MEMORANDUM

TO: ANITA KUNDU - FRESHFIELDS BRUCKHAUS DERINGER

FROM: JAKE MOSES

SUBJECT: DISCLOSURE AND PRIVILEGE IN INTERNATIONAL ARBITRATION

DATE: 29 JULY 2009

Question Presented

Must XXX[1] produce the January and February 2006 YYY[2] preliminary reports and XXX's instructions to YYY as per items 6 and 7 of ZZZ's[3] document request?

Brief Answer

Probably. Explicit rules regarding privilege are nearly non-existent in the international arena. Rather, arbitrators tend to follow general principles of fairness, equality and reasonableness in determining the propriety of document requests. While the reports requested by ZZZ could conceivably be covered by legal or litigation privilege, various factors weigh against this possibility. Finally, concern must be given to negative inferences against XXX that may be drawn by the panel if an objection is made to evidence that should in fairness be disclosed.

Facts

XXX, a German and French consortium, brought a claim for Arbitration in Sweden under the International Chamber of Commerce ("ICC") rules against the Finnish group, ZZZ, to recover for damages suffered as a result of deficient excavation that ZZZ was contractually obligated to carry out in order to prepare a site (owned by ZZZ) for the construction by XXX of a nuclear power plant ("OL3"). After the excavation was finished and the OL3 site was handed over to XXX by ZZZ, XXX engaged YYY to inspect the site and comment on ZZZ's workmanship and the geological character of the OL3 excavation site.

[1] "XXX" refers collectively to the claimants in this arbitration, the consortium consisting of the German corporation XXX and the French Corporations XXX and XXX.

[2] "YYY" refers to the Finnish firm YYY.

[3] "ZZZ" refers to the Finnish respondent in this arbitration as well as any subcontractors hired by the respondent to carry out the excavation of the OL3 site.

Three reports were generated by YYY: one in January 2006 ("January Report"), one in February 2006 ("February Report") and one in November 2007 ("Final Report"). Of the three reports, only the Final Report was submitted with XXX's Statement of Claim in this arbitration. ZZZ has requested disclosure of the January and February Reports. XXX objects to such a disclosure.

Discussion

Wide Discretion

As per the contract between XXX and ZZZ, this arbitration is governed by ICC rules. Those rules are silent on privilege, however, and nearly silent on document production altogether. Article 20(1) reads: "The Arbitral Tribunal *shall* proceed within as short a time as possible to establish the facts of the case by *all appropriate means*, while Article 20(7) provides that "the Arbitral Tribunal *may* take measures for protecting trade secrets and confidential information." [emphasis added] This affords arbitrators under ICC rules a great deal of latitude when making decisions regarding the admissibility of evidence. The language was "deliberately chosen by its drafters in order to avoid imposing the procedural practices of any particular legal system on the participants in ICC arbitrations."[4]

The arbitrator's discretion here is not absolute, however. "[A]n international tribunal cannot simply ignore a request for the laws of privilege to be applied."[5] General principles and guidelines can be gleaned from the practice that has emerged over time as well as some treatment of the subject in other institutional rules of arbitration and model laws. For example, Article 20 of the ICDR Arbitration Rules states that, "The tribunal shall take into account applicable principles of legal privilege, such as those involving the confidentiality of communications between a lawyer and client."

[4] Y Derains, E Schwartz, *A Guide to the Rules of Arbitration* (2nd edn 2005), p 271.

[5] N. Gallagher, "Legal Priileges in International Arbitration" (2003) 6 *Int'l Arb. L Rev.* 45, p. 49

Similarly, the IBA Rules on the Taking of Evidence provide that, " . . . the Arbitral Tribunal shall . . . exclude from evidence or production any document, statement, oral testimony or inspection [where] . . . legal impediment or privilege [exists] under the legal or ethical rules determined by the Arbitral Tribunal to be applicable . . . ." The UNIDROIT Principles of Transnational Civil Procedure and the Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters each provide further (albeit similarly vague) recognition of legal privileges as fundamental transnational law.[6]

Procedural vs. Substantive Law

Procedural law

Of primary importance is the determination whether privilege is governed by procedural or substantive law. These decisions are often made based on the legal background of the arbitrator(s).[7] Common law jurists tend to be split in their tendency to view privilege as a substantive or procedural matter, while civil law jurists more uniformly categorize it as procedural.[8] In the present claim, if the tribunal determines that privilege is governed by procedural law, then it will be governed by *lex loci arbitri*, Stockholm, Sweden. This poses a particular problem for XXX because Sweden is among a

[6] UNIDROIT Principles of Transnational Civil Procedure 18.1: "Effect should be given to privileges, immunities, and similar protections of a party or non-party concerning disclosure of evidence or other information."

Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters Article 11: "In the execution of a Letter of Request the person concerned may refuse to give evidence in so far as he has a privilege or duty to refuse to give the evidence –

a) Under the law of the State of execution; or

b) Under the law of the State of origin, and the privilege or duty has been specified in the Letter, or, at the instance of the requested authority, has been otherwise confirmed to that authority by the requesting authority. A Contracting State may declare that, in addition, it will respect privileges and duties existing under the law of states other than the State of origin and the State of execution, to the extent specified in that declaration.

