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From the editor

Welcome to the latest edition of *Corporate and commercial disputes review*.

In this edition, we feature an analysis of the law on contractual discretion, an issue that will be of interest to clients across all industries and sectors. We also consider trends in case law on contractual interpretation and a recent case concerning agreements to agree.

Turning away from the field of contract law, we examine an important decision on legal professional privilege. We also consider the related subject of data subject access requests and review two recent cases where the Court of Appeal has considered the use of DSARs as a way of obtaining disclosure of documents. On the regulatory side, we review the new Criminal Finances Act and the changes to the suspicious activity report regime.

In relation to company law, we look at a recent case concerning the valuation of shares.

Finally, in light of recent currency fluctuations, we review two recent cases where the courts have grappled with the impact of changes in exchange rates on costs.



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Contractual discretion and its limits

Commercial contracts often afford one party a discretion as to whether or how it exercises its rights or fulfils its obligations. For example, a contractual option may give the option holder the right, but not the obligation, to exercise that option (provided that any applicable conditions are met). In a variety of contexts, a party may require the consent of another to do certain things. Finally, under certain finance and derivatives contracts, one party is often tasked with valuing the underlying assets in certain circumstances (e.g. the close-out of a contract following an event of default).

In such instances, the following question arises: what are the limits, if any, on the exercise of such contractual right or discretion? The simple (if not the most practical) answer is that it is fundamentally a matter of construing the contractual provision in question. That said, there has been substantial judicial scrutiny of this issue in recent years, resulting in the development of a set of principles, which will be of assistance to commercial parties.

This article will survey this line of authorities, including the most recent developments in commercial and finance contexts, and also seek to give some practical points to consider, both before and after any dispute arises as to the proper exercise of the right or discretion in question.

Absolute contractual right and contractual discretion distinguished

In *Abu Dhabi National Tanker Co v Product Star Shipping Ltd (The Product Star)* [1993] 1 Lloyd's LR 397, the discretion in question was the master or owner's ability to refuse to proceed to any port which, in their discretion, was considered as dangerous. Leggatt LJ stated the following principle in relation to the exercise of a contractual discretion:

"Where A and B contract with each other to confer a discretion on A, that does not render B subject to A's uninhibited whim. In my judgment, the authorities show that not only must the discretion be exercised honestly and in good faith, but, having regard to the provisions of the contract by which it is conferred, it must not be exercised arbitrarily, capriciously or unreasonably."

It is important to note that the limitation applied even though there were no express limitations or qualifications on the exercise of such discretion. In a finance context, essentially the same limitation was held to apply in *Socimer International Bank v Standard Bank London Ltd* [2008] EWCA Civ 116, a case in which one party to an agreement for the forward sale of a portfolio of securities was tasked with its valuation.

The authorities are clear that such a limitation applies as a matter of necessary implication (*Cantor Fitzgerald International v Horkulak* [2004] EWCA Civ 1287). Therefore, the rationale for such a limitation is not grounded in some general doctrine of "good faith", but rather that "it is presumed to be the reasonable expectation and therefore the common intention of the parties that there should be a genuine and rational, as opposed to an empty or irrational, exercise of discretion".

Leaving aside for the moment the precise nature of the limitation and how it is applied by the Court (which will be addressed in the next section), when will any such a limitation be implied at all?

In this regard, the Court of Appeal has distinguished between

- The “exercise [of] an absolute contractual right” (*an absolute contractual right*).
- “Making an assessment or choosing from a range of options, taking into account the interests of both parties”¹ (*a contractual discretion*).

There will be no limitation implied in respect of an absolute contractual right, whereas there will be (unless there are clear express terms to the contrary) in respect of a contractual discretion.

It is fundamentally a matter of construction of the particular contractual provision whether the party has an absolute contractual right or a mere contractual discretion. Therefore, the express terms will play a key role. If a contractual provision expressly limits or qualifies the way in which a party can exercise a right or perform its obligations (e.g. the requirement of (commercial) reasonableness or good faith), then it is highly likely to fall on the contractual discretion side of the line.

There are no hard and fast rules in this regard; the wording and the substance of the provision in question must be carefully examined to determine whether it confers an absolute contractual right or a mere contractual discretion. That said, and although not universal, it seems that where a party is entrusted with performing a *quasi-adjudicative* role in the context of conflicting interests of parties, the performance of that role will be subject to a limitation of the type described above.

Finally, being an implied term, the limitation may of course be excluded by contrary express terms. However, authorities suggest that although not utterly impossible, it would be extremely difficult to exclude. For example, in *WestLB AG v Nomura Bank International Plc* [2012] EWCA Civ 495, a fund was to be valued by the calculation agent “in its sole and absolute discretion” and the valuation was to be “final and binding...in the absence of manifest error”. However, this language did not exclude the implication of the limitation.

The limitation on the exercise of a contractual discretion

How are we to interpret the implied limitation on the exercise of a contractual discretion? What are the standards it imposes? The authorities set out the following principles, which apply in the absence of express words to the contrary.

“Reasonableness”

The requirement of honesty and good faith seem clear enough; the party afforded the discretion (the *decision-maker*) must properly direct itself to the task in hand and should not exercise the discretion in question in furtherance of an ulterior motive. With respect to the requirement that the relevant discretion must not be exercised arbitrarily, capriciously, perversely or unreasonably, it seems settled that “reasonableness” in this context is not analogous to a duty to take reasonable care but to *Wednesbury*-reasonableness (i.e. in order for a decision to be impugned, it must be a decision which no rational decision-maker could have arrived at)².

However, this is not to say that the ambit of discretion will be wide in every case. In certain factual circumstances, it may well be that there are only very limited ways in which a party can exercise the discretion in question without falling foul of the rationality test. The more difficult and uncertain the exercise of the discretion in question, the wider the range of rational decisions will likely be. For example, this will likely be the case in the valuation of illiquid securities in difficult market conditions with little or no reliable pricing information³.

This means that, where there is a range of decisions that a party could have taken within the bounds of rationality and the original decision falls within that range, the decision remains that of the decision-maker and the Court does not replace it with a decision which it (or anyone else, for that matter) would prefer.

Own interests

It seems that, at least in certain circumstances, the decision-maker may consult its own interests in exercising a discretion, as opposed to approaching the exercise with complete neutrality. For example, in *Socimer*, the non-defaulting party was forced to retain certain illiquid assets in difficult market conditions as a result of the counterparty’s default under a forward sale contract. Given the difficulties in valuing the assets in question in the prevailing circumstances and the fact that it never sought to retain the assets, it was held that the non-defaulting party was “entitled primarily to consult its own interests” in valuing the assets (subject to the requirements of honesty, good faith and rationality).

¹ *Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd* [2013] EWCA Civ 200 at paragraph [83].

² See, for example: *Socimer*; *WestLB v Nomura*; *Braganza v BP Shipping Limited* [2015] UKSC 17; *Lehman Brothers International (Europe) (in administration) v ExxonMobil Financial Services B.V.* [2016] EWHC 2699 (Comm); and *LBI EHF (in winding up) v Raiffeisen Zentralbank Österreich AG* [2017] EWHC 522 (Comm).

³ See, for example: *Socimer*; *WestLB v Nomura*; and *Lehman v ExxonMobil*.

Similarly in *WestLB v Nomura*, noting that the commercial structure of the transaction was that Nomura, as issuer, was supposed to have no risk in the underlying assets, and the purpose of giving to such a party to the transaction a discretion to value is to enable it to protect itself from risk, it was held that Nomura was “entitled to have an entirely proper regard for any danger to itself from valuing too optimistically” (again, subject to the requirements of honesty, good faith and rationality). Also in *Lehman Brothers International (Europe) (in administration) v ExxonMobil Financial Services B.V.* [2016] EWHC 2699 (Comm), it was held that ExxonMobil, as the non-defaulting party valuing securities in the context of a close-out of a repo transaction under a 2000 Global Master Repurchase Agreement, was “entitled to have regard to its own commercial interests”.

