

**IALS** INSTITUTE OF  
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# IALS Student Law Review

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# Editorial

## Welcome to the IALS Student Law Review

### Tugce Yalcin

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Welcome to 2020's first issue of the Institute of Advanced Legal Studies' Student Law Review (ISLRev), the University of London. This issue has some fascinating articles which deal with hotly debated topics and will be detailed in brief in a moment. However, this issue also represents a changing of the guard as a new Editorial Board has been elected. We would like to take this opportunity to introduce ourselves and also outline and explain the exciting plans we have for the future of the ISLRev.

Before we introduce ourselves, we would like to thank the outgoing Editor-in-Chief, Lovinia Otudor, for her work for the ISLRev. We wish you all the best for your future plans.

This year, ISLRev is fortunate to have one Editor-in-Chief, an Academic Editor, a Deputy Editor and an Associate Editor. We would like to take a moment to introduce each in turn:

**The Editor-in-Chief** is Tugce Yalcin. She is a lawyer working for a global law firm and is specialised in Corporate Law, cross-border M&A and financial transactions as well as Commercial Law, Investment Law and European Law. She is currently a PhD candidate at IALS researching about "*Warranty and Disclosure of Information in M&A Transactions in the Light of the Theory of Contract Law – Comparison of the Common Law and the Civil Law*".

**Our Deputy Editor** for this year is Emmanuel Saffa Abdulai. Emmanuel is a lecturer in media law, academic legal writing, and Rule of Law, Justice and Peace Building at the Fourah Bay College, University of Sierra Leone. He is Editor-in-Chief of the Journal on Human Rights Law in Sierra Leone. Emmanuel is currently a second year PhD candidate at IALS specialising in constitutional and administrative law.

**Our Associate Editor** for this year is George M. Daoud. George has a background in the Law Enforcement, Financial, and is currently in the Legal industry as a practitioner in Canada. He is currently a PhD candidate at IALS, focusing on International Financial Law with an emphasis on Emerging Technologies and its effect on the sophistication of Money/Cyber laundering practices.

We are fortunate to be joined by Professor Anton Cooray from City, the University of London. He acts in the role of **Academic Editor** of the ISLRev.

As we have said, there are big plans ahead for the ISLRev this year. We plan to open up the journal and improve access to all postgraduate students in the UK and, possibly, abroad. This, we are hoping, will attract fascinating articles from the widest possible spectrum of legal expertise.

The opening up of the Journal will be accompanied by an increased number of engagement events. We aim to provide these events several times within an academic year and will bring together academics, practitioners and students to share their perspectives as well as advice on publishing while also giving attendees a chance to network. Please do keep an eye out for more information.

Finally, for each issue of the ISLRev going forward, the Editor-in-Chief will alternate writing an editorial opinion piece at the beginning of each issue. These will give a broad overview of relevant legal topics alongside the articles included in the respective issue.

Without further ado, we are delighted to introduce the following articles of this ISLRev-edition:

**Febechi Chukwu** investigates whether under the English law a breach of indemnity gives a party a right to bring a claim for debt or a claim for damages. He discusses various judgments that recognised breaches of indemnities as giving rise to debt claims as well as the ones that pursued the damages claim approach, as well as gives a potential solution at the end

**Mohammad El-Gendi** discusses whether the UK needs to create a clear case for why the UK should be the preferred place of business in terms of Brexit. Given the fact that unclear, arbitrary and unprincipled laws and rulings may cause businesses to move to the EU post-Brexit, he shows the necessity of reassessing certain key case and areas of law to address their suitability for the new economic climate.

**Naseem Khan** discusses the UK Government's proposals to adopt a codified constitution in England and Wales, Scotland and Northern Ireland after the Brexit Referendum of 2016. The author shows also the reasons behind the lack of support for a codified constitution, weighing up arguments for and against.

**Lara Krayem** examines about the question as to why the EU refrained from using the Temporary Protection Directive that serves the purpose of establishing minimum standards for giving temporary protection and promoting a balance of efforts between Members States when receiving displaced persons. She discusses the reasons behind the non-implementation of the Temporary Protection Directive and whether the mass influx of asylum seekers during the Arab-Spring uprisings was a missed opportunity to activate the Directive.

