

ST MARYS VCNA, LLC v GOVERNMENT OF CANADA

NAFTA Dispute

Report on Inadvertent Disclosure of Privileged Documents

By letter dated 29 November 2012, from the Presiding Arbitrator of the Tribunal in the above dispute, Michael Pryles, I was appointed to enquire into, and determine, two questions that had arisen in the proceedings with respect to certain documents that had been produced by the Claimant investor to Canada, which are said to be privileged and produced inadvertently. The two questions posed for my determination are:

1. Are the documents inadvertently produced privileged?
2. If so, has privilege been waived?

I set out my answers to these questions and the reasons for my conclusions in this Report.

JURISDICTION

An issue has arisen as to whether the documents were not entitled to privilege on the basis that they were brought into existence for an improper purpose. The first matter I need to address is whether I have jurisdiction to consider that issue.

I raised the question of jurisdiction in an e-mail to the parties on 4 December 2012. The submissions on behalf of the Claimant dated 11 December 2012 contain a qualificatory clause in the following terms: "Apart from being beyond the scope of the mandate referred to you...".

There was no elaboration of this assertion, nor any reasoning to support it.

Canada contends that the improper purpose issue falls within the questions submitted for my determination. It submits: "Improper purpose goes to whether privilege exists: where this exception is applied, the documents subject to its application are deemed not to be privileged, at all."

In my opinion this submission should be accepted. In any event, the Claimant did not contest the submission.

Case law in many jurisdictions supports the proposition that the improper purpose/crime/fraud exception goes to the existence of the privilege. (See e.g. *United States v Zolin* 491 US 554,562-563 (1989). Accordingly, the issue falls within the first question referred to me by the Tribunal.

I am reinforced in this conclusion by the initial communication from Canada to the Tribunal of 7 November 2012 which is set out, in part, in Canada's submission to me of 7 December 2012. The improper purpose issue was expressly part of Canada's request for this reference.

Canada also relied on its assertion of improper purpose with respect to the second question i.e. waiver. It referred to one of the factors - "the overriding interests of justice" - to be taken into account on the waiver issue, to which I will further refer below.

THE ARTICLE 1113 (2) ISSUE

An issue in the principal proceedings concerns the status of the claimant St Marys VCNA, LLC ("SMVCNA"), a Delaware corporation. Canada asserts that, pursuant to NAFTA Article 1113 (2), it is entitled to deny the Claimant the benefits of

NAFTA Chapter Eleven. It asserts that SMVCNA is owned and controlled by a Brazilian conglomerate, Votorantim Group, and had no substantial business activities in the United States at any relevant time.

The claim underlying the principal proceedings involves a dispute between a Canadian corporation, St Mary's Cement Inc ("SMC") and the Government of Ontario. That provincial government had issued an order freezing the zoning of SMC's property to its current agricultural and conservation management uses, with the effect that SMC could not proceed with an application for approval to develop a substantial quarry.

On December 23, 2011, by notice to the Government of the United States and to the Claimant, Canada invoked Article 1113 (2). Thereafter, communications and pleadings were exchanged between the parties with respect to the issue of whether and, if so when, SMVCNA acquired substantial business activities in the United States.

It is these considerations which underlie Canada's assertion that the documents on which I am asked to rule are not entitled to privilege on the basis that they manifest an improper purpose, namely, the creation of a purported right on the part of SMVCNA to the protection of the NAFTA Treaty, to which it was not entitled.

Canada asserts that the Votorantim Group transferred the ownership of SMC to SMVCNA "with the intent of manufacturing NAFTA Chapter Eleven jurisdiction via SMVCNA which SMC would not otherwise enjoy".

THE FIRST QUESTION

It was common ground that recognition of attorney-client privilege is a well-established principle of international law. Canada submitted that it was similarly well-established that privilege did not extend to documents in furtherance of an improper purpose. The submissions from the Claimant to me did not expressly admit, but also did not contest, Canada's submissions in this respect.