However, it is suggested that caution must be exercised in this regard. In all of the cases above, the commercial rationale for giving the discretion as to valuation to one party was to protect itself from risk and the difficulty of the valuation in question were key factors in arriving at the conclusion that such a party may take its own interests into account. Although in many cases the very purpose of affording a discretion to one party might well be to protect that party from risk, it may not always be so. If not, it remains to be seen whether taking into account one’s own interest in exercising the discretion satisfies the test of honesty, good faith and rationality.

Process v outcome

The authorities have generally focussed on the end result of the exercise of a contractual discretion. However, in *Braganza v BP Shipping Limited* [2015] UKSC 17, the idea of the Court’s review of not only the outcome of a party’s exercise of a contractual discretion but also the process by which it exercised

the discretion was raised. In that case, the Supreme Court did scrutinise not only the outcome but also the decision-making process. The Supreme Court expressly left open the question of the extent to which the Court’s review of the decision-making process would apply in all contractual contexts, particularly commercial contracts, stressing the importance of the employment context of *Braganza* itself.

The point was raised head-on in *Lehman v ExxonMobil* in the context of a US\$250 million “repo financing extended by an oil major to an international investment bank” and it was decided that a review of the decision-making process in this context was not appropriate. Many will regard *Lehman v ExxonMobil* as a welcome decision for sophisticated commercial parties who, in most cases, may wish to avoid the uncertainties and expense of a full judicial review of the decision-making process pursuant to a contractual discretion.

However, this is not to encourage parties to pay no regard to the process adopted in exercising the discretion. In practice, a rational decision-making process carried out honestly and in good-faith is likely to lead to a robust and defensible outcome. Further, it would be surprising if the Court’s decision on the outcome were not coloured to an extent by the evidence of the process adopted, even where the latter is not formally under scrutiny.

Finally, of course parties are entirely free to expressly provide for the review of both the process and the outcome. For example, the 2002 ISDA Master Agreement provides that the “Close-out Amount will be determined by the Determining Party (or its agent), which will act in good faith and use commercially reasonable procedures in order to produce a commercially reasonable result”. The reference to “commercially reasonable procedures”

means that the Court is able to scrutinise the process undertaken by the determining party.

Result of a non-compliant exercise of a contractual discretion or an absence of an exercise

What does the Court do if: (a) the Court has decided that the original exercise of a contractual discretion was contractually non-compliant; or (b) the discretion had to be exercised but, for whatever reason, the discretion was not exercised at the relevant time (and cannot now be exercised)?

Consistent with the principle set that the decision remains that of the decision-maker, the authorities are clear that the Court will ask a question of what contractually compliant decision the decision-maker would have made⁴.

First, this means that the Court will not simply provide its own preferred contractually compliant decision. To do so would largely deprive the decision-maker of the benefit of the discretion conferred upon it.

Second, it also means that the Court will not automatically accept the decision maker’s bare assertion that it would simply have exercised the discretion in the way that would have been most favourable to it; that is, the party afforded the discretion is not necessarily entitled to the benefit of the most favourable exercise of the discretion it could (rather than would in fact) (in a contractually compliant manner) have made⁵.

⁴ See *Socimer* paragraph [65], *West LB v Nomura* paragraph [58] and *Lehman v ExxonMobil* paragraph [280].

⁵ See, for example, *Cantor Fitzgerald v Horkulak* where the Court rejected the submission that an employer should be assumed that it would simply have paid the minimum permissible level of discretionary bonus instead of working through how it would, in fact, have determined the level (see paragraph [67]).

That said, it may well be that, on the evidence, the most favourable contractually compliant decision which the decision-maker could have made was what it in fact would have made. This is entirely credible in cases such as *Socimer, WestLB v Nomura* and *Lehman v ExxonMobil* where the decision-maker would have been entitled legitimately to consult its own interests. In such cases, however, the decision-maker should ensure that it adduces factual evidence to support its “minimum obligation” case. Given the hypothetical nature of the exercise, this will most likely be in the form of a witness statement from the individual who was (or would have been) entrusted with making the relevant decision⁶. Without such evidence, there is a danger that the Court decides that it has no evidential basis to determine what the decision-maker would have done, or even the Court accepting other party’s evidence as to what it thinks the decision-maker would have done.

Conclusion and practical points

In conclusion, the exercise of contractual discretion has received substantial judicial scrutiny in recent years, with many cases reaching the appellate level. This has produced a number of helpful principles, which should assist parties in their exercise of a contractual discretion, in their scrutiny of the counterparty’s exercise of such discretion and in any disputes resulting from such an exercise.

The key practical points for commercial parties are as follows:

Express terms

Much of the analysis above applies in the absence of further or contrary

express terms in relation to the right or discretion in question. Clear express terms to the contrary may displace the above analysis so careful attention should be given in drafting and interpreting provisions conferring contractual rights or discretion.

The decision maker

One should determine at the outset whether the contractual provision confers: a) an absolute contractual right; b) an absolute contractual obligation; or c) a contractual discretion. Under a), its exercise will be unfettered. Under b), there will be no right or discretion and the obligations must be performed strictly in accordance with the contract. Under c), there may be a range of options, the width of which will depend on the particular circumstances. In an extreme case, there might only be one (or a very narrow range of) rational decision(s), which will make the discretion largely illusory.

Challenging the exercise of the right or discretion

Under a), the exercise cannot be challenged. Under b), the decision-maker will be in breach if it does not perform its obligations strictly in accordance with the contract. Under c), one should assess how wide the decision-maker’s discretion might be and whether its decision likely falls within it, in light of the contractual provision in question and factual circumstances. The more difficult the decision, the more likely it is that the decision-maker will be afforded a wide discretion. In such cases, it may be difficult to displace the original decision.

Adduce the right evidence

Where there has been no (or no contractually compliant) exercise of discretion, the need to produce factual evidence as to what the decision-maker would have done has been mentioned above. In some cases, expert evidence

may also be required to assist the Court in deciding what the range of contractually compliant outcomes is (i.e. what the decision-maker could have done). However, when adducing such evidence, it is important to ensure that the expert evidence addresses the right question: that is, what range of outcomes could the decision-maker have determined, acting honestly, in good faith and rationally. What the experts themselves would have done, or would prefer, is legally irrelevant and will be of little assistance to the Court⁷.

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⁶ Such evidence was adduced and accepted by the Court in *Lehman v ExxonMobil*: see paragraph [336].

⁷ See, for example, *Lehman v ExxonMobil* at paragraphs [330] and [331] and *LBI EHF v Raiffeisen* at paragraph [28].

Contractual interpretation post-*Arnold v Britton*

The decision of the English Supreme Court in *Arnold v Britton* [2015] UKSC 36 was widely viewed as marking a shift to a more literal interpretation of contracts and away from the purposive or commercial approach adopted in *Re Sigma Finance* [2009] UKSC 2 and *Rainy Sky v Kookmin Bank* [2011] UKSC 50. Lord Neuberger stated in *Arnold v Britton* that “the reliance placed in some cases on commercial common sense and surrounding circumstances ... should not be invoked to undervalue the importance of the language of the provision which is to be construed.” In other words, Lord Neuberger sought to give greater weight to the words used in the contract (“the parties have control over the language they use in a contract”) and to deter the courts from re-writing agreements to reflect the courts view of commercial common sense.

This article examines some of the cases that have considered contractual interpretation since *Arnold v Britton*, to identify to what degree it has been followed.

In summary, it seems that the courts have attached more weight to the language chosen by the parties and generally settled on more literal interpretations of contracts. However, subsequent cases have, at least in theory, also heeded sections of the judgment stating that words should be read in their “documentary, factual and commercial context” and have noted that these other factors could

be of significant importance in an appropriate case. Moreover, the most recent decision of the Supreme Court, *Wood v Sureterm Direct Ltd* [2017] UKSC 24, sought to bridge the divide between literal and purposive approaches and cautioning against the suggestion that *Arnold v Britton* marked a departure from earlier practice.