**Martin Kwan** looks at the law of foreign state immunity from a comparative perspective and uses the facts of *Huawei-US* controversy as a test case to illustrate the differences in the laws of various jurisdictions. He examines whether Huawei can sue the US Government and if yes whether it is possible to sue the US government in Canada, England and Wales, Australia, China and the US.

As ever, we are hugely thankful to our authors for their submissions. We would encourage any postgraduate, practitioner and academic who would like to submit an article to get in touch with us. Our details can be found here:

<https://ials.sas.ac.uk/digital/ials-open-access-journals/ials-student-law-review/ials-student-law-review-editorial-board>

We look forward to hearing from prospective contributors. Until then, please enjoy the latest issue of the ISLRev.

Tugce and the ISLRev Editorial Board.

# The breach of contractual indemnities under English law – a debt claim or a damages claim?

Febechi Chukwu

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## Introduction

Indemnities are a fundamental part of contracts in English law<sup>1</sup>, and are often heavily contested and negotiated. ‘No-one likes to give them and everyone wants the benefit of them’<sup>2</sup>. Parties to a contract will look to ensure that any indemnities inserted into the contract reflect their commercial interests, and as a consequence the form of the indemnities inserted into contracts are often some of the most challenged parts of that contract. Unfortunately, this is one of those areas of English law that has not developed to give clarity and certainty to commercial parties.

In their analysis of contractual indemnities, Carter and Courtney identified the split in approach with regards to how breaches of those indemnities are perceived. They state in the first instance that ‘an action to enforce the clause is an action for contract damages’<sup>3</sup> but later recognise that ‘in contract, it is sometimes suggested that an action on an indemnity is a claim in “debt”’<sup>4</sup>. Two judgments reported in 2015 from the High Court of England and Wales illustrated this divergence of opinion on how English law deals with breaches of indemnities. The decision in the case of *ABM Amro Commercial Finance plc v Ambrose McGinn & others*<sup>5</sup> (the “**ABM Amro Case**”) took the approach that a breach of an indemnity gave rise to debt claims. Pursuing an apparently opposite approach, the decision in the case of *Durley House Limited v Firdale Hotels plc*<sup>6</sup> (the “**Durley House Case**”), held that breaches of indemnities gave the indemnitee a right to claim for damages. These were two decisions delivered within a few months of each other, seemingly following different approaches.

This apparent lack of clarity in the approaches of the English courts when looking at indemnities is concerning. The purpose of this article is to consider in detail the approaches of the courts to the consideration of the commercial remedies available to parties for breach of indemnities under English law. Does it result in either a debt claim or a damages based claim? Crucially this article will look to determine if English law has reconciled these two approaches, and if it is possible to try to present these decisions of the English courts as being part of a clear overall approach to the interpretation of indemnities.

Firstly a detailed background of indemnities will be presented in order to aid readers to better understand the context of the debt-damages debate. The second part of this article will look at the approach of the English courts in considering breaches of indemnities as giving rise to debt claims as the appropriate commercial remedy. The development of English law to support this approach will be assessed through an analysis of some of the leading judgments that support this position, and a review of how the courts have applied this approach.

The third part of this article will focus on the judgements of the English courts over the years that support the damages claim approach. The merits and limitations of this will be considered, and a comparison made to the debt claim approach.

Finally the article will argue that it is not possible nor advisable to choose a fixed approach under English law for breaches of indemnities. The focus in the courts should be on the interpretation of the indemnity clause in question to determine which remedy is most suitable. The law has attempted to show flexibility

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<sup>1</sup> Reference to English law in this essay means the laws of England and Wales, and reference to the English courts means the courts of England and Wales.

<sup>2</sup> CMS Law Now *Indemnities: what is all the fuss about?* (23 June 2016)

<sup>3</sup> J W Carter and W Courtney ‘Indemnities against breach of contract as agreed damages clauses’ [2012] *Journal of Business Law* 555 p558

<sup>4</sup> *ibid*

<sup>5</sup> [2014] EWHC 1674 (Comm.)