Insofar as there may be any dispute as to this matter, I am of the opinion that the policy considerations underlying the existence of privilege support the proposition for which Canada contends. The privilege exists to serve the public interest in the administration of justice. (See e.g. *United States v Zolin* supra @ 562). It does not extend to communications which undermine the integrity of, or otherwise constitute an abuse of, the administration of justice. Documents that came into existence for such an improper purpose are not entitled to attorney-client privilege from the outset.

This is a widely accepted proposition in the domestic law of many jurisdictions. A number of Canadian authorities, together with statements manifesting international recognition of the principle, were referred to in Canada's submission and were not challenged by the Claimant. As I have noted, similar authority exists in the United States (e.g. *United States v Zolin* supra).

The basic thrust of Canada's contentions in this respect is that the Claimant "improperly sought to manufacture jurisdiction by changing the nationality of the investment after the dispute in issue had arisen and has thereafter sought to give a misleading impression of that company's activity". The alleged conduct extended to "the creation of

misleading evidence regarding the timing, nature or extent of the Claimant's alleged US business activities".

I recognise that the Tribunal will have to finally determine this issue. In its Reply submissions of 24 December 2012, the Claimant submitted that the entire issue should be left to the Tribunal. However, once I decided the jurisdictional question, the issue falls within the first question referred to me and I must address it.

The evidence before me in this respect is entirely documentary and many of the documents are self-serving. Nevertheless, I must make the relevant findings of fact for purposes of determining the issue referred to me.

I approach the fact-finding exercise with a recognition of the seriousness of the allegation and that I am determining the issue for interlocutory purposes. I am finding facts, on the evidence and submissions made to me, in order to determine whether Canada's case on improper purpose is sufficiently strong to overcome the attorney client privilege that would otherwise attach to the documents in dispute. This is not the same standard as would apply to a determination of the dispute on a final basis.

In its submissions, Canada relied on evidence which is available to it without reference to the documents in dispute. Its particular focus was the timing of relevant steps.

The dispute between the Government of Ontario and SMC had arisen in April 2010. The Notice of Intent to Submit a Claim to Arbitration, in accordance with NAFTA Article 1119, was filed on May 13, 2011. The Notice of Arbitration, in accordance with NAFTA Article 1120, was served on September 14, 2011. These two documents are not before me. According to Canada's letter of 26 January 2012, the Notice of Intent refers to conduct occurring between

October 2008 and April 12,2010 and the Notice of Arbitration extends to conduct of April 20,2011.

Canada relies on certain facts to establish a "reasonable" basis for its contention that SMVCNA was no more than a shell, so that I am justified in reviewing the allegedly privileged documents to determine whether any, and if so which, of those documents is entitled to privilege. It further relies on the same facts to determine the strength of its improper purpose case for purposes of the issue which I have to decide.

The facts set out in Canada's submissions and in the documents it put before me include:

*The Votorantim Group caused the US company SMVCNA to be constituted in October 2010, 6 months after the dispute had arisen.

*There was no mention of SMVCNA in a wide range of public databases and news services searched by Canada, as set out in paragraph 43 of its Brief Outline of Jurisdictional and Substantive Defences dated 31 August 2012.

*SMVCNA did not appear in Votorantim's public financial statements as a holding company for its North American operations, or at all.

*SMVCNA had no employees, no bank account, no place of business and no registration to do business until after it had launched its claim against Canada.

*The Claimant's US bank account was only opened on 27 May, 2011.

*The Claimant's only capital contribution from its Canadian owner, VCNA, was made on 1 June, 2011, before which the Claimant had no funds.

*The Claimant's web page was created between 5 May, 2011 and 20 May, 2011.

Canada also contends that, on the face of documents available to it, there is evidence that "SMVCNA employees manipulated evidence and made statements contrary to fact", specifically:

*The Claimant produced documents dated 2 May 2011 purporting to evidence the secondment of five employees to SMVCNA, whereas subsequent e-mails of 12 May, 2011 suggest that one of those employees was still being considered for secondment, with the implication that the first documents had been backdated.

*An e-mail of 4 May, 2011 indicated the steps that were still needed to be taken in Nevada to establish a business presence.

*The paucity of the number of corporate meetings held in Nevada by the "enterprise that claims to be the 'directing mind' of the Votorantim Group's North American cement companies".

