind*. In their view there is no room for any exceptions to the rule, nor judicial discretion.

Minority – abolish the no reflective loss rule

Led by Lord Sales (with whom Lady Hale and Lord Kitchin agreed), the minority disagreed. They held in effect that there was no reflective loss rule as a principle of the law of damages or a rule of company law. They rejected the "legal fiction" that a shareholder's loss is equal to a company's loss. In their view, a shareholder's loss may be different. A share is a piece of property, the market value of which depends on the estimation of the future business prospects of the company and not just its net asset position. A recovery by the company may not eliminate a shareholder's loss. Instead of having a rule, they advocated approaching claims on a case by case basis, using expert evidence on share valuation and using procedural devices to manage the risk of concurrent claims by a shareholder and a company.

Comment

The controversial earlier Court of Appeal decision had potentially increased the difficulties for creditors seeking to hold shareholders accountable for asset-stripping a defendant company.

The Supreme Court ruling has confined the scope of the rule to within its original limits in Prudential, applying only to certain types of claims by shareholders – ie claims for a diminution in the value of their shareholding or reduction in distributions by virtue of such shareholding where there are concurrent actionable claims by the shareholder and the company, regardless of whether the company pursues any claims.

Over time the rule had expanded to bar claims not just by a shareholder, as shareholder, but also to other types of claims and claimants, eg employees and creditors. The extension of the principle to such cases, the Supreme Court held, "has the potential to have a significant impact on the law and on commercial life". The Supreme Court has halted that expansion.

The finding that the rule does not apply to creditors will be welcomed by finance parties and judgment creditors, regardless of the fact that the judges were divided on the precise reason why it doesn't apply. The majority found that the rule did not apply to a creditor as it only applies to certain types of claims by shareholders. The minority found that the rule does not apply as there should not be a rule at all.

For conflicts of law enthusiasts, the majority classified the application of the rule as a question of company law, which is a departure from the previous approach of considering it as a question of procedural law. This categorisation will impact the conflicts of law analysis in claims with cross-border elements.

The facts of this case reinforce the importance of planning beyond a substantive dispute to the risks, costs and ease of enforcement. Creditors or claimants who suspect that asset-stripping is likely should consider early strategies to pre-empt such wrongdoing.

In a claim against an owner of companies which had been asset-stripped in order to avoid satisfying judgments against them, it was held that the "reflective loss" principle did not extend beyond precluding shareholder claims against the company for diminution in the value of their shares where the company had a concurrent claim. Thus, the rule in *Prudential Assurance Co Ltd v Newman Industries Ltd* [1982] Ch. 204

preventing shareholders from bringing such claims, where their losses flowed purely from losses sustained by the company through wrongdoing, did not apply to an ordinary creditor who was not also a shareholder.

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Contract

Money down the drain? how to avoid damages being sunk by remoteness

Attorney General of the Virgin Islands v Central Water Associates [2020] UKPC 18, 13 July 2020

The fact that your contract has been breached and the breach has caused you losses is not enough for you to make a recovery. Remoteness is the often overlooked third leg of the damages stool. In this case the Privy Council gave more guidance on how the rules in this area work.

The British Virgin Islands Government needed a water reclamation and treatment plant. It therefore engaged Central Water Associates (**CWA**) under two agreements: a design and build agreement (the **DBA**), under which the Government would provide a site prepared for construction and CWA would build the plant; and a management, operation and maintenance agreement (the **MOMA**), under which CWA would operate the plant. That, at least was the plan. The Government effectively pulled the plug when it failed to provide the site. CWA subsequently terminated the DBA; this meant that a condition precedent to the MOMA was not satisfied such that it, too, fell away.

Although the Government's failure had ultimately brought down both the DBA and the MOMA it had done so in somewhat different ways. The Government had breached an express promissory condition of the DBA, which gave CWA a right to claim damages. However, most of CWA's losses flowed from the profits it would have earned under the MOMA, and there had been no breach of any express term of the MOMA. True, a condition precedent had not been satisfied, but failure to satisfy a condition precedent is not in itself a breach (in a pure condition precedent a party does not promise that it will do something, it simply agrees what will happen if that something does not happen) and so does not give rise to a damages claim. So (the Government argued) the contract that had been breached did not give rise to the lost profits; and the contract that gave rise to the lost profits had not been breached.