Exsus Travel Ltd v Baker Tilly [2016] EWHC 2818 (Exsus)

Exsus, which concerned the interpretation of a standstill agreement, is a clear application of the more literal

approach to contractual interpretation. The issue arose in the context of a claim for professional negligence against auditors. Recital (B) of the standstill agreement provided that: “The purpose of the Agreement is to suspend the running of the applicable limitation period both in contract and tort in respect of the [relevant claims] for a period of 12 months from the date of this Agreement or any later date agreed in writing by the Parties or until this Agreement is terminated in accordance with its terms (the “Standstill Period”).”

The agreement did not contain any provisions permitting termination of the “Agreement”, but clause 3 did allow the parties to terminate the “Standstill Period” “at any time” on at least 28 days’ written notice.

The judge decided that the recital divided “clearly” into two parts: “(a) a period of 12 months from the date of this Agreement or any later date agreed in writing by the Parties” and “(b) until this Agreement is terminated in accordance with its terms”. The judge further held that the second part of Recital (B) must refer to the Standstill Period termination right, as although the drafting was “imprecise” this intention was “clear”. On the facts, the Standstill Period had not been extended or terminated early, so it expired 12 months after the agreement was made applicable to the claims.

The claimants had argued that the construction of Recital (B) was untenable when considered in its commercial and factual context, particularly because it was unrealistic for the claimant to commence proceedings within one year, due to other pending litigation. The judge stated that the claimant's construction was "not saved by reference to the factual matrix, partly because there is no need to depart from the natural meaning of the words".

MetLife Seguros De Retiro SA v JP Morgan Chase Bank [2016] EWCA Civ 1248

The judgment of Hamblen LJ in this case is another faithful application of *Arnold v Britton*, focusing primarily on the language selected then cross checking against the wider context and commerciality. The case concerned the final redemption amount payable by the issuer (JP Morgan) to a noteholder (MetLife). This amount was to be calculated based on a published Argentine inflation index (the CER) unless a so called CER Event occurred, in which case JP Morgan would calculate the amount payable in good faith and in a commercially reasonable manner.

One CER Event was that the "Republic of Argentina... takes any action which... prevents or has the effect of restricting or limiting (a) the calculation or (b) announcement of the CER or any of the values used to determine the CER". MetLife asserted that this CER Event had arisen because the Argentine government had manipulated the CER figures and the CER should be a genuine measure of inflation.

Hamblen LJ rejected MetLife's argument. His reasons included: (a) inserting a genuineness requirement

involved re-writing the contractual terms; (b) the wider contract supported the plain reading of the words – it suggested that use of the CER should be mechanical, not a process that required difficult judgments; and (c) the plain reading made commercial sense – investments such as these were often CER linked whereas linking investments to a "genuine measurement of inflation" was unknown in the market.

Lewison LJ reached the same conclusion as Hamblen LJ, although he viewed *Re Sigma Finance* as the relevant authority on the interpretation of financial instruments and considered that it had "not been overtaken" by *Arnold v Britton*. Lewison LJ highlighted passages from *Re Sigma Finance* supporting a contextualised approach and stated that the "documentary context" is of "critical importance". This may represent a slight shift in the weight to attribute to the various factors applied when interpreting provisions, at least in the context of complex financial instruments, and has been echoed by the Supreme Court in the *BNY Mellon* case (discussed below). It is also, however, potentially significant for its endorsement of *Re Sigma Finance*, which may re-open the door to purposive interpretation arguments in the future.

BNY Mellon Corporate Trustee Services v LBG Capital No.1 Plc [2016] UKSC 29 (BNY Mellon)

In *BNY Mellon*, the Supreme Court confirmed that LBG could redeem certain contingent convertible notes issued in 2009 as part of a capital raising programme. The redemption trigger included in the documentation had been anchored to a concept (capital tierings) which was later

superseded, so that the clause could no longer be triggered. The Supreme Court held that a dynamic definition should be substituted, as this was an obvious mistake by the parties and it was clear how it could be corrected.

The judgment emphasised the wider documentary context as a factor when interpreting complex financial instruments. It also acknowledged the need to understand the commercial purpose of the instruments and the "general thrust" of background market conditions in order to interpret them. Although this case can be distinguished from *Arnold v Britton* as here it was held that there was a clear drafting mistake, it can also be viewed as a triumph of commercial common sense. It will be interesting to see if this could perhaps be used to reposition the balance of the relevant factors in a suitable future case on contractual interpretation.

Wood v Sureterm Direct Ltd [2017] UKSC 24

In this recent case, the Supreme Court appears to have confirmed that the cases applying *Arnold v Britton* in the lower courts discussed above have taken the correct approach. However, in a unanimous decision the Supreme Court stated that *Arnold v Britton* did not in fact mark a departure from the approach in *Rainy Sky*. Rather, the two cases were essentially saying the same thing.

The case concerned whether liability for past mis-selling was recoverable under an imprecise and "opaque" indemnity in an SPA. The indemnity required the Seller to indemnify the Buyer against a comprehensive list of events arising out of "claims or complaints registered with the [company's regulator]... against the company". The Seller argued that it did not have to indemnify the Buyer

because the company had reported itself to the regulator, so there was no complaint against it.

Although the Supreme Court considered the indemnity in its contractual and commercial context, it concluded that the interpretative tool of “principal” importance was still a “careful examination of the language”. The Supreme Court adopted the literal interpretation of the indemnity advanced by the Seller and disregarded what many would have understood to be the parties’ commercial intention in agreeing such an indemnity.

Lord Hodge noted that it has long been accepted that interpretation is not a purely “literalist exercise focused solely on... the wording” but requires consideration of the contract as a whole, the wider context, business common sense and the commercial purpose. According to Lord Hodge, the amount of weight attributed to each of these factors depends on the context. The Supreme Court expressly acknowledged that some contracts may need to be interpreted with “greater emphasis” on their factual matrix and commercial purpose for reasons such as informality, brevity, differing drafting practises, deadline pressures and failures of communication.

Looking to the future

It now seems clear that although *Arnold v Britton* positioned language as a crucial factor when interpreting contracts, other factors, such as the documentary and commercial context, should also still be taken into account and in an appropriate case may be of significant importance. Understood in this light, subsequent cases have followed the judgment in both their statements of the relevant test and in their application, largely

settling on language driven, or literal, interpretations.

However, the Supreme Court is due for a significant changing of the guard over the next two years. Half of all the Supreme Court justices will have changed between mid-2016 and the end of 2018, including Lords Neuberger and Sumption, who are widely regarded as the strongest supporters of freedom of contract and a more literal interpretation of contracts. It will be interesting to see if their successors, perhaps drawing on the spirit of decisions such as the *BNY Mellon* case, move away from the present trend for literalism and adopt a greater willingness to use contractual interpretation as a tool to rewrite parties’ bargains in appropriate cases.

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Privilege and the “client” in *The RBS Rights Issue Litigation* [2016] EWHC 3161 (Ch) – UK and US perspectives

In a judgment handed down in December 2016, the English High Court has held that notes of interviews with current and former employees of a corporation as part of an investigation by in-house and external lawyers are not privileged as a matter of English law. The Court also confirmed that English privilege rules should be applied in cases before the English court so that, even though the interview notes were likely to have been privileged as a matter of US law, they were not privileged as a matter of English law.

This decision does not change the position under English law, but it nevertheless provides an important illustration of legal advice privilege under English law and, in particular, the need to appreciate who is the “client” on an ongoing basis. In addition, the case provides a stark reminder of the complexities surrounding privilege in cross-border litigation and investigations and the need to consider the privilege rules not only in the jurisdiction in which a party is currently engaged, but also the jurisdictions where proceedings or regulatory investigations may subsequently be commenced.

Background

This issue arose within proceedings known as *The RBS Rights Issue Litigation* in which the claimant shareholders of the Royal Bank of Scotland (RBS) are seeking to recover investment losses incurred further to the collapse of RBS shares on the grounds that the prospectus for the 2008 rights issue of shares in RBS was not accurate or complete. As part of this ongoing litigation the claimants sought disclosure and inspection of interview notes in relation to two internal investigations involving interviews by or on behalf of RBS (involving in-house, US and UK lawyers, as well as the RBS Group Secretariat (the Secretariat), consisting of non-lawyers) with current and former employees. One of these investigations had arisen in response to subpoenas by the US Securities and

Exchange Commission relating to RBS’s sub-prime exposures.