*Canada asserts that:

"The Claimant has provided evidence of less than ten people directly employed by it, none of whom it paid, who were rarely if ever present in the Claimants' alleged Nevada place of business and who were simply existing Votorantim Group employees subject to partial, paper 'transfers' about the time the Claimant filed its Notice of Intent... while maintaining responsibilities for other companies. The Claimant has

provided no evidence that any person spent anything more than minimal time on SMVCNA specific activities.”

In its reply submissions of 11 December, 2012 and 24 December 2012, the Claimant rejected Canada's submission in strenuous terms.

By way of evidence the Claimant put before me a letter of 10 January 2012 and the Statement of Claim filed in the principal proceedings. These documents indicate that SMVCNA asserts that it is the parent company of many United States subsidiary companies with operations in ten states, employing over 1800 people and having assets of more than \$1.6 billion. Further details of substantial business activities are set out.

As I understand Canada's position with respect to these matters, it accepts that the Votorantim Group has extensive business interests in the United States, but asserts that they were not, at any relevant time, activities of, or controlled by, the Claimant. It was subsequently interposed for the purposes of “manufacturing” the NAFTA claim.

It is notable that in its submissions to me and in all of the documents on which it relies, the Claimant does not assert that these “substantial business activities” existed as at the date of the Ontario freezing order, nor at the date of the Notice of Intent, nor at the date of the Notice of Arbitration, being the times upon which Canada's submissions focus.

The facts which I have set out above, in my outline of Canada's submissions, are supported by documentary evidence. Significantly, they are not expressly denied or challenged in any way in the Claimant's submissions to me. Nor did the Claimant put before me any facts which could undermine the specific facts on which Canada relied. The Claimant chose only to assert the existence of identified,

substantial business activities without specifying how or when they came to be activities of SMVCNA.

For the interlocutory purpose with which I am concerned, I find the facts on which Canada relies to exist. I further find that the evidence of business activities on which the Claimant relies do not undermine the proposition that such activities were not the activities of, or controlled by, SMVCNA at any of the points of time on which Canada relies.

It appears from the letter of February 8, 2011, annexed to the Statement of Claim, that the Claimant contends that Article 1113 (2) requires Canada to establish that the Claimant has “no substantial business activities” in the United States *as at the date that Canada invoked the Article*.

The letter goes on to state that the relevant denial of benefits occurred on 22 December, 2011. No doubt for that reason the Claimant has maintained a position in the principal proceedings, and in the proceedings referred to me, which simply does not engage with Canada's submissions as to the position earlier in 2011 or in April 2010.

I have not received submissions on the legal issue of the proper interpretation of the Article. This is a matter of significance. If the Claimant's apparent interpretation is correct, then its conduct up to December 2011 could not be impugned for improper purposes or for generating misleading evidence.

In the absence of submissions, it is not appropriate for me to decide this question in any definitive way. Perhaps, I should simply ignore the point, on the basis that the parties have good reason not to pursue it before me. However, as the Claimant's contention has been put before me in an indirect manner, I do not believe I should proceed on the basis of the interpretation for which Canada contends unless I am

satisfied that its position on the issue of interpretation was reasonably arguable.

The rights of an investor under NAFTA arise, and relevantly arise only, if conduct that occurred at a particular point of time operated adversely to the commercial interests of the investor. This appears from the particular provisions invoked by the Claimant in its Statement of Claim identifying "treatment" (Articles 1102, 1103 and 1105) and conduct said to constitute deprivation of property (Article 1110). It is at the time of the "treatment" or deprivation that the "benefits of this Chapter to an investor... and to investments of such investors", within the meaning of Article 1113(2), accrue.

This interpretation best serves the objectives of an investment treaty, specifically, in the case of NAFTA, Article 102(1)(c) "increase substantially investment opportunities in the territories of the Parties".

I am satisfied, for purposes of the present reference, that I should proceed on the basis that it is at the point of time of the impugned conduct, or at the latest at the time of a Notice of Arbitration, that the issue of whether the investor "has no substantial business activities in the territory" is to be determined and not at the time of denial of benefits by a Party to the treaty. I find Canada's approach to the interpretation of Article 1113(2) to be reasonably arguable.

