

September 2018

# FRC v Sports Direct

## Summary

- 1 In what "*is believed to be the first application of its type to have reached the courts*", Arnold J in *Financial Reporting Council Limited v Sports Direct International PLC* [2018] EWHC 2284 granted an order requiring Sports Direct International PLC ("**SDI**") to disclose to the Financial Reporting Council ("**FRC**") (and solely for the purposes of the FRC conducting an investigation into SDI's auditor) documents over which SDI asserted legal professional privilege ("**LPP**"). It was held that this was not an infringement of SDI's LPP. The decision is being appealed.
- 2 This is a landmark decision concerning the extent to which a client of an audit firm can claim LPP over documents in the context of a regulatory investigation into the audit firm. It extends the principle that privileged material can be provided by a regulated person to that person's regulator, where this takes place for the purposes of an investigation by the regulator into the conduct of the regulated person. The same rule now applies to the production of privileged material to the regulator by a client of the regulated person.
- 3 The decision is an important development in the law of LPP, particularly in the context of regulatory investigations, and raises significant legal and practical issues.
- 5 The FRC had exercised its powers (see paragraph 1(3) of Schedule 2 to SATCAR and rule 10(b) of the AEP) and required SDI to provide documents because the FRC considered them relevant. The documents included 19 emails and 21 email attachments (the "**Disputed Documents**") that related to the audit of SDI's 2016 financial statements. SDI withheld this material on the grounds of LPP.
- 6 The parties agreed that communications with the accountants providing tax advice could not generate LPP (*R (Prudential plc) v Special Commissioner of Income Tax*). The Court was asked to consider three issues of principle regarding the claim to privilege, namely whether:
  - 6.1 legal advice privilege applies to documents by virtue of those documents having been attached to emails passing between SDI or its subsidiaries and its lawyers (the "**Communication Issue**");
  - 6.2 SDI's waiver of privilege by sending copies of documents to GT for the purposes of audit extends to the FRC (the "**Waiver Issue**"); and
  - 6.3 production of the documents to the FRC would infringe any privilege of SDI (the "**Infringement Issue**").

## The facts

- 4 Arnold J heard an application by the FRC for an order requiring SDI to provide it with documents over which SDI asserted LPP and which the FRC required for an investigation (the "**Investigation**") into the conduct of SDI's auditors, Grant Thornton UK LLP ("**GT**") in relation to the audit of SDI's 2016 financial statements.

## The Communication Issue

- 7 Arnold J dismissed this claim to privilege and confirmed that pre-existing non-privileged documents cannot be the subject of LPP merely because they are sent by a client to a lawyer or by a lawyer to a client for the purposes of advice or litigation. Such communications were to be distinguished from those which, while not explicitly seeking or receiving legal advice, can nonetheless attract LPP if they form part of the continuum of

communication between client and lawyer relating to the obtaining and giving of legal advice (*Balabel v Air India* [1988] 1 Ch 317).

### The Waiver Issue

- 8 SDI accepted that, in sending five of the 19 emails comprising the Disputed Documents to GT, there was a limited waiver of privilege, but contended that the waiver did not extend beyond GT or beyond use for audit purposes. The FRC argued that any waiver of privilege as against GT, even if only for audit purposes, necessarily entailed a waiver as against the FRC as GT's regulator.
- 9 Arnold J agreed with SDI: the "*regulatory process was entirely distinct from the process of audit*". They were not in any sense part of a single process, but reflected "*a fundamental separation of function and responsibility*". By sending the privileged documents to GT for the purposes of audit, SDI did not waive privilege as against the FRC.

### The Infringement Issue

- 10 The judge acknowledged that this was "*the most important and far-reaching issue raised by the present application, and the most difficult*". The FRC argued that, even if the Disputed Documents were protected by legal advice privilege and that privilege had not been waived by disclosing them to GT, disclosure of those documents for the purposes of the Investigation would not infringe SDI's privilege.
- 11 Arnold J took the view that "*the production of documents to a regulator by a regulated person solely for the purposes of a confidential investigation by the regulator into the conduct of the regulated person is not an infringement of any legal professional privilege of clients of the regulated person in respect of those documents. That being so, in my judgment the same must be true of the production of documents to the regulator by a client*" (emphasis added). The FRC's application was granted in relation to the Infringement Issue.
- 12 If the judge was wrong in so concluding, he adopted Lord Hoffman's '*alternative reason*' from *R (Morgan Grenfell & Co Ltd) v Special Commissioners of Income Tax* [2003] 1 AC 563 and found that even if the disclosure of the documents to the FRC infringed any LPP, the statutory regime '*could be construed as having authorised it*' on the basis the infringement was a '*technical one*'.

### Practical lessons

- 13 As shown by the judge's own comments, this decision is controversial. There are significant issues of substance for the Court of Appeal. In the meantime, there will be a number of points of interest for clients.
  - 13.1 Clients will rightly ask about the potential for further use of LPP material that is disclosed in this way and what restrictions might, in a particular case, be placed on such use, for example use in hearings in private and/or Court Orders.
  - 13.2 There will be a question about so-called "gateways" and whether there will be circumstances in which one regulator will be able to pass such LPP material to another regulator.
  - 13.3 Clients will be concerned about the implications of this decision for the investigatory work of regulators other than the FRC.
- 14 These points raise complicated legal issues and firms will want to seek specific advice on the facts of their particular cases.

### Contact us



**Stephen Roberts**

Partner

T: +44 20 7809 2336

M: +44 7909 926 418

E: [stephen.roberts@shlegal.com](mailto:stephen.roberts@shlegal.com)



**Sean Jeffrey**

Partner

T: +44 20 7809 2034

M: +44 7584 235 262

E: [sean.jeffrey@shlegal.com](mailto:sean.jeffrey@shlegal.com)



**Kate Cordery**

Partner

T: +44 20 7809 2397

E: [kate.cordery@shlegal.com](mailto:kate.cordery@shlegal.com)



**Alex Irvine**

Senior associate

T: +44 20 7809 2195

E: [alex.irvine@shlegal.com](mailto:alex.irvine@shlegal.com)