CWA was not ready to see its claim flushed away in such a fashion. It advanced two arguments before the Privy Council:

1. There was an implied term in the MOMA that had been breached. Unfortunately for CWA, it changed its position between the original arbitration and the appeal, so it was impossible for the Privy Council to find there had been an error of law in the original finding and it would be inappropriate on an appeal of a question of law to consider a factual assertion that had not been advanced before the arbitration tribunal.
2. The parties had known about the MOMA when they signed the DBA; indeed, the agreements were signed on the same day and by the same people. So it was entirely foreseeable that a breach that resulted in termination of the DBA would also cause a loss of profits under the MOMA. Those profits were therefore properly recoverable for the breach of the DBA, even though they arose under another contract. This was the remoteness issue.

The Privy Council started its analysis with the frequently cited rule in *Hadley v Baxendale*. There, it was found that two types of losses were recoverable: (i) those losses that arise in the ordinary course from such a breach of contract; and (ii) losses that were specifically in the contemplation of the parties at the time of contracting, typically because one party tells the other that it is unusually exposed to loss in some way. In light of that decision and the subsequent case law, the Privy Council formulated five propositions:

1. Damages for breach of contract are compensatory; they are intended to put the party whose rights have been breached in the financial position it would have been had the contract been performed.
2. However, recovery is limited to such part of the loss actually resulting as was, at the time the contract was made, reasonably contemplated as liable to result from the breach. To be recoverable, the type of loss must have been reasonably contemplated as a serious possibility. In applying this approach the Privy Council cautioned against a pure probabilistic approach. Probability was relevant but, as the Supreme Court had noted in The Achilleas: "If a manufacturer of lightning conductors sells a defective conductor and the customer's house burns down as a result, the manufacturer will not escape liability by proving that only one in a hundred of his customers' buildings had actually been struck by lightning."
3. The question of what was reasonably in the parties' contemplation depends on what they knew at the time, or at the very least what the party subsequently in breach knew at the time.
4. The test is objective – it is not what the defendant actually contemplated that matters, it is what they must be taken to have contemplated.
5. The criterion for assessing what a party had in its contemplation is a factual one.

Applying those propositions the Privy Council found that the losses under the MOMA would have been in the reasonable contemplation of the Government at the time it entered into the DBA: as was plain from both the terms of the contracts and the way they were entered into, they were intended to operate together. The Government had the requisite knowledge to satisfy the second limb of *Hadley v Baxendale*, meaning its remoteness defence failed.

The decision does not change any of the rules on remoteness, but is a useful, if rather short, summary of the key principles. It will obviously be of interest to litigators (and litigants) considering damages claims. Keep in mind, however, that references to "indirect and consequential loss", often used in exclusion clauses, have been held to refer to losses recoverable under the second limb of *Hadley v Baxendale*, making this a decision of wider application. It may be a case about sewers, but it is in no way limited to suing.

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On notice – spa tax claim unenforceable as inadequate notice given

Dodika v United Luck [2020] EWHC 2101 (Comm), 31 July 2020

A tax indemnity claim under a share purchase agreement was unenforceable because inadequate notice was given. The buyers gave notice of their claim by solicitors' letter. However, that notice was inadequate, as it did not provide reasonable detail of the matter giving rise to the claim.

The letter (sent shortly before the relevant deadline) made reference to an ongoing "investigation by the Slovene Tax Authority … into the transfer pricing practices" of a subsidiary of Outfit7 (the company sold, and best known for the popular Talking Tom and Friends app and media franchise). However, there was no reference in the letter to the factual basis of the claim under the tax covenant – the claim would not be based on the mere existence of a tax investigation. In particular, the letter did not identify the underlying facts unearthed during the investigation which were relied on by the buyers to support their claim.

