EU legal commentary: UK Court of Appeal decision in *Real Estate Opportunities Ltd v Aberdeen Asset Managers Jersey Ltd and others*

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Abstract This short piece reports on a significant Court of Appeal decision on the relationship between, on the one hand, the confidentiality provisions in s. 348 of the Financial Services and Markets Act 2000 — specifically those pertaining to documents and material arising out of FSA investigations into regulated firms and individuals — and, on the other hand, the need for relevant and appropriate discovery for claimants in any subsequent civil litigation involving such firms and individuals.

Keywords: *civil litigation, discovery in proceedings brought by third parties against firms subject of FSA investigation, confidentiality of documents relating to FSA investigation of regulated firms and individuals*

BACKGROUND TO THESE PROCEEDINGS

The Civil Division of the UK's Court of Appeal made an important ruling on 9th March, 2007, on a preliminary point relating to discovery and inspection of documents which the claimant sought in the overall context of their civil claim for damages against two companies within the Aberdeen Asset Management group and against UBS. The claimant, Real Estate Opportunities Ltd (REO) was a Jersey-based investment company that had been floated with a split-capital structure; the Aberdeen companies had acted as investment managers to it and UBS had acted as sponsor to its flotation. The claimant's allegations in the main civil proceedings that gave rise to the preliminary point of discovery were:

- that Aberdeen and UBS owed REO after its formation and incorporation tortious duties of care to provide it with advice in relation to the flotation, the financial model to be adopted upon its flotation, the proposed content of the listing particulars and the investment objectives and policy it should adopt; and
- that Aberdeen and UBS acted in breach of certain agreements between REO and them relating to the flotation of REO and that, in the period after flotation, Aberdeen acted in breach of contract and duty, in particular in making various investments in securities in this period.

As is now well known and part of the folklore of scandal in the UK retail finance sector, the market in shares of investment companies with a split-capital structure collapsed in 2001 amid allegations of cross-investment, sloppy corporate governance arrangements and risk controls, inappropriate marketing of split-capital investment products to retail investors etc. Extensive investigations into active participants in this industry were conducted by the UK Financial Services Authority (FSA) (incidentally, the Jersey Financial Supervision Commission also investigated the Jersey-based Aberdeen defendant company under very similar legislative powers). The outcome of those investigations was an agreed compromise between the FSA and most of the firms under investigation. A settlement fund of some £194m was created to compensate those who had invested in zero-dividend preference shares. The Aberdeen group contributed £74m to that fund but made no admissions of liability. The FSA made no findings of any breaches of its principles or rules, nor did it actually take disciplinary action against any of the firms or key individuals involved in the split-capital investment company sector. As part of the FSA's investigations, a number of employees and former employees of all three defendant companies were interviewed and transcripts of those interviews were disclosed by the FSA to the defendant companies themselves after the interviews had taken place. It was the degree to which information contained in these documents could be used by the claimant in its civil claim which formed the issue in dispute here. The defendant companies sought to prevent the claimant having access to these documents via the normal pre-trial discovery and inspection process. In order to justify resisting access they sought to rely on the statutory confidentiality provisions in s. 348 of the Financial Services and Markets Act 2000 (FSMA) which prohibit the FSA from disclosing information relating to the discharge of its functions and extend to primary and secondary recipients of such information. The defendant companies therefore argued that were they to disclose such regulatory investigation material in these civil proceedings they would be committing a criminal offence and would risk prosecution for contravention of s. 348. They also relied on the prohibition in s. 391 of the FSMA on the 'publication' of warning notices or any details concerning them by the FSA or the persons to whom they are given, arguing that as the documents contained references to the FSA's warning notices of potential enforcement action then allowing inspection of them would constitute infringement of this section too.

THE DECISION

Both the High Court and the Court of Appeal reached the same conclusion — the documents were discoverable and the defendants' arguments that ss. 348 and 391 of the FSMA prevented their disclosure in civil litigation were wrong. In the Court of Appeal, Lady Justice Arden set out four questions, the answers to which would resolve this dispute:

> '(i) Can a person be said to "obtain" information from the FSA for the purpose of section 348 of FSMA if the FSA gives that person a document containing information which he already has even if he is not the source so far as the FSA was concerned?
>
> (ii) Can a person be said to "obtain" information from the FSA for the purpose of section 348 of FSMA if he knew that information already, or, in the case of a body corporate, knowledge of that information was attributed to it under the general law?
>
> (iii) Did the [High Court] judge err in the exercise of his discretion by ordering inspection of the documents notwithstanding the objections raised by UBS?
>
> (iv) Will the [Court] order for the inspection of warning notices result in publication of them contrary to section 391 of FSMA?'

The answer to each question, she ruled, was 'No' and the Court therefore affirmed the lower Court's decision to allow discovery and inspection of the disputed documents arising out of the earlier regulatory investigation of the defendant companies.

PRACTICAL IMPLICATIONS

This ruling will have the practical effect of making it much harder for financial institutions faced with civil claims from current or former clients, customers and counterparties to keep information supplied to them by the FSA as a result of regulatory investigation or enquiries out of the pre-trial discovery process. Why does this matter? Its significance lies in the fact that so many regulatory standards and obligations are expressed squarely in terms of obligations to identify, measure and manage various aspects of risk. Therefore, when the regulator tasked with the implementation and monitoring of these standards has investigated a regulated firm and/or its staff for possible contraventions of these standards, it is only to be expected that many of the exchanges which took place between a regulated firm and its regulator will focus on evidence of that firm or individual's performance of its regulatory risk management obligations. So that transcripts of interviews, for example, or reports of impressions gained by the regulator of the firm's discharge of its regulatory risk management obligations, may all contain questions or comments addressed to the firm which relate to issues such as 'was a risk spotted?' 'Was it discussed at board level? If so how often? Was it reviewed? What models were employed to manage it? What risk indicators were used to measure the probability and impact levels of that risk?'

The questions put by the regulator in the investigation, the answers made by the firm or individual under investigation and comments in correspondence of the FSA's impressions of that firm's risk management ability can all form powerful weaponry in the armoury of a clever claimant lawyer in subsequent civil proceedings brought against that same firm. These proceedings may well be brought in tort law, for negligence or for breach of statutory duty, or in contract or fiduciary law, but if a claimant can avail itself of the evidential assistance rendered by earlier regulatory material of relevance to the same facts, events and circumstances with which its own civil claim is concerned then it becomes much easier to substantiate allegations made against a defendant firm. This will embolden private litigation and the enforcement of rights in private law against firms which have been the subject of regulatory investigation, whether or not regulatory enforcement action for breach of regulatory standards was subsequently taken against that firm. It is perhaps no accident that the defendant companies concerned in this decision settled the damages claim in the main proceedings in the wake of the Court of Appeal's ruling that information relating to the FSA investigation could form part of the evidence bank in the civil claim. There is no reason why evidence as to attitudes to, awareness of and actions in the face of risks within the business should not be as significant in a common law court judging a damages claim as it is in a regulatory investigation. It is only a matter of time before the common law courts and judiciary are weighing evidence gleaned from regulatory investigations into risk management by the firm for its significance to the issue of whether or not the firm had fallen below expected common law standards of skill and care.