<sup>6</sup> [2014] EWHC 2608 (Ch.)

in a complex area, and judges should steer away from firm pronouncements that breaches of indemnities necessarily fall into a specific category.

## Background to indemnities under English law

As stated in the introduction above, indemnities are an important feature of commercial contracts, and are often the subject of important negotiation by the parties to the contract. Indemnities have been described as 'a significant part of any contractual dealing'<sup>7</sup>, and it is useful to emphasise the important but contentious nature of indemnities to contracting parties. Despite their importance, there is a relative lack of academic consideration of the topic.

### What is an indemnity?

A broad response to that question is set out in a book called the Law of Guarantees, which states that 'an indemnity, in its widest sense, comprises an obligation imposed by operation of law or by contract on one person to make good a loss suffered by another'<sup>8</sup>. A useful practical example to illustrate this can be drawn from the construction services industry, where a Hospital Trust awards a facilities management contract to a contractor after a tender process. The Trust will want to ensure that the contract executed with the contractor includes indemnities in its favour so that the contractor will be liable to pay the Trust a certain sum if, during the life of the contract, certain events occur that result in the employer being exposed to or incurring certain losses. Bennett provides his perspective on contractual indemnities, stating that 'as a general proposition, indemnities look to make the party best able to manage a particular risk responsible for the consequences of the possible event occurring'<sup>9</sup>. Parties therefore negotiate what issues and risks should be covered by an indemnity, and the extent of the cover provided. From a practical perspective, indemnities can be said to be beneficial as they ensure that the party that can manage the contract best is liable to prevent certain risks from materialising, and should be financially liable for those risks should they materialise and cause the innocent party to suffer a loss<sup>10</sup>. They act as an effective way to manage contractual risk.

The practical and commercial significance of indemnities cannot be understated, however as already mentioned, there does appear to be conflicting views presented by the English courts regarding what remedies are available when an indemnity is breached. This article will now consider the different views presented by the English courts on the available grounds for innocent parties to claim when an indemnity has been breached, and whether it is a claim for debt or for damages. It is crucial to understand that 'this is more than a semantic difference'<sup>11</sup> as 'the answer is critical because it dictates the nature of the indemnified party's claim and thus whether the Damages Rules apply'<sup>12</sup>. Appreciation for this distinction and how it is practically applied by the English courts has a real impact on commercial parties. Before addressing that debate, it is firstly important to briefly set out the difference between an action for debt and a damages claim.

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<sup>7</sup> M Bennett *Drafting Effective Indemnity Clauses* paper presented at the College of Law on 18 February 2016 p3

<sup>8</sup> G Andrews and R Millett, *The Law of Guarantees* 6<sup>th</sup> edition (London: Sweet and Maxwell, 2012) at para. 1-012

<sup>9</sup> Bennett op.cit. p4

<sup>10</sup> *ibid*

<sup>11</sup> N D'Angelo 'The indemnity: It's all in the drafting' [2007] 35 *ABLR* 93 p107

<sup>12</sup> *ibid*. The Damages Rules referred to are the standard Common law rules that limit claims for damages, such the rule on remoteness and the rule requiring mitigation of loss.

## What is a debt claim? What is a damages claim?

A debt claim arises where a party is liable to pay a fixed sum under a contract, and fails to do so<sup>13</sup>. The contract between the parties will normally be clear on the sum owed, and any claim will be based on the contractual obligation undertaken. An example of this is where a party who has done work sues for the agreed remuneration or bonus<sup>14</sup>. A simple understanding of a claim for damages is provided in McGregor on Damages, which states that there are three requirements for a damages award:

1. an award in money;
2. for a wrong;
3. which is a civil wrong.<sup>15</sup>

In contract law, damages will be awarded where there has been a breach of contract, and the payment of money will be awarded as 'compensation to the claimant for the damage, loss or injury he has suffered through that breach'<sup>16</sup>.