The court observed that the recipient of a notice would wish to know, at least in general terms, the three key elements of any contractual claim, i.e. the factual basis, the legal basis, and the quantum. The purpose of the notification was to enable the recipient to "deal with the [c]laim" (e.g. by performing further investigation, seeking clarification, notifying third parties, accessing archived documents, obtaining professional advice, assessing the merits of the claim, making a financial provision etc.).

However, in the court's view, if a reasonable recipient of the letter had been asked what general facts the claim was based on, they would have answered "I do not know".

Even if it was assumed that the sellers had detailed factual knowledge of the tax investigation, the notice was still inadequate. A compliant notice needed to indicate how the claim arose out of the specific facts identified. In the present notice, the compendious reference to the tax investigation was insufficient – it failed to identify the particular factual matters relied on by the buyers to support their claim. Further, the buyers had not identified the factual basis for their claim in any prior correspondence.

This case is another reminder that it is critical to comply carefully and fully with contractual notice provisions. The consequences can be severe if they escape notice.

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Data protection

CJEU invalidates EU-US Privacy Shield framework and upholds EC Standard Contractual Clauses

Data Protection Commissioner v Facebook Ireland and Maximillian Schrems, [2020] 7 WLUK 245, 25 August 2020

The CJEU invalidated the European Commission's (the EC) adequacy decision on the EU-US Privacy Shield and upheld the general validity of the EC standard contractual clauses for cross-border data transfers (SCCs). However, compliant data transfers under SCCs will become more onerous for data exporters, importers and supervisory authorities, and the reasoning of the CJEU will have significant impact on other mechanisms for international transfer from the EEA to third countries, in particular countries where national laws provide for surveillance powers and insufficient judicial redress for individuals from the EU.

The case revolved around the validity of transfers of personal data EU Facebook users to the US, following the Snowden revelations concerning mass surveillance practices by US agencies and law enforcement authorities. The claim by the Austrian citizen Maximillian Schrems resulted in invalidation of the EU-US Safe Harbor programme by the CJEU back in 2015 (**Schrems I case**). The EU and the US established since then a new framework for international data transfers, the EU-US Privacy Shield, and the EC had adopted an adequacy decision allowing free flow of personal data to recipients in the US certified under this framework. In the meantime, Facebook implemented EC controller-processor SCCs to ensure its data transfers from the EU were covered. In the Schrems II case, Maximillian Schrems contested the legality of Facebook's data transfers to the US under the SCCs, and the validity of the SCCs as a mechanism for cross-border transfers to third countries without adequacy status.

EU-US Privacy Shield

Although the referring court did not ask the CJEU to look into the EU-US Privacy Shield framework, the

CJEU's Advocate General (**AG**) had discussed it at length in its December 2019 opinion (available here) and questioned its validity, particularly in relation to the right to respect for private life and the right to an effective remedy. The AG considered, amongst other issues, Section 702 of the US Foreign Intelligence Surveillance Act and expressed doubts about the conformity of the EC's Privacy Shield decision with Art. 45(1) GDPR.

In Schrems II, the CJEU has now examined the EC adequacy decision 2016/1250 for the EU-US Privacy Shield and declared it invalid. The CJEU noted that the framework does not protect personal data of EU residents from US surveillance, and fails to ensure that EU individuals have effective and enforceable remedies through the courts or an effective Ombudsman in relation to certain US mass surveillance laws.

This means that transfers from the EU can no longer be made to the US in reliance on the fact that the recipient is certified under the EU-US Privacy Shield. It is important to note that the CJEU decision does not affect the validity of the Swiss-US Privacy Shield framework, but the Swiss supervisory authority has already issued a press release stating that it will study the judgment and comment on its impact in due course.