[7] G Born, *International Commercial Arbitration Volume II* (2009) p 1893.
[8] K Berger, "Evidentiary Privileges: Best Practice Standards versus/and Arbitral Discretion" (2006) Arbitration International, Vol. 22 NO.4, pp. 506-07.

number of civil law countries that recognize legal privilege with regard to external, but not in-house counsel.[9] In this claim, the documents XXX wishes to withhold from production were created before outside counsel became involved with the case.[10] Thus, even if XXX's in-house counsel commissioned the January and February reports, no privilege exists under Swedish law to protect the reports from production.

Substantive Law

If, on the other hand, the tribunal views privilege as being governed by substantive law, there are a number of consideratoins, any one of which may be controlling depending on the disposition of the arbitrator. Three basic principles provide a foundation or starting point in understanding the choice-of-law determination:

> First, it is generally acknowledged today that an international arbitral tribunal is under no obligation to apply the general conflict of laws rules which the courts at the seat of the arbitration have to apply as part of their *lex fori*. An international arbitral tribunal has no *lex fori*. Secondly, international arbitral tribunals, by their very nature, are inclined and entitled to take a comparative approach in tackling choice of law issues . . . . Thirdly, it is generally acknowledged that in making choice of law decisions, international arbitral tribunals should do justice to the legitimate expectations of the parties.[11]

Once the tribunal has determined to approach privilege substantively (versus procedurally), there are many avenues through which it might address the conflicts of laws issue:

1. Choice of law by the parties

[9] Lex Mundi, *In-House Counsel and the Attorney-Client Privilege* (2004), http://www.lexmundi.com/lexmundi/AttyClient_Privilege_List.asp?SnID=165325678.

[10] Freshfields Bruckhaus Deringer, lead counsel for XXX.

[11] K Berger, "Evidentiary Privileges: Best Practice Standards versus/and Arbitral Discretion" (2006) Arbitration International, Vol. 22 No. 4, P 507. See also O. Sandrock, "Welches Kollisionsrecht hat ein Internationales Schiedsgericht anzuwenden?" (1992) Recht der Internationalen Wirtschaft p 789.

In this scenario the arbitral tribunal is bound to apply the law selected by the parties.[12] However, the contracts between XXX and YYY fail to specify the applicable law so this approach is unavailable to the tribunal in this case.

2. "Closest connection" or "most significant relationship" test

> While the law of the place where the attorney practices on a regular basis should be considered as the most appropriate law applicable to legal privilege, some transactions may involve several attorneys from different jurisdictions and potentially different applicable laws. In addition, it might be appropriate to consider the application of other laws to decide on the issue of confidentiality, such as the law governing the dispute, the place where the document was created or where it is located, the domicile of the party claiming confidentiality. The law of the place of arbitration might be considered if relevant, although in general it is chosen for its neutrality and convenience and has little, if any, connection with the parties and their counsel.
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> When such conflicts of laws arise, the "closest connection" rule, adopted by the 1980 *Rome Convention on the Law Applicable to Contractual Obligations,* by the 1987 *Swiss Private International Law Statute* or the similar "most significant relationship" rule adopted in the United States by the ALI in the Restatement on Conflict of Laws, can be used as a guiding principle.[13]

In this case the only privilege rules that would be potentially helpful to XXX are work-product privilege under U.S. law and litigation privilege under English Law. Neither the claimants nor the respondents have any relevant ties to the United States. Some of XXX's external counsel consists of English lawyers, however they were hired after the present dispute arose and long after the reports in question were generated by YYY for XXX. If the tribunal here applies a "closest connection" test, it most likely would select the laws of Finland since it is the home country of the respondent as well as the place of execution of the contract. Beyond Finland, it is conceivable that the tribunal would apply German or French law based on the nationalities of the Claimants. In any case, whether

[12] K Berger, "Evidentiary Privileges: Best Practice Standards versus/and Arbitral Discretion" (2006) Arbitration International, Vol. 22 NO. 4, pp.508-09.
[13] P Heitzmann, "Confidentiality and Privileges in Cross-Border Legal Practice: The Need for a Global Standard?" ASA Bulletin, Vol. 26 No. 2 (2008), pp. 218-19.

Finish, German or French law is applied, there is no privilege rule that would protect the January and February Reports from disclosure.

3. The "most favorable" privilege rule

> The most favorable privilege rule allows courts to take into account privilege rules under the law of the state of execution or of the state of origin under Article 11 of the 1970 *Hague Convention on the Taking of Evidence*. In addition, under the Hague Convention, Member states may recognize privileges available in third party states (to date, only the Netherlands made a declaration that it would respect the law of states other than the state of origin or execution).
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> In this situation a tribunal would apply the law of the party, which provides the broadest protection to sensitive documents.[14]

Here, the laws of the parties are Finnish, German and French, respectively. The outcome would be the same regardless of which party has the most favorable privilege rule because none of the privilege rules in question include the equivalent of the English litigation or the U.S. work product privileges.