The importance of the distinction between the two is that a beneficiary of an indemnity may prefer to pursue an action for debt where there is a breach of that indemnity, rather than seek damages as claims for damages are limited by two important requirements:

1. the 'remoteness of loss' rule – a loss will only be recoverable if it arose in the usual course of things or the losses were contemplated by the parties at the time the contract was executed; and
2. the 'mitigation' rule – the innocent party will not be able to recover losses which he should have avoided or which he could have avoided had he taken reasonable steps.<sup>17</sup>

Certainly a party defending a claim for breach of indemnity may prefer to defend a damages claim and rely on the above two rules. Practically some parties may actually prefer to pursue a claim for damages because the amount being claimed does not need to be quantified at the time nor does there need to be proof that a demand for payment was made<sup>18</sup>. There are therefore different reasons why different parties may seek a particular form of remedy when an indemnity clause in a contract is breached. It is important to emphasise the practical significance of the debt-damages debate for commercial parties to a contract, and the need for clarity in English law in its resolution of disputes for breaches of indemnities.

## Breach of an indemnity; debt claim?

As referred to earlier, the purpose of this article is to consider whether English law has a clear approach with regards to the interpretation of indemnities in instances of breach, and the basis on which a claim for that breach is considered in the courts. Bennett considers 'of fundamental importance jurisprudentially'<sup>19</sup> and of 'somewhat practical importance'<sup>20</sup> whether the claim is one based on debt, or whether it is a claim for damages. There is the argument that English law recognises that a claim based on a contractual indemnity gives rise to a claim in debt. The ABM Amro Case saw a ruling by Mr Justice Flaux in the High Court which supports this approach. The claimant in the case, ABM Amro purchased the debts of its clients Jenk Sales Brokers Limited ("**JSBL**") under an agreement dated 30 June 2003. Each of the defendants, Ambrose McGinn, Ross Lawrance Beattie and Marcus Leek, were directors of JSBL. They entered into a deed of indemnity with the claimant (in the case of the first two defendants

<sup>13</sup> *Chitty on Contracts*, edited by H. Bealer, 33<sup>rd</sup> edn (London: Sweet & Maxwell, 2018), Vol.1, at para. 27-002

<sup>14</sup> *ibid*

<sup>15</sup> *McGregor on Damages*, edited by Edelman, Colton & Varuhas, 20<sup>th</sup> edn (London: Sweet & Maxwell, 2017) at para.1-001

<sup>16</sup> *Chitty on Contracts* op.cit. at para. 26-001

<sup>17</sup> *ibid* at para. 26-002

<sup>18</sup> R Zakrzewski 'The Nature of a Claim on an Indemnity' [2006] 22 *Journal of Contract Law* 54 p66

<sup>19</sup> Bennett op.cit. p6

<sup>20</sup> *ibid*

in May 2007 and with the third defendant in December 2008), which included a conclusive evidence clause, which essentially extended liability from JSBL to the defendants. In May 2009, JSBL entered into administration. The claimant appointed an agency to collect outstanding debts from JSBL, and over two years the agency pursued collection of as much outstanding debt as possible. After those two years passed, the administrators of JSBL acknowledged in writing to the claimant that JSBL was still indebted to the claimant in the sum of £8,924,783. The claimant then sought to recover that outstanding sum from the defendants under the deeds of indemnity in the courts. The defendants argued that as their liability was secondary not primary, any liability that they had was discharged by material variations to the original agreement for the purchase of the debt. Further they also argued that the claimant had not taken the proper steps to collect and enforce the debts and also that the claimant was essentially estopped from relying on the agreement in respect of debts notified after 24 February 2009. The claimant served certificates of indebtedness on the defendants in October 2013 as part of its claim for sums owed and as conclusive evidence against the defendants. The claimant applied for summary judgment at the High Court. Flaux J, decided the case, holding that the inclusion of a conclusive evidence clause in the deeds of indemnity meant that the liability of the defendants was primary and not secondary. In addition, and crucially, the judge held that there was no obligation on the claimant to mitigate its losses nor could the defendants rely on the defence that their liability should be limited as a result of the claimant contributing to its own losses. This was because the liability owed by the defendants was primary and not secondary.