CONCLUSION ON FIRST QUESTION

The rights for which the Claimant contends are derived from a treaty between sovereign states entered into for the benefit of their citizens, relevantly, in this context, their corporate citizens, on the basis of reciprocity. Matters concerning the integrity of the application of this reciprocal arrangement between sovereign states must be given

substantial weight in any decision-making process arising under the treaty.

It is a fundamental condition of Chapter 11 of NAFTA that an investor claiming the benefit of the protections therein contained is doing so as a corporate citizen of a Party to the treaty, other than the nation against which the claim is made.

Canada referred me to the reasoning of the Tribunal in *Phoenix Action v Czech Republic* ICSID Case No. ARB/06/5 of April 15, 2009.

After referring to prior cases, the Tribunal said:

“(92)... A corporation cannot modify the structure of its investment for the sole purpose of gaining access to ICSID jurisdiction, after damages have occurred.

.....

(95)... An international investor cannot modify *downstream* the protection granted to its investment by the host State, once the acts which the investor considers are causing damages to its investment have already been committed.

.....

(106) In the Tribunal's view, States cannot be deemed to offer access to the ICSID settlement mechanism to investments not made in good faith. The protection of international investment arbitration cannot be granted if such protection would run contrary to the general principles of international law, among which the principle of good faith is of utmost importance.”

The Tribunal concluded on the facts of that case:

“(142)... The unique goal of this ‘investment’ was to transform a pre-existing domestic dispute into an

international dispute subject to ICSID arbitration under a bilateral investment treaty. This kind of transaction it is not a *bona fide* transaction and cannot be a protected transaction under the ICSID system."

I accept that this approach is applicable to determination of a privilege issue in the context of NAFTA, by way of analogy.

Where a State seeks to invoke Article 1113 (2) and credibly asserts a strong case that attorney-client privilege has been misused for the purpose of creating the false impression that a corporation was entitled to rights under the treaty as an investor, including that, at relevant times, it had substantial business activities within the territory of another Party to the treaty, the public interest in the proper administration of treaty rights and obligations requires the evidence in support of the contention to be given considerable weight in any decision making process under the treaty.

In the proceedings before me the Claimant has chosen not to contest the evidence put forward by Canada as at the times Canada asserts, and I have found for present purposes, to be relevant. I have formed the view, on the basis of the unchallenged evidence put before me, that Canada has a strong case that the Claimant is the vehicle for a scheme to obtain the right under NAFTA to institute and pursue proceedings, being a right to which neither it nor its controllers were entitled. The case is sufficiently strong to overcome the attorney client privilege for documents which came into existence as part of that scheme or which otherwise evidence the scheme.

THE DOCUMENTS

I have reviewed the documents. None contain admissions of the existence of the scheme. However, some contain statements which are consistent with its existence and

others identify activity by persons which may be inconsistent with the purported transfer of their employ to SMVCNA. I find that five documents do not appear to me to be of that character and, accordingly, should not be released.

I mark those which should be released "yes" and those that should not "no", as follows:

- *04645 (A)-December 9, 2010-Yes
- *00393-December 23, 2011 -no
- *05217-January 26, 2012-no
- *04908 April 27, 2011-yes
- *05316 January 9, 2012-yes
- *05305-December 30, 2011-no
- *06583 August 21, 2012 to October 12, 2012--yes
- ~~*01994-May 18, 2011-yes~~
- ~~*05020-May 18, 2011-yes~~
- *05082-May 25, 2011 yes
- *05305-December 30, 2011-no

THE WAIVER ISSUE

If the documents were not privileged at all, as I have found, in theory no question of waiver arises. However, in view of the Claimant's jurisdictional challenge and the terms of the reference to me by the Tribunal, I will make findings on the second question

There was common ground as to the relevant legal principles applicable to a case of inadvertent disclosure of documents entitled to attorney-client privilege. Both Canada and the Claimant referred me to the decisions of NAFTA Tribunals in *Glamis Gold v United States of America*, 21 April, 2006 and *Bilcon of Delaware v Canada*, 2 May, 2012.