Standard Contractual Clauses

The CJEU confirmed that the EC adequacy decision for Controller to Processor SCCs is valid and provide appropriate safeguards for transfers of personal data to third countries. However:

- SCCs should be viewed as offering the basic level of protection. Data exporters must assess on a case-by-case basis whether additional safeguards are needed. They should verify the legal conditions in a country and in particular the laws which may apply to the particular parties/data before making a transfer. Where necessary, they must put additional measures of protection in place to address any issues. However, where foreign law imposes obligations on the recipient contrary to the SCCs and which are therefore capable of impinging on the contractual guarantee of an adequate level of protection against access by the public authorities, the transfer cannot be made.
- The SCCs already require the recipient to notify the exporter of any change in law affecting compliance with the SCCs. The CJEU states that if the situation cannot be remedied by the parties, the data must be returned or destroyed; transfer in breach may give rise to a compensation claim for damages suffered by individuals.
- The extent of the obligation to verify and report under the SCCs is not clear. According to the CJEU, exporters should take into account the EC's findings of adequacy. Necessary and proportionate access under mandatory requirements of foreign legislation which do not go beyond what is necessary in a democratic society to safeguard national security, defence and public security should not pose a problem, but compliance with an obligation which goes beyond what is necessary for those purposes must be treated as a breach of SCCs.
- National supervisory authorities (**DPAs**) must suspend transfers based on SCCs where they take the view that, in the light of all the circumstances of a particular transfer, they are not or cannot be complied with in the destination country and the data cannot be protected by any other means. The CJEU noted the obligation under the SCCs on the recipient to make the controller aware of issues in a particular jurisdiction and on the controller to pass this information to the DPA to investigate.

Effect on Current and Future Transfers

Transfers can no longer be made to the US in reliance on the fact that the recipient is certified under the EU-US Privacy Shield.

Controllers may continue to use SCCs to transfer data outside the EEA but will need to assess whether laws in the destination affect the protection provided by the SCCs in their particular case. If not, or where they are notified by the recipient that there is an issue affecting compliance with the SCCs, they should take steps to implement additional measures to establish necessary protections under the SCCs and consider whether notification of DPAs is necessary. This is clearly burdensome for controllers and will impact the ease with which SCCs can be implemented.

Whether controllers may continue transferring personal data to the US on basis of the SCCs is unclear. The CJEU invalidated the EU-US Privacy Shield because of surveillance powers and laws in the US and the lack of effective judicial redress mechanisms for EU residents. In this respect, the private contractual arrangements under the SCCs are unlikely to be considered to offer better protection or redress than the Privacy Shield. Arrangements to store the data of Europeans in EU-based data centres or encrypt data will

not likely change the situation, on their own, as recently adopted US laws (including the CLOUD Act) seek to capture any data of US companies stored worldwide.

In this respect, we expect that the same reasoning will also apply to transfers under binding corporate rules (**BCRs**). BCRs already require a corporate group to disclose to the BCR lead any national laws that might impede compliance with the BCRs. It is logical for supervisory authorities to expect assessment of transfers under the BCRs to specific jurisdictions and the restriction of transfers where a conflict leads to inability to enforce protections. In contrast to the SCCs and EU-US Privacy Shield, BCRs do offer judicial redress mechanisms to data subjects whose personal data are covered by the BCRs.

The CJEU referred to the alternatives for transfer under Art. 49 GDPR (such as a data subject's explicit consent or transfer for performance of a contract, etc.) but these alternatives will not be suitable for general business use, given that the European Data Protection Board (**EDPB**) guidelines consider these alternatives appropriate only where safeguards such as SCCs are not available.

Next steps

The EC has stated in a press conference that it will produce guidance for businesses, issue a cross-border transfers toolbox under the GDPR, speed up adoption of the modernised SCCs, review current adequacy decisions to align with the CJEU decision and look into the future of the EU-US Privacy Shield framework.

The US Secretary of Commerce voiced disappointment with the invalidation of the EU-US Privacy Shield framework and stated that the Department of Commerce will continue administering the framework, including processing submissions for self-certifications and maintaining the Privacy Shield list. In addition, the certified organisations are not relieved of their obligations under the framework.

