Dispute Resolution

March 2013

DISPUTE RESOLUTION BULLETIN

Piercing the corporate veil - the Supreme Court's ruling

The recent decision of the UK Supreme Court in *VTB Capital plc v Nutritek International Corp and others* (6 February 2013) emphasises the strength of the principle of separate corporate identity and indicates that the English courts will allow the corporate veil to be pierced only in very exceptional circumstances – and not in order to treat the company's "alter ego" as a co-contracting party.

VTB Capital plc (VTB) had entered into a loan facility agreement with Russagroprom LLC (RAP) for approximately US$225 million, to finance RAP's acquisition of nine companies operating in the dairy industry from Nutritek International Corp. (NUT). After RAP defaulted on the loan repayments, VTB alleged that NUT had made fraudulent misrepresentations which had induced VTB to enter into the loan facility agreement.

It transpired that a Mr Malofeev was the owner of both NUT and RAP, as well as of Marshall Capital Holdings Ltd. (Marshall), the ultimate owner of NUT. In August 2012, the Court of Appeal had refused to allow VTB to bring a contractual claim against Mr Malofeev.

VTB appealed to the Supreme Court, arguing that Mr Malofeev (and by extension Marshall) had used RAP's separate legal status to disguise the control that they exercised over it and had therefore misled VTB into believing that the transaction they were entering into was at arm's length and at a genuinely negotiated price. The Supreme Court refused the appeal and upheld the Court of Appeal decision, refusing to allow VTB to pierce the corporate veil and bring contractual claims against Mr Malofeev.

In reaching their conclusion, the Supreme Court conducted a full analysis of the principle of piercing the corporate veil, including whether such a principle exists at all in English law. After highlighting the fact that very few cases have supported piercing the veil and taking

into account that there was no binding House of Lords/Supreme Court decision expressly recognising and endorsing the piercing of the veil doctrine, Lord Neuberger concluded that it was unnecessary and inappropriate to decide in this instance whether the Court can pierce the veil of incorporation.

If the Supreme Court allowed the veil to be pierced in this case, it would lead to Mr Malofeev, the person controlling the company, being treated as if he had been a co-contracting party to the agreement - and he was not. It would be wrong to treat him as if he was a party when at the time the agreement was entered into, none of the actual parties to the agreement intended to contract with him and he did not intend to contract with them, and thereafter, he never conducted himself as if, or led any other party to believe, he was liable under the agreement.

The only judgment which supported extending the principle to make someone a co-contracting party was the decision in *Antonio Gramsci Shipping Corp. v Stepanovs* (25 February 2011). The Supreme Court commented that the conclusion in Gramsci was driven by the desire to ensure that someone who had been the "moving spirit" behind a dishonourable transaction could not avoid liability by hiding behind a corporate veil. This is not enough to justify piercing the corporate veil. A company should not be treated as anything other than a legal person completely and legally distinct from any individual behind the veil.

This decision restates and re-emphasises the strict orthodoxy of corporate identity. Unfortunately, the questions as to whether a principle of piercing the corporate veil exists at all and if so, the scope of the circumstances in which it is possible to pierce it, remain unanswered. However, it is likely that this decision will discourage the expansion of the doctrine into cases where it appears just to do so to get at an alter ego, further reinforcing the position of corporate identity as fundamental to the conduct of business.

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The Courts' approach to arbitration in Hong Kong - and some implications

A recent decision of the Hong Kong Court of Final Appeal in *Pacific China Holdings Ltd v Grand Pacific Holdings Ltd* (21 February 2013), is the latest in a series of decisions demonstrating the Hong Kong judiciary's reluctance to interfere with arbitration awards.

Grand Pacific obtained an ICC arbitration award against Pacific China for around US$55,000,000. Pacific China appealed to the Hong Kong Court of First Instance, alleging that there had been violations of Article 34(2)(a) of the UNCITRAL Model Law (Article 34(2)(a)). The Court of First Instance agreed and set the award aside. Grand Pacific then appealed to the Hong Kong Court of Appeal.

Broadly, Article 34(2)(a) is concerned with the conduct of arbitrations, both in terms of procedural fairness and compliance with the terms of the underlying agreement to arbitrate. As noted by the Court of Appeal, in assessing whether there has been a breach of Article 34(2)(a), *"the Court is concerned with 'the structural integrity of the arbitration proceedings'. The remedy of setting aside is not an appeal, and the Court will not address itself to the substantive merits of the dispute… It will address itself to the process…"* .

On the facts, the Court of Appeal concluded that there had been no breach of Article 34(2)(a). It indicated that in order for the Court to set aside an award under this provision, the conduct complained of must be sufficiently serious or egregious

that one could say a party had been denied due process. This is a high threshold to satisfy and should cause potential appellants to think twice before seeking to set aside an award on these grounds in Hong Kong.

The Court of Appeal also commented that even if there had been a violation of Article 34(2)(a), the Court could still refuse to set aside an award if it was satisfied that the tribunal could not have reached a different conclusion. (However, it recognised that there may be breaches so egregious that an award would be set aside even though the result would not be different.)

In the taxation proceedings that followed Grand Pacific's successful appeal, the Court awarded them indemnity costs, explaining that *"… if a party was unsuccessful in setting aside or resisting enforcement of the arbitral award, in the absence of special circumstances, he should pay costs on an indemnity basis."*

On February 21 2013, the Hong Kong Court of Final Appeal refused Pacific China leave to appeal the Court of Appeal's decision, noting that *"The rulings complained of were made by the tribunal in the proper exercise of its procedural and case management discretions, reflecting its assessment of the requirements of procedural fairness as appropriate to the circumstances. There is no basis for interference by the Court."*

There is significant overlap between Article 34(2)(a) and section 89 of the Hong Kong *Arbitration Ordinance (Cap. 609)*, which sets out the grounds on which the Court may refuse to enforce a foreign arbitration award under the New York Convention. It is therefore anticipated that the Hong Kong Courts would take a similarly robust approach to attempts to resist enforcement of New York Convention awards on the basis of lack of procedural fairness and/or failure to comply with the terms of the underlying agreement to arbitrate.

Arbitrators in Hong Kong have a high degree of autonomy in their management of arbitrations and the Court will be reluctant to interfere with this autonomy except in the most exceptional circumstances.

Therefore, parties involved in arbitration with a Hong Kong dimension would be well advised to raise any concerns as to procedural fairness and/or failure to comply with the terms of the underlying agreement to arbitrate at the time of the arbitration, rather than waiting until after the award is published, or sought to be enforced, before doing so.

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Conferences & Events

HFW International Arbitration Seminars
Hong Kong (Tuesday 16 April 2013)
Singapore (Friday 19 April 2013)
London (Thursday 23 May 2013)

HFW Dispute Resolution Seminars
HFW London
(30 April and 14 May 2013)

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