Importantly, the judgment in this case by Flaux J was emphasising that the claimant could recover monies owed by the defendants as a form of debt as it was a primary obligation, as opposed to pursuing a claim for damages. There is some analysis of the case which suggests that the decision of Flaux J was a consequence of the inclusion of 'wording in the conclusive evidence certificate clause which entitled the claimant, when arriving at the amount payable...to take into account all liabilities...and to make a reasonable estimate of any contingent liability'<sup>21</sup>, which has been suggested to support the argument that the sums owed was as a debt as it 'was not dependent upon any conclusive determination of liability of the Company [JSBL]'<sup>22</sup>. This is an important point, and the judge was clear in his analysis in determining that the claim for breach of indemnity in this instance was a debt claim. Evidently Flaux J considered the specific facts of the case in arriving at his decision, nonetheless the ruling delivered if considered without context and in broad general terms, could give the impression that English law is settled on this matter. Tedjani, in his conclusion to his review of indemnities in SPAs, states the following; 'An indemnity is a debt claim. The trigger is an agreed event and the remedy is an agreed sum'<sup>23</sup>. This assertion presents a rigid understanding of the law and judgments in this area, and incorrectly ignores the inconsistency in the consideration of breach of indemnity claims by the English courts.

There are other rulings in the English courts that have considered indemnities, and support the proposition that a claim for breach of an indemnity is to be understood as a debt claim. In *Jervis v Harris*<sup>24</sup>, a prominent case dealing with property law and more specifically repairing covenants for dilapidations, Lord Justice Millett, one of the three judges hearing the case, considered the indemnities at question, and gave a relatively detailed assessment of the position of indemnities under English law. He stated as follows;

*"The short answer to the question is that the tenant's liability to reimburse the landlord for his expenditure on repairs is not a liability in damages for breach of his repairing covenant all. The landlord's claim sounds in debt not damages; and it is not a claim to compensation for breach of the tenant's covenant to repair, but for reimbursement of sums actually spent.....The law of contract draws a clear distinction between a claim for payment of a debt and a claim for damages for*

<sup>21</sup> Sherman and Sterling 'Case Comment – United Kingdom: indemnity – conclusive evidence certificate' [2014] *Journal of International Banking Law and Regulation* p116

<sup>22</sup> *ibid* p116-117

<sup>23</sup> M Tedjani 'Indemnities in private share deals' [2019] *Company Lawyer* 39 p46

<sup>24</sup> Ch. 1991 J.No.416

*breach of contract.....a debt is a definite sum of money fixed by the agreement of the parties as payable by one party to the other in return for the performance of a specified obligation by the other party or on the occurrence of some specified event or condition...<sup>25</sup>*

Millet LJ, considering the facts of that case, was clear in his assertion that a claim for breach of the indemnity sounds in debt and not damages, although the esteemed judge appears not to have ruled in general terms. His decision represented another example of a breach of an indemnity being deemed to result in a debt claim, although the ruling did not go as far as Flaux J.

The decision of the Court of Appeal in the case of *Royscot Commercial Leasing Limited v Ismail*<sup>26</sup> (the “**Royscot case**”) is also a relevant authority in this area and supports the argument that English law recognises breaches of indemnities as giving rise to debt claims. Flaux J relied on this ruling in his judgment in the *ABM Amro Case*, establishing that where a claim for breach of indemnity was for a specific sum, it was a claim for debt. The background to the *Royscot case* is that the claimant was a leasing company that entered into an agreement with a company called *Mina Enterprises Limited*. The claimant would rent certain equipment to the company for a total amount of £31,449.20 to be paid monthly by the company. This agreement was entered into on 10 May 1988. At the same time, the defendant, Mr. Mohammed Ismail, who was a director of *Mina Enterprises Limited*, entered into an indemnity with the claimant. During the life of the contract, *Mina Enterprises Limited* went into liquidation, and the claimant repossessed the goods, as it was entitled to do under the agreement, and sold them at auction for £498.60. The claimant then also sought to bring a claim to recover the outstanding rental sum that was owed as a result of the early termination of the contract (minus the amount recovered at auction for the equipment). The defendant, having provided an indemnity to the claimant, was liable to pay what was owed. The defendant presented several arguments, including that the claimant had failed to properly mitigate its losses and therefore could not claim the amount alleged as a consequence. The matter ended up progressing to the Court of Appeal as stated earlier, where the judges decided to dismiss the appeal by the defendant. The judges recognised a breach of indemnity as resulting in a debt claim, and as a result the usual rules of mitigation and contributory liability that may arise in damages claims did not apply here. The actual judgement was written by Lord Justice Hirst, with Lord Justice Kennedy and Lord Justice Glidewell concurring. Hirst LJ considered the arguments of the claimant ‘correct as a matter of law’. The claimant had argued that;