Various national supervisory authorities have already reflected on the Schrems II decision and raised their doubts that transfers to the US can continue under SCCs. For instance, the **Irish Data Protection Commissioner** has issued a statement saying that the use of SCCs for transfer to the US is now questionable not least because assessments will need to be made on a case-by-case basis.

Some German DPAs also commented on the case. The **Hamburg DPA** stated that the CJEU was not consistent in upholding SCCs. It says that although BCRs, individual agreements and SCCs can continue to be used for transfers, uncertainty for transfers has increased compared to 5 years ago, when the EU-US Safe Harbor was invalidated. The DPA noted that EU supervisory authorities should come promptly to a common understanding on how to deal with companies that continue relying on Privacy Shield. Taking a strict stance, the **Rhineland-Palatinate DPA** issued a FAQ where it clarified that following invalidation of the Privacy Shield, controllers should not wait for instructions from supervisory authorities but must immediately switch to alternative transfer mechanisms under the GDPR, as there is no transition period to remedy non-compliance is contemplated. The Rhineland-Palatinate DPA further stated that DPAs are reviewing the impact of the CJEU decision on other transfer mechanisms.

The press release of the CJEU is available here, and the Decision here.

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Privilege

Legal advice privilege: does a lawyer get you home and dry?

A v B [2020] EWHC 1492 (Ch), 10 June 2020

It is often assumed that if a lawyer plays some part in the creation or production of a document, it automatically becomes privileged, giving it protection from disclosure in subsequent litigation. This High Court is a reminder that legal advice privilege will only apply between a lawyer and client when the document (or other evidence) reflects that its dominant purpose is to provide legal advice in a relevant legal context. The case reported below examines privilege in a regulatory context and therefore will be of interest to those employers in financial services and other regulated sectors.

The dispute arose in a regulatory context in that the Financial Reporting Council (**FRC**) sought disclosure of documents from the auditor (B) of a large retail client in the context of an investigation by the FRC into the auditor. The client (A) asserted that certain of those documents were privileged, that the privilege in those documents belonged to A and that they should not be disclosed by B to the FRC. The first case concluded that the auditor can form its own view on whether the documents were privileged. These subsequent proceedings looked at the substance of five documents, which included board minutes, to establish whether they were privileged or not.

What is legal advice privilege?

Legal advice privilege attaches to communications made in confidence between lawyers and their clients for the dominant purpose of giving or obtaining legal advice in a relevant legal context. As the judge in this case noted, this extends to documents (such as internal communications within a company) which reproduce legal advice for dissemination to those who need it, provided confidentiality is maintained.

It is not necessary for each communication between a lawyer and client to contain legal advice or a request for legal advice in order for legal advice privilege to apply. It is sufficient for it to be advice on what can or should prudently and sensibly be done, so long as that advice is given in a legal context. Where that is the case, the entirety of the communication is privileged. In other words, the continuum of communication between lawyer and client will be protected.

Documents examined by the High Court

The table below sets out the documents examined by the High Court together with the outcome on privilege and the judge's reasoning.

Document	Why privilege was asserted by the client	Privileged	Court Reasoning
Executive Committee Minutes x 2	– GC had modified versions of the documents – Documents marked confidential & privileged – There was a section headed Legal & Regulatory matters	No	– Documents amounted to a record of the meeting – They did not contain legal advice – GC's input was no more than fulfilling a secretarial function – Lawyers often perform secretarial functions by recording discussions at important meetings – GC spent no more than a few minutes editing documents – Calling a document privileged does not affect its status

Document	Why privilege was asserted by the client	Privileged	Court Reasoning
			– There was nothing in the document to indicate that legal advice had been given at the meeting
Board Meeting minutes	The metadata showed that the minutes were originally prepared by a lawyer from an external law firm	No	The evidence simply pointed to it being a record of the meeting which neither expressly recorded the communication of advice nor in its form reflected legal advice which had been given
Risk Register	Prepared by GC with the dominant purpose of giving legal advice	No	– How to mitigate risks could amount to legal advice but not in these circumstances – A document is not privileged because it takes account of legal advice; it would need to communicate or make clear the substance of that legal advice
Draft Chairman's script	– The version was prepared by an external lawyer and included comments by the lawyer – The document contained one comment from the external lawyer which had been struck out in track changes but was still visible	No	– This particular version of the script was not likely to have been produced by the lawyer as the lawyer's comment had been deleted – With the exception of the deleted comment, there was nothing to indicate that it communicated legal advice