4. The "Least Favorable" Privilege Rule

> The least favorable privilege rule is the polar opposite of the most favorable rule. The tribunal here would apply the law of the party which provides the lowest standard of protection.[15] The analysis here mirror's that under the "most favorable" privilege rule. Since the rules under the laws of any of the parties do not include a litigation privilege, it makes no difference which of the parties respective rules the tribunal determined was applicable. XXX's objection to the production of the January and February reports would have no basis in law.

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[14] P Heitzmann, "Confidentiality and Privileges in Cross-Border Legal Practice: The Need for a Global Standard?" ASA Bulletin, Vol. 26 No. 2 (2008), pp. 219-220.

[15] J.H. Rubinstein and B.B. Guerrina, 'The Attorney-Client Privilege and International Arbitration' (2001) 18 J. Int'l Arb. P 596

Good Faith

In spite of the wide discretion arbitrators have with regards to admissibility of evidence, there is broad agreement internationally that "international arbitrators should accede to an appropriate privilege objection raised in good faith."[16] But where an objection does not appear to have been raised in good faith, the objection will likely fail as well cast the party making objection in a bad light.

"Precisely because arbitrators enjoy great discretion to decide on matters related to issues of privilege and confidentiality, reasonableness should always guide arbitral tribunals in their decision. As Jan Paulsson explained, civility and reasonableness have a lot to do with ethics.[17] General principles such as personal honor, honesty and integrity (found in most rules and codes such as the CCBE Rules), are often used as guiding principles to decide on ethical issues. They should also be considered in this process for deciding on privilege issues."[18]

XXX claims that the January and February Reports were drafts, and that they were created with litigation in mind. However, in early communications with ZZZ, XXX referred to the reports in a manner highly suggestive that the reports were, in fact, final reports. Moreover, whether final or not, XXX made clear that it was relying on these reports as a basis for its claims against ZZZ. The tribunal will likely not take seriously XXX's current claim that the reports were drafts meant for internal purposes only.

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[16] K Berger, "Evidentiary Privilges: Best Practice Standards versus/and Arbitral Discretion" (2006) Arbitration International, Vol. 22 No. 4, p 501.

[17] J Paulsson, "Ethics and Codes of Conduct for a Multi-Disciplinary Institute" [August 2004] 70 Arbitration 3, p 193.

[18] P Heitzmann, "Confidentiality and Privilges in Cross-Border Legal Practice: The Need for a Global Standard?" ASA Bulletin, Vol. 26 No. 2 (2008), pp. 223-24.

Conclusion

Before the tribunal gives serious consideration to an objection to ZZZ's document request, it must first determine whether legal privilege is governed by procedural or substantive law. If it is determined to be a procedural issue, which is especially likely if the majority of the arbitrators come from a civil law background, any objection to the production of the reports must be governed by the laws of Sweden, which do not recognize any privilege with regards to communications between a party and its in-house counsel. Thus, in order to have any chance of success an objection based on privilege must be determined at the outset to be a substantive issue and therefore potentially controlled by non-Swedish law.

However, even as a substantive issue it is unlikely that the laws of a favorable jurisdiction, such as English law, will be applied to this case. Germany, France and Finland are the only countries with a substantial relation to this dispute in terms of the nationality of the parties, or the places of origin and execution of the contracts. It is very likely that the laws of one of these states will govern the substantive issues in this dispute.

Moreover, given the lack of precise rules governing admissibility of evidence in arbitration, questions of good faith, equality and fairness will probably dominate any analysis of objections to the disclosure of documents. Our grounds for withholding the requested documents are two-fold: 1) the document is a draft, and not the document actually relied on in our claim, and 2) the document was created with litigation in mind, putting it in the category of documents protected by litigation privilege.

Both of these arguments are seriously vulnerable to attack. Prior to the creation of the Final Report, XXX referred to the documents multiple times, both in the claims and in correspondence

with ZZZ. In discussing the reports in question, XXX's tone is highly suggestive that they are final reports, rather than drafts, and in one instance before this claim was filed, XXX expressly indicated to ZZZ that the Janurary and February reports would be forwarded to ZZZ. Additionally, XXX's explicit statements indicate that XXX relied on the January and February Reports not just internally, but in making and quantifying its claim.

In order to make the 2nd argument (that litigation privilege applies) the tribunal must first be convinced that questions of privilege should be governed by the laws of England, a jurisdiction with virtually no relation to this dispute. XXX currently has English lawyers working on this claim, but it will likely be viewed by the arbitrators as disingenuous to suggest that the English lawyers, who were not employed by XXX until well after the January and February Reports were completed, could have influenced XXX's actions or expectations with regard to its procurement of those reports.

These arguments run the risk of painting XXX in a bad light in the eyes of the arbitrators. Even if the tribunal grants an objection to the production of the reports, which seems unlikely, the information already available to the tribunal will likely create a negative inference that is at least as damaging as the reports themselves. Considering the low probability of success and the potential consequences moving forward, I recommend against objecting to the production of the January and February YYY Reports.