Arbitration - United Kingdom

Risk of confidential information misuse bars firm from acting further

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Introduction

Law firms can act against their former clients, but not in circumstances where they were given confidential information and where there is a real – not just theoretical or fanciful – risk that the information will be misused.

The recent High Court decision in *Georgian American Alloys, Inc v White & Case LLP*(1) concerned a law firm that acted against its former clients' owners in London Court of International Arbitration (LCIA) proceedings and High Court proceedings. The case illustrates the high evidential burden which law firms must discharge to show that there is no real risk of misuse of the confidential information received from their former clients.

Facts

In September 2010 a legal team at the defendant law firm advised Mr Pinchuk and a related entity in a dispute with Pinchuk's joint venturers, two businessmen who – like Pinchuk – were of Ukrainian origin. In April 2011 a different team at the law firm was asked to advise on a corporate restructuring of the claimant companies. The claimants' ultimate owners were Pinchuk's two joint venturers.

The law firm's conflicts search picked up that the Pinchuk team was advising on a matter potentially adverse to the joint venturers. However, the Pinchuk team had not heard from its clients for a number of months and believed that the dispute had been settled.

The restructuring team was engaged in May 2011. In the course of the engagement, the team became privy to information concerning the identity and location of the claimant companies' assets.

A year later, it emerged that Pinchuk's dispute with the joint venturers had not been settled after all. The Pinchuk team was instructed to recommence work, which included identifying the joint venturers' assets. The law firm issued proceedings on behalf of Pinchuk against the joint venturers in the High Court in March 2013. At this point, the law firm established ethical screens (also known as 'Chinese walls') between the Pinchuk team and the restructuring team.

In addition to the High Court proceedings, the law firm commenced LCIA arbitration proceedings on behalf of Pinchuk against the joint venturers and another businessman in August 2013. Pinchuk applied to obtain information from the claimant companies relevant to the LCIA arbitration proceedings in a US district court. The law firm confirmed that the applications were not based on any information supplied in relation to the restructuring, but on publicly available information.

Upon being served with the US application, the general counsel for a number of the claimant companies expressed concern to learn that the defendant law firm was acting for Pinchuk. In October 2013 the general counsel wrote to the law firm demanding that it cease acting for Pinchuk in both the High Court and the arbitration proceedings. The law firm refused to do so. The following month, the claimants issued proceedings seeking to restrain the law firm from continuing to act for Pinchuk.

The law firm conducted an internal investigation, which confirmed that none of the documents saved on its document system under the restructuring client number had

been accessed by any member of the Pinchuk team. With the exception of staff who had left the firm and could not be contacted, the staff working for Pinchuk were interviewed and confirmed that they had not discussed the restructuring with the restructuring team and – before being added to the ethical screen – had not been aware that the law firm advised on the restructuring at all.

The law firm ceased acting for Pinchuk in the LCIA arbitration in December 2013, but continued to act in the High Court litigation. The claimants' application for an injunction restraining the law firm from continuing to act was granted in January 2014.

Issues

In reaching its conclusion, the High Court confirmed well-established principles applicable to the granting of injunctions against a client's former solicitors.

Pre-conditions for obtaining injunction
The court held that where a claimant seeks to restrain its former solicitors from acting in a matter for another client, it must establish that:

- the solicitors possess information that is confidential to the claimant and to the disclosure of which the claimant has not consented; and
- the information is or might be relevant to the new matter in which the interest of the other client is or might be adverse to its own.

Although the burden of proof is on the claimant, it is not a heavy one.

The judge held that the claimants had satisfied both pre-conditions. The information imparted to the law firm about the joint venturers' assets and their interest in the claimant entities was confidential and the claimants had not consented to its disclosure. Moreover, the information was relevant to the court proceedings commenced by Pinchuk. The fact that the joint venturers – not the claimants – were parties to those proceedings made no difference to that conclusion. The claimants' interests were adversely affected by virtue of their ultimate owners' interests being adversely affected.

Degree of risk
Once the former client had established that the two pre-conditions had been satisfied, the evidential burden shifted to the defendant firm to show that, even so, there was no real risk that the information would come into the possession of those now acting for the other party. The risk of misuse had to be a real one – not merely fanciful or theoretical – but it did not have to be substantial.

The starting point was that, unless special measures are taken, information moves within a law firm. The law firm's internal investigation did not discharge the evidential burden on the law firm as to the risk of disclosure before the introduction of ethical screens. As to the investigation that the Pinchuk team had not accessed relevant documents, this did not preclude the possibility of oral disclosure. As to the confirmations obtained in interviews, the possibility remained that there had been inadvertent disclosure. The court also noted that no confirmations had been obtained from staff who had left the law firm or from the restructuring team.

The court concluded that the law firm had failed to discharge its evidential burden, and that there was a real risk that the confidential information had come into the possession of some of the Pinchuk team before the ethical screens were set up. Accordingly, use of that information (at least inadvertently) would be made in the High Court action against the joint venturers.

Relevance of ethical screens
Unless the court is satisfied on the basis of clear and convincing evidence that effective – not merely all reasonable – measures have been taken to ensure that no disclosure would occur, the injunction should be granted. An effective ethical screen must be an established part of the organisational structure of the firm, not created *ad hoc* and dependent on the acceptance of evidence sworn for the purpose by members of staff engaged on the relevant work.

The claimants' confidential information was provided to the restructuring team from May 2011 onwards. From May 2012, the Pinchuk team began to evaluate claims against the joint venturers. However, no measures of any sort to avoid the passing of the claimants' information were put in place until the establishment of the ethical screens in March 2013. As such, they were not an established part of the organisational structure of the firm.

Relevance of prejudice to Pinchuk
Counsel for Pinchuk argued that he would be gravely prejudiced if the injunction were granted. The defendant law firm was the firm of his choice and he had developed a close relationship with its solicitors.

The court gave this argument short shrift. Although an injunction was a discretionary

remedy, it did not follow that the court had to weigh the interests of the other client against the interests of the client that had otherwise satisfied the requirements for the grant of the injunction. Any impact on Pinchuk was not a relevant consideration.

Relevance of delay

The law firm argued that the claimants should have applied for the injunction earlier. Pinchuk commenced court proceedings against the joint venturers in March 2013, but the claimants waited until October 2013 before asking the law firm to cease acting for him.

The court disagreed. It concluded that it would not have been clear to a layman confronted with Pinchuk's particulars of claim that there was a risk that confidential information imparted during the restructuring might be used by Pinchuk against the joint venturers. It was only when the court proceedings were viewed in light of the allegations made in the LCIA arbitration proceedings – commenced in August 2013 – that the link to the information provided to the law firm in the course of the restructuring became clear.

The court indicated that if the law firm had informed the claimants in March 2013 that ethical screens had been established, the position with respect to its argument that the claimants had unduly delayed their application may well have been different. However, the law firm did not inform the claimants about the ethical screens, undermining any argument of undue delay.

Comment

The court's ruling is a reminder to law firms not only to put in place rigorous policies for the handling of conflict of interest policies, but also to ensure their implementation – including the notification of clients affected when ethical screens are established.

The standards set by the court for establishing effective ethical screens are high. Clients' relationships with shareholders or ultimate owners must be taken into consideration, and the ethical screens must be put in place early on.

Clients can – and should – enquire how their law firm handles conflicts of interest and remain vigilant as to the identity of any law firms instructed in proceedings against them or their affiliates. However, the onus to inform clients about conflicts of interest remains firmly on the law firm instructed.

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Endnotes

(1) [2014] EWHC 94 (Comm).