Comment

The case is a useful application of the rules on legal advice privilege, which neatly illustrates how privilege will very often not be available, notwithstanding the involvement of lawyers in the creation of documents. It is the nature and content of the document that is critical and not the way it was created, or who was involved in its creation. Particular points to note include:

1. Labelling a document as privileged is not determinative of its status.
2. Having a lawyer create a document will not necessarily mean that the document is privileged. It will only benefit from legal advice privilege if the document contains advice or is part of the continuum of giving advice. In particular, where litigation is not in contemplation, a fact finding exercise would not be privileged, unless it could be said to be part of the process of providing legal advice. This is a question of fact.
3. Having a lawyer set up, run, or provide secretarial assistance to a committee will not mean that the committee's papers are automatically subject to privilege.
4. The fact that a document has been produced, with advice having first been taken, does not mean that the document is privileged.
5. Where maintaining privilege is important, this needs to be considered at the outset of a matter and at any stage where there is particular sensitivity around certain documents.
6. It is better to be conservative and to assume that privilege will not apply, rather than proceeding on the assumption that it will.

7. Having something open and on the record is not necessarily a bad thing. In many cases it will be positively helpful in establishing a client's position – and the facts are the facts – they can never be cloaked by privilege.

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Sanctions

The long arm of OFAC: English law contracts and U.S. secondary sanctions

Lamesa Investments Ltd v Cynergy Bank Ltd [2020] EWCA Civ 821, 30 June 2020

A provision in an English law facility agreement stating that the borrower would not be in default if "sums were not paid in order to comply with any mandatory provision of law" allowed the borrower to avoid making payments where to do so could result in the imposition of U.S. secondary sanctions.

While the decision of the High Court was upheld, its reasoning was not. The judgment is a useful illustration of the approach to the interpretation of sanctions-related clauses, particularly in financing agreements.

Lamesa, acting as lender, was a Cypriot company wholly owned by a group company registered in the British Virgin Islands. The group company's owner was added to a list of "Specially Designated Nationals" by the U.S. Department of The Treasury Office for Foreign Assets Control (**OFAC**). As a result, Lamesa became a "blocked person" under a U.S. federal law, exposing Cynergy, the English borrower, to secondary sanctions if it made payments to Lamesa.

Cynergy refused to make payments, relying on a clause in the facility agreement allowing it to escape a default if "sums were not paid in order to comply with any mandatory provision of law, regulation, or order of any court of competent jurisdictions."

The Court of Appeal noted:

- The provision was a standard term in common usage. The focus, therefore, should be on the words used (and not the particular factual background).
- Clear words are required to abrogate a repayment obligation.
- The court must take account of the commercial interests of both parties (the judge at first instance seemed to have preferred those of Cynergy).
- The relevant context:
- The provision was not just about sanctions.
- It did not extinguish the entitlement to be paid interest and be repaid capital. Rather, if engaged, Cynergy would not be in default.
- Ultimately, the provision was an attempt to balance the lender's need to be paid on time and that of the borrower not to infringe mandatory provisions of law.

The court stated that because the provision was ambiguous, context and commercial common sense were relevant. It held:

- The clause was intended to be used by international banks. A risk facing international banks is the problem of dealing with U.S. secondary sanctions. Tier 2 lending is an EU concept, and the parties were EU financial institutions. If a "mandatory provision of law" only referred to one that directly

bound the borrower not to pay, it would have almost no possibility of taking effect.