*“a claim under a contract of indemnity, such as this, is not a claim in damages at all, but is a claim in debt....Accordingly, it should not be open to a person providing an indemnity to challenge his obligation to pay under the contract of indemnity by reference to principles relating to the assessment of damages for breach of contract which have no application to debts.”<sup>27</sup>*

Emphasising the point later in his judgment, Hirst LJ added that ‘it is therefore, in my judgment, implicit in the majority decision that the rules of mitigation do not apply to a claim for a debt due’<sup>28</sup>.

The above authorities show that there may be a clear thread of reasoning in English law which supports the position that a breach of indemnity will result in a debt claim. Judges have considered this matter, and there are a number of rulings which mandate that rules of mitigation and contributory liability should not apply to claims for breach of indemnity, which supports the debt claim approach. Despite evidence

<sup>25</sup> *ibid* p202

<sup>26</sup> [1993] WL 1465298. See also the decision of the High Court in the case of *Codemasters Software v Automobile Club de L'Ouest* [2009] EWHC 2361. The case concerned interpretation of an indemnity, and was heard by Mr Justice Warren in the High Court. In delivering his judgement Warren J included the following; “*The law, so far as I am concerned, is therefore that questions of mitigation do not arise under contracts of indemnity so as to give the indemnifier a defence to any part of a claim for which he would otherwise be liable under his indemnity.*” This would appear to support the debt claim approach, rather than the damages claim approach. See also the judgment of Lord Hoffman in *Caledonia North Sea Ltd v BT Plc* [2002] S.C. (H.L.) 117 p143 where he appeared to distinguish claims for breach of indemnity from breaches of contract stating “*But this is not a claim for breach contract. It is a claim to an indemnity for a liability...*” It would appear the distinguished Lord Hoffman was differentiating the nature of a breach of contract claim based in a remedy for damages, from the breach of indemnity claim.

<sup>27</sup> *ibid* p3. The learned judge stated, in response to this argument, ‘in my judgment this submission is correct as a matter of law’

<sup>28</sup> *ibid* p4



of this approach by the courts, the conclusion cannot be considered to be completely certain, and it will be demonstrated that there are decisions in the English courts that support the alternative view that breach of indemnities claims are damages based claims. Even some apparent proponents of the debt claim approach acknowledge the lack of absolute certainty in English law. Bennett, an Australian lawyer, considering the nature of indemnities under common law, but principally based on the English law rulings on this matter, provides tacit support for the debt claim approach, stating that ‘on balance, it seems recovery under a contractual indemnity is a right of reimbursement and not subject to the issues relevant to recovering damages....the claim is therefore more in the nature of a debt’<sup>29</sup>. Note his support for this particular approach is not absolute, and his arguments are certainly relevant when focusing solely on the English law position on indemnities. There needs to be some acknowledgment of the complexity of the judicial approach to this issue, and the next section of this article will present English law authorities that support the damages based claims approach and highlights that complexity.

## Damages for breach of an indemnity

The alternative approach under English law with regards to the breach of indemnities in contracts, is as mentioned above, that they give rise to claims for damages. There are some clear judgments by the English courts that support this approach.