RBS attempted to resist disclosure of the interview notes on the grounds that

- The interview notes were subject to legal advice privilege.
- Apart from the interview notes taken by the Secretariat, the interview notes constituted lawyers’ privileged working papers.
- The English court should apply US federal law under which the interview notes were said to be privileged.
- Even if English law governs the question of privilege, the English court should exercise its discretion to withhold the documents on the basis that they were privileged under US law.

Legal advice privilege

The leading English authority on legal advice privilege is the Court of Appeal’s decision *Three Rivers (No 5)*¹, where it was held that the “client” for the purposes of legal advice privilege was the three-man Bingham Inquiry Unit set up to deal with certain legal

¹ *Three Rivers District Council and others v Governor and Company of the Bank of England (No 5)* [2003] QB 1556.

issues and that information gathered from employees outside this unit was no different for legal advice privilege purposes from information obtained from third parties.

In the present case, RBS claimed that the interview notes were protected by legal advice privilege on the basis that they recorded a communication between a lawyer and a person authorised by RBS (including current and former employees) to communicate with the lawyers for the purpose of RBS seeking legal advice. In what the Court considered to be “the fundamental and most powerful part of RBS’s case”, RBS submitted that it was not contrary to *Three Rivers (No 5)* that where an individual, with the authority of a corporation which is seeking legal advice, communicates to the corporation’s legal advisers at their request either instructions or factual information in confidence and for the purpose of enabling that corporation to seek or receive legal advice, that communication (including any factual information) should be treated as if the individual were part or an emanation of the client and protected by legal advice privilege accordingly. RBS contended that such treatment is necessary in order to fulfil the purpose of the protection afforded by legal advice privilege. Further, RBS sought to distinguish *Three Rivers (No 5)* on the basis that it concerned “internal” preparatory documents created by employees to send to the lawyers and not direct communications between such employees and the lawyers. RBS also pointed to academic criticism of the case and its disapproval in other jurisdictions, in particular the Court of Appeal in Singapore.

The claimants countered that legal advice privilege only covers communications between a client (narrowly defined) and his lawyer for the purpose of the lawyer giving and that client seeking or receiving legal

advice and that the gathering and communication of information by a person who is not strictly the client (even if they are an employee of the client) is not protected by privilege even if carried out at the request of the client and/or its lawyers.

The High Court acknowledged that *Three Rivers (No 5)* was a “controversial decision”, but found that it was nevertheless bound by it. The Court held that although the interview notes recorded direct communications with RBS’s lawyers, they comprised information gathered from employees or former employees preparatory to and for the purpose of enabling RBS, through its directors or other persons authorised to do so on its behalf, to seek and receive legal advice.

In other words, the RBS employees and former employees who were interviewed by the legal team did not fall within the narrow definition of “client” as defined in *Three Rivers (No 5)* and therefore the communications were not covered by legal advice privilege.

Lawyers’ working papers

It is generally accepted under English law that lawyers’ working papers are privileged under the legal professional privilege doctrine on the basis that they provide a “clue” to the lawyers’ advice or reveal the “trend of advice” which the lawyer is giving. For this reason, it may be difficult to show that verbatim transcripts of non-privileged interviews are privileged, even if the notes are taken by a lawyer. The Court noted, in this regard, that an interview note which recorded the lawyer’s own thoughts and comments on what he was recording with a view to advising the client would almost certainly be privileged.

However, the Court considered that the question was ultimately evidential and, on the facts, RBS’s evidence did not go far enough to substantiate the claim to privilege on the basis of lawyers’ working papers. It was not enough simply to say that the interview notes were not verbatim and that therefore they must contain legal input or selection justifying the claim to privilege. Although the interview notes were said to reflect the lawyers’ mental impressions, this was not supported by any assertion that the notes did in fact contain material that would or could reveal the trend of the legal advice – and the Court did not consider that it would be proportionate or appropriate in the circumstances to permit RBS to supplement its evidence given that the matter had already been argued out.

Applicable law

RBS contended that US federal law should apply on the basis that it was the jurisdiction with which the engagement or instructions, pursuant to which the communications arose and the interview notes came into question, was most closely connected.

The Court was not unsympathetic to RBS’s submissions, but it held that there was no sufficient basis for disturbing what was considered to be the well-established convention or practice of the English court of applying the law of the forum to determine whether or not a particular communication or document was privileged – in this case, English law.



Discretion

The Court recognised that it had a discretion whether or not to order production where a party resisted disclosure of documents, but the Court made clear that it was likely to lean heavily in favour of disclosure unless there were “compelling grounds” or a “special case” to take a different approach (such as the risk of violence, intimidation, interference with witnesses or destruction of evidence). It did not find such grounds in this case.

What does this mean in practice?

The decision is significant for all corporates involved in cross-border investigations and litigation. It is an important reminder that under English law what is privileged in one jurisdiction will not necessarily be

privileged in another, and that the status of interview notes and other potentially sensitive documents will ultimately depend on the law of the forum where the question of privilege is being addressed.

It confirms that, in cases involving legal advice privilege, English courts of first instance will continue to be bound by the narrow definition of “client” in the *Three Rivers (No 5)* decision of the Court of Appeal which, for now, remains good law – albeit that the judge in this case seemed to have sympathy with RBS’s position and acknowledged that *Three Rivers (No 5)* is controversial.

For now, therefore, it remains vital to consider carefully who the “client” is in each case both at the outset and as the matter develops. Indeed, the judge also noted that in a corporate context it may be that only individuals

singly or together constituting part of the “directing mind and will” of the corporation can be treated as being, or being a qualifying emanation of, the “client” for the purposes of legal advice privilege. However, as RBS submitted, this would restrict the scope of legal advice privilege available to corporate bodies yet further and go beyond the findings in *Three Rivers (No 5)*. It would also introduce a significant burden on lawyers to ensure that they took their instructions from and gave their advice only to those individuals constituting the “directing mind and will” of the corporate client, with ample scope for dispute around who those individuals actually were. In practice, it only re-emphasises the need for careful scrutiny of the position on an ongoing basis.

On the other hand, some reassurance can perhaps be taken from the judge’s view that interview notes recording the

lawyer’s own thoughts and comments with a view to advising the client would almost certainly be privileged – provided that, when challenged, a party can demonstrate some attribute of or addition to the interview notes which distinguishes them from verbatim transcripts by revealing or at least giving a clue as to the trend of legal advice being given.

In any event, the judge made clear that it “may be that in a suitable case the Supreme Court will have to revisit the decision”. However, although the judge granted RBS permission to appeal directly to the Supreme Court, rather than having to go through the Court of Appeal, there are no longer plans to appeal this case to the Supreme Court. It therefore remains to be seen whether there will be another opportunity for *Three Rivers (No 5)* to be overturned and a wider definition of “client” for the purposes of legal advice privilege to prevail.

Although RBS did not claim litigation privilege at first instance, it would also be helpful for the Supreme Court to address and provide direction on when an investigation becomes sufficiently adversarial or confrontational to constitute litigation for litigation privilege purposes, as this also remains a grey area under English law.

Until then, English privilege law remains unchanged.

The US perspective

Practitioners who are accustomed to the jurisprudence surrounding privilege under US law may be surprised by the limitations that the English courts in the *RBS* and *Three Rivers (No 5)* decisions placed on the application of privilege.