These determinations adopt the intermediate position, increasingly common in many jurisdictions, between the traditional bifurcation that once a document has been

disclosed privilege is lost, on the one hand, and that proof of inadvertence is of itself enough to permit the reassertion of the privilege, on the other hand.

The two Tribunal decisions indicate that a range of factors must be taken into account and balanced, with a view to determining whether a waiver of privilege has occurred. These factors are:

- (a) The reasonableness of the precautions taken to prevent inadvertent disclosure in view of the extent of the document production;
- (b) The number of inadvertent disclosures;

- (c) ~~The extent of the disclosure;~~
- (d) Any delay and measures taken to rectify the disclosure; and
- (e) Whether the overriding interests of justice would or would not be served by relieving the party of its error.

On the issue of reasonableness of precautions, the Claimant notes that it reviewed some 12,000 documents in response to the requests of Canada and only 11 documents were inadvertently produced. The Claimant's submission to me of 11 December 2012 identified the reason for the inadvertent disclosure as a computer problem with the program that contained the Master Index of documents. As a result of power surges, the coding of the documents in the Index was corrupted. The Claimant stated that the 11 documents upon which I am asked to rule had been marked for exclusion from production, but they were inadvertently produced with 621 other documents.

In its reply submissions of 7 in December 2012 Canada noted that the claimant had produced a detailed index containing the 11 documents, a related CD-ROM and a hardcopy of its documents submitted. The submission added:

“We are unaware of how power surges could cause indexes to include specific document descriptions, or burn copies of specific document onto a CD-ROM, or insert paper copies of documents into boxes”.

In its earlier submission of 7 December 2012, Canada relied on the fact that numerous other communications to or from in-house counsel and the Claimant's counsel in the NAFTA proceedings were disclosed. It submitted that there was a ~~substantial lack of care in the review process undertaken to exclude documents entitled to privilege.~~

In my opinion, it is understandable that if a Master Index is corrupted it is likely to lead to the production of documents in each of the different ways identified. On the materials before me I am not able to reject the explanation proffered by the Claimant. It establishes the relevant inadvertence. It does appear that there is some failure in the process of checking the computer-generated Master Index, in view of the original intention to claim privilege. However, there is nothing before me to suggest that this involved a significant level of default on the part of the Claimant's lawyers.

The second factor, concerning the number of inadvertent disclosures, is also not a significant element in favour of a finding of waiver. There are only 11 documents from some 12,000 considered and 632 disclosed.

The third element ---the extent of the disclosure in the matter ---on the authorities, it appears, is directed to the importance of the information contained in the disclosed documents. The submissions on behalf of Canada do not

suggest that there is any other relevance of the documents beyond the matters arising relevant to the Article 1113 (2) issue. None of the documents, on their face, indicate an improper purpose. However, with respect to the documents I have not excluded from production in answer to the first question, I can see how they may assist proof of an overall scheme. In that respect this element is entitled to some, albeit not significant, weight.

On the fourth element, Canada accepted that the Claimant requested the return of documents within five days of its initial production which, according to the Claimant's submissions to the Tribunal of November 23, 2012, were three working days. This was prompt and this element does not support a finding a waiver.

With respect to the final--- overriding interests of justice--- factor, the submissions of Canada focused on the same considerations as it put forward in support of the improper purpose submission.

The first four elements, set out above, do not, in my opinion, suggest that waiver of so important a right as attorney-client privilege has occurred in the circumstances this case. Such a conclusion could only be drawn if determinative weight was given, in all the circumstances, to the fifth element.

I repeat my reasoning above on the improper purpose ground, particularly the section headed "Conclusion on First Question". Canada has made a strong case, on the evidence before me, that recognition of attorney client privilege would support an attempt to create the appearance of a right to pursue a NAFTA claim to which the Claimant is not entitled.

On this basis, the "overriding interests of justice" element is, in my opinion, entitled to determinative weight. The

Claimant should not be relieved from its error. I find that the privilege was waived by the inadvertent disclosure.



James Spigelman .

27 December 2012.