- The provision must have intended the borrower to be capable of obtaining relief from default if its reason for non-payment was to "comply" with a foreign statute that would otherwise be triggered. The EU Blocking Regulation (which seeks to limit the extra-territorial application of third country laws) was known to regard U.S. secondary sanctions legislation as imposing a "requirement or prohibition" with which EU parties were otherwise required to "comply".
- Although U.S. legislation cannot prohibit, and does not purport to prohibit, a payment by Cynergy to Lamesa, its effect is clearly one of prohibition as the EU Blocking Regulation makes clear.
- Once the U.S. legislation is seen as an effective prohibition, Cynergy's reason for non-payment is indeed to comply with it.

One member of the Court of Appeal had doubts about the interpretation of "in order to comply with" and whether this meant in order not to comply with the U.S. legislation or in order to avoid the risk of being sanctioned. However, he did not dissent.

Comment: This case is of particular interest to non-U.S. banks that are parties to English law governed contracts, especially where they do not routinely include contractual provisions that expressly refer to U.S. sanctions. This is because the judgment clarifies that a reference to a "mandatory provision of law" may include reference to U.S. secondary sanctions.

Going forward, banks will need to consider carefully the drafting of their agreements to ensure that they are not disadvantaged in circumstances where there is a risk that their counterparty may be targeted by U.S. sanctions or the arrangements may otherwise carry a U.S. secondary sanctions risk.

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Key contacts

If you require advice on any of the matters raised in this document, please call any of our Litigation and Dispute Resolution partners, your usual contact at Allen & Overy, or Karen Birch.

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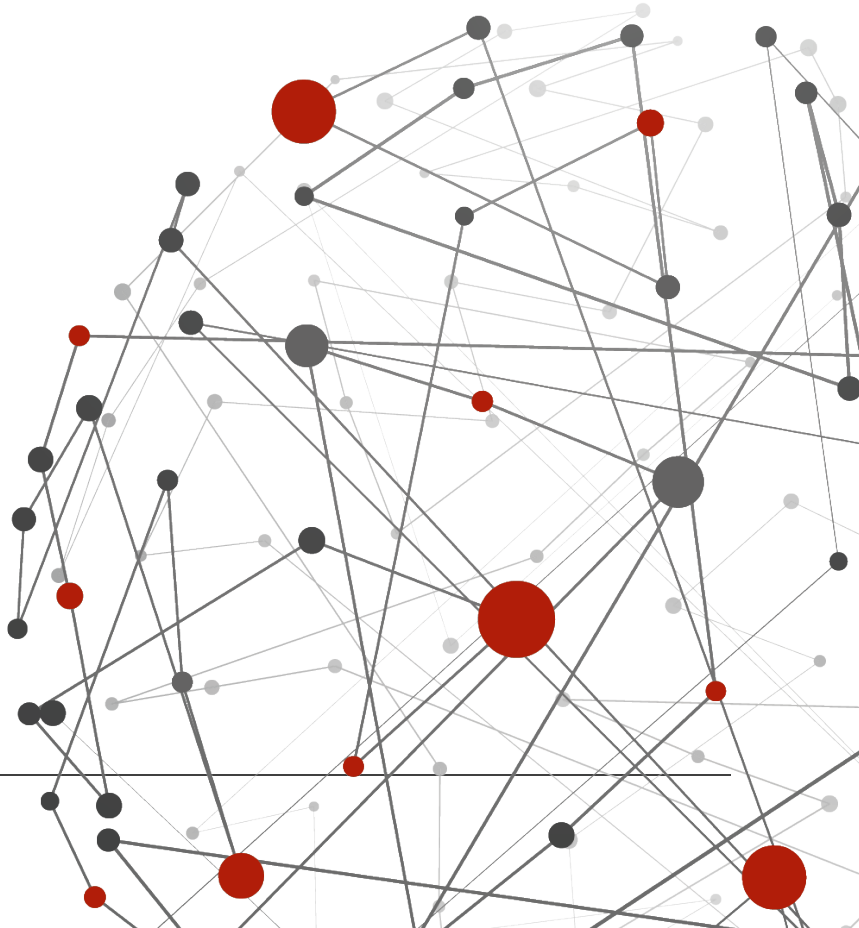

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