Notes and Memoranda of Witness Interviews

US courts have not been as restrictive as the English courts in their definition of the “client” in the corporate context. In *Upjohn Co. v United States*, the US Supreme Court made clear that the corporate “client” can extend beyond the control group (i.e. those individuals responsible for giving instructions to the lawyer and receiving the lawyer’s advice) so as to provide attorney-client privilege protection to a lawyer’s communications with employees who are not members of the control group. Specifically, the court held that employee communications are protected by the corporate privilege if (1) they are made to counsel at the direction of company superiors; (2) they concern matters within the scope of the employees’ in-house duties; (3) the information is not available from upper-level management; (4) the employee was made aware that he or she was being questioned in order for the company to receive legal advice; and (5) the communication was ordered to be kept confidential and remained confidential.

Given that the attorney-client privilege in the United States extends to employees who fall outside of the control group, the contents of interviews with those employees will typically be protected by the privilege. Companies have, therefore, been successful in resisting disclosure of interview memoranda on the basis of attorney-client privilege with such individuals. Companies have also been successful in resisting disclosure of interview memoranda under the work product doctrine.

The courts in the United States have been somewhat divided about whether the attorney-client privilege in the corporate context extends to communications with former

employees.² While a number of courts have found that communications with former employees are privileged so long as the communication is limited to knowledge that the former employee acquired during the course of his or her employment, other courts have found that counsel’s communications with a former employee of the client corporation should be treated no differently from communications with any other third-party fact witnesses. The takeaway, though, is that attorneys’ notes of communications with former employees are likely to receive less protection before the US courts than notes of communications with current employees.

Applicable privilege law

US courts may have taken a different approach to the applicable privilege law than the English court in the *RBS* case. Unlike in the *RBS* case, a US federal court would likely not apply the law of the forum in order to determine issues of privilege. Instead, a US federal court would be more likely to apply the law of the jurisdiction in which the communication was made, provided that that jurisdiction had the most direct and compelling interest in the question and that its law was not contrary to the public policy of the forum. In the case of the notes at issue in the *RBS* case, a US court would have been more likely to agree with *RBS* that it should apply US privilege law given the interviews’ connection with a US investigation and the fact that a number of the interviews occurred in the United States.

² In his concurrence in *Upjohn*, Chief Justice Burger offered his opinion that “a communication is privileged when, as here, an employee or former employee speaks at the direction of the management with an attorney regarding conduct or proposed conduct within the scope of employment.”

Key practical considerations

The RBS case highlights the following key takeaways for practitioners involved in an investigation

- Where English law may apply to the investigation, carefully consider who the “client” would be, as communications with individuals other than those constituting the “client” may ultimately be disclosable.
- Consider whether claims or investigations could arise in jurisdictions other than that in which the original investigation is occurring. If cross-border conduct is involved, other jurisdictions may apply their own privilege law to the relevant claim/investigation material. If privilege does not apply in these other jurisdictions, the material may have to be disclosed, which may affect whether or not privilege can continue to be claimed in other jurisdictions.
- Remember that it will be more difficult to withhold lawyers’ notes of interviews with individuals who do not form part of the “client”. In the US, for work product purposes, interview notes should not merely state that they contain attorney mental impressions and advice but should appreciably contain such impressions and advice. In addition, if the privilege is challenged, the practitioner should be able generically to describe in sufficient detail the types of observations and impressions contained within the document and how the attorney’s thoughts, impressions, or trend of advice could be deduced by the content or omission of content

from the writing. In the UK, such interview notes will only be privileged so long as they give a “clue” as to the lawyers’ advice or reveal the “trend of advice” which the lawyer is giving. Again, it will not be enough to argue that the notes reflect the lawyer’s mental impressions: it must be possible to assert that the notes did in fact contain material that would or could reveal the trend of the legal advice.

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UK Court of Appeal allows data subject access requests to be made in furtherance of litigation

Under the UK Data Protection Act 1998 (DPA), data subjects have rights to obtain copies of their personal information through a data subject access request (DSAR). Data subjects frequently use DSARs to obtain information in the context of non-data protection disputes with data controllers. There has been much controversy over this practice, particularly as the £10 maximum fee the data controller may charge can dwarf the cost of complying with the request, and two relevant Court of Appeal decisions.

On February 16, 2017 in *Dawson-Damer v Taylor Wessing LLP* [2017] EWCA Civ 74, the English Court of Appeal ordered a law firm, Taylor Wessing LLP (TW), to comply with the Appellants' DSARs. TW were the English solicitors to Grampian Trust Company Limited (Grampian), a Bahamian sole trustee of a discretionary trust of which Ms Dawson-Damer was a beneficiary. Grampian made certain substantial payments of funds from the trust which Ms Dawson-Damer and her children challenged as invalid, submitting DSARs for copies of all personal data held on them by TW. The claimants subsequently brought proceedings in the Bahamas challenging the validity of Grampian's payments, and sought from the English court (i) declarations that TW had failed to comply with their DSARs; and (ii) orders requiring them to comply.

On March 3, 2017 the Court of Appeal handed down judgment in the joint hearing of *Ittihadieh v Cheyne Gardens & Ors* and *Deer v University of Oxford* [2017] EWCA Civ 121. In *Ittihadieh* a resident disputed the response provided to their DSAR by the residential management company responsible for their building. *Deer* related to a DSAR made against the data subject's former employer, in the context of Employment Tribunal proceedings.

In this article we cover the key issues considered by the Court of Appeal in both of these judgments, namely

- Whether the court can use its discretion not to compel compliance with a DSAR made in furtherance of litigation.
- What amounts to "disproportionate effort" under the DPA.

- The extent of the DPA's legal professional privilege exemption.

DSARs made in furtherance of litigation and the court's discretion

The Court of Appeal in *Dawson-Damer* considered whether a court can use its discretion under section 7(9) of the DPA not to compel compliance with a DSAR where the data subject's real motive is to use the personal data to assist in litigation. Overturning the first-instance decision that data subjects could not use DSARs as a tool to obtain documents to assist with litigation proceedings as this was not a "proper purpose", the Court of Appeal rejected the notion that the court's discretion should be limited based on the underlying purpose of the DSAR. As the DPA does not limit the purposes for which a DSAR may be made, the Court of Appeal concluded that it would be "odd" to conclude that the sole purpose of a DSAR must be to verify the accuracy of the data subject's personal data. Such a "no other purpose" rule would have undesirable consequences, such as non-compliance by data controllers on the basis that the data subject had an ulterior motive for making the DSAR and satellite litigation to determine the purpose of the DSAR. Provided that a DSAR did not amount to an abuse of the court's process (which the court noted the mere holding of a collateral purpose

would not normally give rise to) or result in a conflict of interest, the court could not use the purpose of a DSAR as a reason to limit the exercise of its discretion to compel a data controller to respond under section 7(9) DPA.

In *Ittihadieh and Deer* the Court decided that although the underlying purpose of a DSAR is for the data subject to check the accuracy of their personal data and to see if it is being processed lawfully, the right of access is not subject to “any express purpose or motive test.” Following *Dawson-Damer*, it was held that the fact the data subject may have “collateral purposes”, such as litigation, when making the DSAR will neither invalidate it nor relieve data controllers from their obligation to respond. Unlike *Dawson-Damer*, however, the Court of Appeal in this judgment indicated that the data subject must also wish to check the accuracy of their personal data for the request to be valid, effectively emphasising the “collateral” nature of any additional litigation purpose.

In terms of the court’s discretion to order a data controller to respond, *Ittihadieh and Deer* cited a number of factors which the court may take into account, including

- Whether there is a more appropriate route to obtaining the requested information, such as disclosure in legal proceedings.
- The nature and gravity of the data controller’s breach.
- The absence of a legitimate reason for the DSAR (even though a collateral purpose of assisting in litigation is not an absolute bar).
- Where the application is an abuse of rights, for example where litigation is pursued merely to impose a burden on the data controller.

- Where the personal data is of no real value to the data subject.
- The potential benefit to the data subject.
- Whether or not the data subject was the author or recipient of the document in question.

However, in the absence of any of these factors, where it is clear that the data subject legitimately wishes to check the accuracy of his or her personal data, or simply provided that a DSAR is submitted in a valid form (namely a request made in writing – including via email or social media), that is a good enough reason for the court to exercise its discretion in the data subject’s favour.

What amounts to disproportionate effort?

In *Dawson-Damer*, the Court of Appeal examined whether TW was justified in refusing to search for documents across 30 years of client files on the basis that it would involve disproportionate effort for the purposes of section 8(2) of the DPA. Here, noting that the first-instance decision had erroneously determined the scope of documents protected by legal professional privilege as addressed below, the Court of Appeal found that, to date, TW had done no more than review their files; they had produced no evidence to show what they had done to identify personal data or that it would involve disproportionate effort to take any further steps to do so. Thus, the mere assertion that it would be too difficult to search through voluminous papers was not enough to justify TW’s reliance on the section 8(2) exemption. The Court of Appeal did, however, indicate in this case that the “disproportionate effort” test applies to the search as well as the mere supply of copies of the results

(which widens the exemption beyond the UK Information Commissioner’s current guidance).

In *Ittihadieh and Deer* it was noted that there is no express provision of the DPA which relieves a data controller from the obligation to supply personal data on the ground that it would be disproportionate to do so. However, while the principle of proportionality cannot justify a blanket refusal to comply with a SAR, it was held that it does limit the scope of the efforts that a data controller must take in response. Going further than *Dawson-Damer*, the Court of Appeal held that the “obligation to search is limited to a reasonable and proportionate search”, and is not an “obligation to leave no stone unturned”. Consequently, the result of a search does not necessarily mean that every item of personal data relating to an individual will be retrieved as a result of a search. “There may be things lurking beneath another stone which has not been turned over”, and the mere fact that a further and more extensive search reveals further personal data relating to the data subject does not necessarily mean that the first search was inadequate.

The extent of the legal professional privilege exemption

In *Dawson-Damer*, TW responded with a blanket claim of privilege based on the legal professional privilege exemption to the production of personal information under the DPA. TW also argued that, in circumstances where they had been Grampian’s lawyers for some thirty years, it was neither reasonable nor proportionate for them to carry out a full search to determine whether a particular document was covered by privilege. At first instance, the judge held that the legal professional privilege exemption



covered all documents that Grampian would be entitled to withhold in the Bahamian proceedings. It was therefore not reasonable or proportionate to expect TW to carry out any search for personal data or to determine which documents were privileged as this was a matter of Bahamian law that would be time-consuming and costly to resolve.

Again reversing the first instance approach, the Court of Appeal in *Dawson-Damer* took a narrow approach to the legal professional privilege exemption in paragraph 10 of schedule 7 of the DPA, holding that it only applies to documents protected by legal professional privilege as a matter of English law in the context of legal proceedings in the UK. Furthermore, the exemption did not extend to documents that are subject to a right of non-disclosure (such as certain documents that are not disclosable

to a beneficiary under trust law), but which are not also protected by legal professional privilege. This latter point does not come as a surprise as the DPA expressly states that DSAR rights apply notwithstanding any rule of law prohibiting disclosure other than where covered by an exemption.

In *Ittihadieh and Deer* the Court confirmed there is no obligation to search for material covered by legal professional privilege, although a data controller will be expected to conduct a proportionate search to identify and separate out any non-privileged personal data.

Comment

Although the Court of Appeal in *Ittihadieh and Deer* cited *Dawson-Damer* as the leading authority on a number of key DSAR principles, in many ways

this later judgment has opened the door to further arguments which data controllers might potentially use to counter data subject access requests which appear particularly onerous and unreasonable.

On the one hand, the Court of Appeal's decision in *Dawson-Damer*, influenced in large part by the intervention of the Information Commissioner, dashes hopes and signals "business as usual" to data controllers faced with DSARs in the UK. As the Information Commissioner submitted, "The cost of compliance is the price data controllers pay for processing data". The decision confirms not only that the legal professional privilege exemption will be narrowly construed, but also that data controllers cannot avoid compliance by arguing that responding would be expensive or time-consuming – albeit that the ruling does enable data controllers to argue that the

“disproportionate effort” exemption applies to the search process as well as to the supply of data. This decision has also made clear that a data controller cannot refuse to comply with a DSAR based on a data subject’s alleged ‘real motive’, not least to avoid the risk of satellite litigation to determine the motive for a DSAR in the first place.

On the other hand, although the Court of Appeal’s latest judgment in *Ittihadieh* and *Deer* follows *Dawson-Damer* in a number of key aspects, it does appear to give more comfort to data controllers in various ways, including that data subjects should be able to show a legitimate reason for making the DSAR (even if there is also a collateral purpose); that the principle of proportionality does limit the scope of the efforts that a data controller must make in response and does not oblige data controllers to leave no stone unturned; and that the court will take the broader factual matrix into account when deciding whether or not to use its discretion to compel a data controller to respond to a DSAR.

Ittihadieh and *Deer* also sends a warning to data subjects on costs. In this case, the costs award in *Deer*’s favour was reduced at first instance by 25% because of the judge’s assessment of her motive in pursuing the litigation as “essentially antagonistic”. The Court of Appeal agreed with this approach, citing CPR Part 44.2(4)(a) which requires the court to take into account a party’s conduct in deciding what order to make about costs. In this case, balancing what *Deer* had achieved against the cost involved (disclosure of 33 further documents following a review of over 500,000 documents at a cost to Oxford University of £116,116), coupled with *Deer*’s overall conduct, the Court of Appeal found that the judge had been entitled to deduct costs as he did.

Thus, at least for now (and potentially also under the General Data Protection Regulation, which envisages the possibility of data controllers refusing to act on a “manifestly unfounded or excessive” request), data controllers may have new grounds to argue against complying with unreasonable requests, or broad requests for all personal data held about a particular individual, which cause the largest burden on data controllers.

The GDPR will prohibit data controllers from charging a fee to respond to data subject requests, shorten response time frames from 40 to 30 days, provide harsher penalties for non-compliance, and likely increase the costs of complying with DSARs and the new data subject rights (data portability and right to be forgotten), particularly for those controllers holding large quantities of personal data about individuals. Although it remains to be seen whether courts will follow the harsher line in *Dawson-Damer* or the more lenient approach in *Ittihadieh* and *Deer*, at a minimum all EU data controllers should have a strategy for locating, searching for, and parsing data sets to comply with DSARs and the other new rights when the GDPR comes into effect in the UK in May 2018.

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Make me a SuperSAR: Criminal Finances Act 2017

The Criminal Finances Bill received Royal Assent on 27 April 2017. Its aim is to significantly improve the government’s ability to tackle money laundering and recover the proceeds of crime, and is considered the most significant development in the UK’s anti-money laundering laws since the introduction of the Bribery Act in 2010. This article will focus on the changes to information sharing in connection with the suspicious activity reports (SARs) regime, although we note there are a number of broader changes under the Act, including the introduction of unexplained wealth orders, disclosure orders for AML investigations and the corporate failure to prevent tax evasion.

Background

The Act has made several key amendments to the SARs regime: POCA regulated entities can now share information if certain conditions are met and the National Crime Agency (NCA) can extend the “moratorium period” that prevents dealing in property that is subject to a SAR by up to six months.

By way of background, SARs are reports which alert law enforcement agencies that certain client or customer activity is suspicious and might indicate money laundering or terrorist financing. Under the Proceeds of Crime Act 2002 (POCA) and the Terrorism Act 2000 persons in the regulated sector are

required to submit a SAR in relation to information that comes to them in the course of their business if they know, or suspect, or have reasonable grounds for knowing or suspecting, that a person is engaged in, or attempting, money laundering or terrorist financing.

Information sharing

The Act provides a new mechanism for information sharing between POCA regulated entities (e.g. banks and financial institutions) in relation to suspected money laundering. Under the Act, information can be shared either on the regulated entities’ own initiative or at the request of the NCA. The Act sets out the conditions under which such information sharing can

take place including that the required notification has been made to an NCA authorised officer. This notification will be treated as satisfying the requirements to make disclosures about suspected money laundering under ss 330 and 331 of POCA. The Act provides that a relevant disclosure, made in good faith by a regulated entity, will not breach any obligations of confidence owed by the person making the disclosure or any other restriction on the disclosure of information. This change is significant and responds to the concerns of many regulated entities about breaching confidentiality obligations by sharing their customers’ information.

Following the exchange of information, the Act provides for the information to be provided to the NCA in a joint disclosure report (otherwise known as a “super SAR”). The super SAR mechanism is intended to fulfil both entities’ reporting obligations and will obviate the need for multiple entities to submit SARs on the same subject matter.

The provision for the sharing of information between private entities builds on the work of the Joint Money Laundering Intelligence Taskforce (JMLIT). JMLIT was initially a twelve month pilot task force made up of UK and international banks, the British Bankers Association and law enforcement agencies. It has

been praised for demonstrating the benefits of information sharing to disrupt money laundering in the UK. Building on this success, the information sharing provisions in the Act aim to increase efficiency in reporting potential instances of money laundering. The amendment enables regulated entities to access more information prior to submitting their SAR (or super SAR) reports, allowing them to compile detailed intelligence about potential money laundering and to provide a more complete picture of the facts. There was hope from businesses in the regulated sector that the amendments would go further to reduce the reporting burden on them and remove the consent regime with an “intelligence-led approach”, but the proposal was not progressed for lack of a suitable alternative. The ultimate changes are more of a compromise with a view to better use of both public and private sector resources to fight money laundering.

Whilst the aims behind the amendments are clearly worthy, there are a number of uncertainties in the provisions which may result in regulated entities being reluctant to make use of the new mechanism. Whilst the Act gives regulated entities the ability to make an information sharing request, there is no obligation to do so. Without such an obligation it is difficult to predict how proactive regulated entities will be in requesting information from each other, rather than simply submitting a traditional SAR. The possibility of sharing information and submitting joint reports could be extremely useful to some entities, as long as their interests align, however it could prove problematic where entities are not in agreement as to whether a SAR needs to be submitted. The new option to request additional information also

creates a further administrative burden, a regulated entity must make both the required notification, and then the super SAR.

Extension of moratorium period

Under the Act, the NCA now has the ability to extend the “moratorium period” (i.e. the period pending consent from the NCA) that prevents dealing in property subject to a SAR by up to six months. The maximum moratorium period under the previous regime was 31 days. In order for the moratorium period to be extended, there must be an application by a senior officer (i.e. a member of the police, HMRC or NCA) to the Crown Court. The Court can only grant an extension where an investigation is ongoing, is being conducted diligently and expeditiously, further time is needed to complete the investigation and such an extension is considered reasonable in all the circumstances.

While the potential to increase the moratorium period by up to six months may raise concerns for time critical, or high value, transactions, under the previous regime the NCA often found that 31 days was not a long enough period to carry out a thorough and diligent investigation. The fact that the Act only allows for the moratorium period to be increased incrementally, by 31 day extensions, and a condition for the extension is that the ongoing investigation is being carried out “expeditiously”, should reduce the risk of unwarranted lengthy extensions. It should be noted that it is currently rare for the NCA to refuse consent and if this remains the case, the extended moratorium period should only impact a limited number of cases. In such cases, regulated entities will need

to continue to carefully consider the “tipping off” provisions under POCA when dealing with customers.

Looking Forward

The changes to the SAR regime are certainly positive from an information sharing perspective, but it remains to be seen how frequently these new provisions will be relied upon by businesses and the NCA alike, and how the uncertainties in the provisions will be dealt with in practice.

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Valuing a company's shares following unfair prejudice

Section 994 of the Companies Act 2006 provides protection for minority shareholders of a company where affairs of the company have been conducted in a manner which was unfairly prejudicial to their interests.

One of the remedies that a court may order on a successful unfair prejudice petition is for the purchase of shares. However, where such an order is made, how should the price of those shares be determined? This was the question before the Court of Appeal in the case of *Wann v Birkinshaw* [2017] EWCA Civ 84.

Background

The case concerned the shares in Quarry Walk Park Limited (the 'Company') which owned and operated a lodge park providing self-catering holiday accommodation close to Alton Towers. The Respondent, one of four equal shareholders, brought an unfair prejudice petition in respect of his alleged exclusion from the management of the Company.

Following the hearing of the unfair prejudice petition, the Appellants (the three other shareholders) had been ordered to purchase the Respondent's shares at "a fair value, being a rateable proportion of the total value of the Company as at 10 April 2013". Further, the purchase was to be on certain assumptions, including that: the company was a going concern; the parties were a willing vendor and willing purchasers operating at arm's length; and without any discount to the value of the shares because they were a minority shareholding. A single joint expert provided a valuation of £2.85 million

based on "multiple of earnings" or "profits" and which was said to reflect the trading potential of the business. The Judge accepted this valuation.

The Appellants argued that a deduction of £1.4 million should have been made from the £2.85 million to take into account the Company's net borrowings at the relevant time.

Court of Appeal

The Court of Appeal began by emphasising that such an order is for the purchase of shares in the company and not the company's assets. In the Court of Appeal's view, the phrase "the total value of the Company" had to be construed as a reference to the total value of the issued share capital of the company – and this meant the market value of the issued share capital. In the absence of a clear indication to the contrary, the "value" of the shares of a company, could refer only to the price that would be received for it on a sale.

On the facts, the critical question then arose of whether, in valuing the share capital of the company, a deduction should be made for the company's net borrowings of £1.4 million. In the view of the Court of Appeal, the company's net borrowings as at the valuation date should be taken into account. The expert evidence justified a conclusion that a price of £2.85 million on an earnings basis for the entire share capital would be reduced in the course of negotiation by half the net borrowings (£700,000) to arrive at a value of £2.15 million, giving a fair value for the Respondent's shares of £537,500.

Comment

The court hearing an unfair prejudice petition has a wide discretion in determining the valuation methodology. While the decision is very much based on the facts, the Court of Appeal has indicated that clear words will be required to value a company's share capital by something other than its market value.

It is therefore important for parties to give real thought to how the shareholding is to be valued, prior to the petition hearing, in the event that an order to purchase is granted.

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Agreement to agree – will it be enforceable?

In *Teekay Tankers v STX Offshore & Shipbuilding* [2017] EWHC 253 (Comm), the High Court considered whether an option agreement relating to the construction of oil tankers was void for uncertainty.

Facts

The Claimant, an oil tanker operator, entered into an option agreement with the Defendant, a shipbuilder. The agreement granted the Claimant three options, each in respect of an order of four tankers. It provided that, upon exercise of an option, delivery dates “shall be mutually agreed” between the parties, but the Defendant “will make best efforts to have a delivery” in 2016 for Option one tankers and in 2017 for Option Two and Three tankers. It also provided that within 10 days of exercise of an option, the parties would enter shipbuilding contracts. The parties and their subsidiaries also entered into other agreements, including four shipbuilding contracts, each in respect of an order of one tanker.

In around mid-2013, the Defendant entered into restructuring discussions with creditors.

The Claimant exercised ‘Option One’ by a letter dated 2 October 2013. However, no delivery dates were ultimately agreed and the parties did not enter into shipbuilding contracts in respect of the four tankers under the option.

The Claimant issued proceedings in April 2014. It contended that the Defendant had repudiated and renounced the option agreement and that it was entitled to and did terminate that agreement. It claimed damages for loss of profits. The Defendant contended that the option agreement was void due to uncertainty of its terms. It based on its argument on the wording “shall be mutually agreed”, contending that the contract failed because delivery dates, an essential matter, were not agreed between the parties and rather left to be agreed in the future. In other words, the option agreement was an unenforceable ‘agreement to agree’. It also argued alternatively, that it did not repudiate or renounce the option agreement.

The Claimant did not dispute that delivery dates were an essential matter. However, it argued that the parties could not have intended that the option agreement was non-binding and also that it contained an effective mechanism for determination of delivery dates, without the need for future agreement. The Claimant argued the latter point based on two alternate implied terms. Its primary case was the delivery date was the earliest date the Defendant offered using its best efforts in 2016 (Option One) or 2017

(Options Two and Three) and failing this, the earliest date it was able to offer using its best efforts. Alternatively, it argued that the delivery date was an objectively reasonable date having regard to the Defendant’s best efforts obligation, to be determined by the court if not agreed.

Judgment

The Commercial Court considered the principles on agreements to agree in the leading Court of Appeal authorities of *Mamidoil-Jetoil Greek Petroleum* and *B J Aviation*. A key principle arising from these decisions is that, if on a true construction of the contract, the parties have left an essential matter (such as price in a contract for the sale of goods or supply of services) to be agreed in the future, then the contract is likely to be unenforceable due to uncertainty. The decisions are also authority for the proposition that, where the court is satisfied that the parties intended that their bargain be enforceable, it should strive to give effect to that intention by construction or by the implication of a term. However, the implied term cannot be inconsistent with the court’s construction of the express terms of the contract.

The Commercial Court accepted the Claimant’s argument that the parties had intended to enter into a binding contract and therefore it should strive to give effect to the option agreement. It noted, among other matters, that

the option agreement was part of a ‘package’ of contracts and the consideration for the Defendant to grant the options included the Claimant’s subsidiaries entering into the shipbuilding contracts.

The Court then turned to the implied terms issue. It considered the leading authorities on implied terms, including *Marks and Spencer*, where the Supreme Court confirmed that an implied term should (to a reasonable reader at the time the contract was made) be so obvious as to go without saying, or to be necessary for business efficacy. The court held that, despite ‘striving to its utmost’, it was unable to imply either term. It held that the first, the ‘offer date’ implied term, would operate as a ‘unilateral’ contract scheme, i.e. the Claimant would be required to accept any delivery date that the Defendant was able to offer using its best efforts. This scheme would be inconsistent with the provision of the option agreement which provided for delivery dates to be mutually agreed. It held that the second, the ‘reasonable date’ implied term, would be inconsistent with the Defendant’s obligation to “make best efforts” to deliver within 2016 or 2017.

The Court noted the distinction between on the one hand, an agreement to use best efforts to achieve a particular result and on the other hand, an agreement to use best efforts to reach agreement on an essential term in a contract. It held that the option agreement fell into the latter category. It also briefly commented on the nature of an ‘essential matter’. In the case of *MRI Trading* a shipping schedule had been left to be agreed between the parties; the Court of Appeal upheld an implied term that the shipping schedule would be reasonable. The Commercial Court distinguished this case on the basis that a shipping schedule was a ‘matter of routine’, and also that in *MRI Trading*, shipping schedules had

been agreed in each of the previous two years (i.e. were readily assessable). It held that in contrast, in this case, delivery dates were an essential matter and not readily assessable, as no criteria had been specified and there were many relevant considerations to agreeing a delivery date.

Accordingly, the Commercial Court held that although the parties intended the option agreement to be binding, it was not enforceable owing to uncertainty, as an essential matter, delivery dates, were not agreed and left for future agreement between the parties. The court also held that, had it not reached this finding, it would have found that the Defendant’s conduct amounted to a renunciation of the contract and that it was liable to the Claimant.

Comment

This decision is an illustration that, where an essential matter in a contract is left by the parties to be agreed in the future, there is a risk that if a dispute arises, the contract will be held to be unenforceable. It is notable that in this case, the court found that the parties had intended that the contract be enforceable and that it should aim to uphold their bargain, but nevertheless was unable to do so. A key commercial term of the transaction is likely to be an essential matter, such as price, or delivery dates in this case.

Practically speaking, to minimise this risk, where flexibility is required and an important commercial term cannot be fixed at the time the contract is entered into, the parties should include provisions which operate in default of agreement between the parties.

The case is also a reminder that the courts will be slow to imply terms into a contract where they can be construed to be inconsistent with an existing contractual scheme, even if necessary

to give effect to the parties’ intention that the contract be enforceable.

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The impact of currency fluctuations on the costs of litigation

World currency markets have seen significant currency fluctuations in recent months, in particular following the result of the UK's referendum on its membership of the EU. While the most immediate impact of this will be felt by corporates in relation to international trade, it is also of considerable significance to cross-border litigation. Businesses across the world regularly choose the English courts to settle disputes with many cases in the Commercial Court involving at least one foreign party.

Months or years may pass between a breach of contract giving rise to loss and the claimant being awarded a judgment during which time exchange rates may change considerably. English procedural law provides mechanisms to protect a litigant in the English court against this risk – most obviously a claim may be brought in a foreign currency (the currency of the contract) and the court has power to award judgment in that currency.

The position regarding costs and currency fluctuations is less clear. However, for foreign parties who pay their lawyers in Pounds sterling, the point is no less relevant. As with any litigation, many months may pass between a party incurring legal costs and the court making a costs order for that party to recover all or part of its costs from the other side.

In two recent cases, it has been argued that costs orders should include an order for an additional sum which reflects any currency loss caused by the decline in the exchange rate between the Pound and the Euro since any payments of costs were made to the party's lawyers and the court's order for costs.

The first case was *Elkamet Kunststofftechnik v Saint-Gobain Glass France* [2016] EWHC 3421 (Pat), in which the issue was described as a 'novel point' by Arnold J. The claimant, a German company, had to exchange Euros into sterling in order to pay its lawyers throughout the litigation. By the time that a costs order was made in favour of the claimant at the conclusion of the claim, the amount payable to the claimant in sterling was worth a lot less when converted back into Euros. Accordingly, the claimant argued that it should be compensated for the

additional cost it incurred as a result of exchange rate losses.

Arnold J ordered a payment of £20,000 to reflect the currency loss suffered as a result of movement in the exchange rate between sterling and Euros since proceedings began and, in particular, following the referendum result on 23 June 2016. It was also notable in that case that the defendant, a French company, declined the option of a costs order in Euros.

Arnold J accepted the claimant's argument that the purpose of a costs order was to put the receiving party back into the position it would have been in had it not had to spend the costs to which the order relates. In this regard the Judge also noted the court's power to award interest on costs which is often exercised. Accordingly, if a foreign company has had to exchange its local currency into Pounds for the purpose of meeting the costs of litigation, it should be compensated for additional expenditure as a result of currency fluctuations in the same way it is entitled to be compensated for being kept out of its money by way of interest.

In doing so, Arnold J rejected that defendant's arguments that as a matter of principle, the purpose of an order for costs is to compensate a party for costs incurred in litigating in the jurisdiction and should therefore be in Pounds



irrespective of the source of the funds. The Judge had more sympathy with the defendant's reference to practical considerations: namely that exchange rates can go up as well as down, and that satellite litigation in respect of such matters should be discouraged. Nevertheless, he was prepared to order a sum of £20,000 in respect of exchange rate fluctuations.

In contrast, in the case of *MacInnes v Gross* [2017] EWHC 127 (QB), a little over two months later, Coulson J took the opposite view and declined to follow the decision in *Elkamet*. While this involved a hearing as to the principle of costs rather than a summary assessment as in *Elkamet*, Coulson J nevertheless departed from Arnold J's reasoning. In particular, he was doubtful of the proposition that an award of costs should be treated as an order for compensation, as if it were a claim for damages. In his view "there are inherent differences between

the two regimes, and that orders for costs have never been regarded as compensating the payee for the actual costs that he has paid out. On the contrary, unless the payee has an order in his favour for indemnity costs, he will never recover the actual costs that he has incurred". Finally, Coulson J did not "see the close analogy between ordering interest on costs, which is commonplace, and ordering exchange rate losses due to the particular time that the costs were paid, which is not. The paying party can work out in advance the additional risk created by the potential liability to pay interest on costs, but any potential liability to pay currency fluctuations is uncertain and wholly outside his control". He also commented that it could be argued that "the generous rate of interest on costs at 4% over base is designed to provide at least some protection to the payee against such events."

Where do these two decisions leave us? The differing approach is clearly unhelpful to parties and it may be that the conflict will need to be resolved by the Court of Appeal. Nevertheless, the decisions demonstrate that this is a live issue and is something parties will need to be aware of – whether as a point to raise, or as one to defend.

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