The ruling in the Durley House Case and the decision in the ABM Amro Case were delivered within weeks of each other, and it this contrast in approach by the High Court, on what appeared to be similar questions, that illustrates the complexity in this area of the law. The background to the Durley House Case is as follows. The claimant, Durley House Limited, had entered into a lease with Cadogan Estates Limited (“**Cadogan**”). The claimant had also entered into an agreement with Firmdale Hotels plc (the defendant), including a form of indemnity under which the defendant would pay for rent due under the lease to Cadogan. The lease terminated in 2012, and the claimant vacated possession owing a substantial amount of rent. Cadogan served a statutory demand on the claimant for the rent in September 2012, and brought proceedings against the claimant in County Court for the outstanding sums owed as rent and other payments that it claimed were due. Judgment was found in favour of Cadogan for arrears of rent in the sum of £2,129,830, in addition to damages and interest. That judgment has not been satisfied, the lease was the only asset of the claimant and the claimant was subsequently an insolvent company. Cadogan obtained possession of the property in January 2013. The claimant then sought to rely on the agreement in place with the defendant in order to ensure payment of the outstanding rent due by the defendant.

Stephen Morris QC, then sitting as a Deputy High Court judge, delivered the judgment. He considered many different issues including the validity of the indemnity, in arriving at his conclusion in this judgment, however the important aspect of his ruling to consider here is in relation to the remedy available for breach of the indemnity, and the judge made some interesting statements on this in his decision. He stated;

*“It is certainly the case, that the English authorities are at one in taking the view that the remedy for breach of a contract of indemnity is damages, rather than one for a contractual sum due (i.e. debt)”<sup>30</sup>.*

This was quite a bold and clear statement by the judge, and it appears very difficult to reconcile his statement with the ruling of the High Court in the ABM Amro case. Morris QC concluded “that the Defendant is liable to the Claimant for damages for breach of the obligation to indemnify”<sup>31</sup>. Evidently the outcome from this particular case was that breach of an indemnity should clearly be seen as giving rise to a claim for damages in favour of the recipient of the indemnity. There is the argument that ‘the

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<sup>29</sup> Bennett op.cit. p8

<sup>30</sup> n6 above p29

<sup>31</sup> ibid p30

policy considerations reflected in the doctrines of mitigation and remoteness...have proved strong enough for the courts to seek to incorporate them into many indemnities as a matter of construction'<sup>32</sup>. Applied here, the suggestion is that some courts may be driven by policy considerations, such as a 'desire to incentivise the avoidance of avoidable loss'<sup>33</sup>, and therefore incorporate the principles of remoteness and mitigation into their decision regarding a claim, and this has had an impact, explaining why some courts have determined that a breach of an indemnity entitles a party to a claim for damages rather than debt. This is certainly an interesting argument, and it is difficult to disprove. However, notwithstanding the reasoning for those decisions by the English courts, the fact they have taken that approach in some instances demonstrates the lack of consistency in this area.

The judge in the Durley House Case also relied extensively on a previous case in English law, where the House of Lords considered issues regarding indemnities at length. This case was *Firma C-Trade SA v Newcastle Protection and Indemnity Association*<sup>34</sup> (the "**Fanti Case**"). Note that this particular dispute was joined with another for consideration by the Law Lords.

The background to the Fanti Case was a cargo claim in respect of the loss of cargo on a motor vessel. The owners of the vessel had entered it in the P&I club, which it was a member of, and which protected and indemnified the members against losses for liabilities on the ship. The member did not defend itself against the claim from the cargo owners, and therefore judgment was entered against it in default, and the cargo owners were awarded damages with interest. However the judgment was not satisfied, and the member was then ordered to be wound up by the Companies Court. The cargo owners then brought an arbitration claim against the P&I club, seeking to rely on an indemnity against them under the Third Parties (Rights Against Insurers) Act 1930, as the member had been wound up. The arbitrator decided in favour of the P&I club, however this ruling was appealed through the courts. The claimant in this appeal is the cargo owner and the defendant is the relevant P&I club. The case considered complex issues of marine insurance law, and it is useful to note that the Law Lords accepted the arguments of the defendant, and upheld the 'pay to be paid' condition. The important aspect of this case for this article are the judgments delivered specifically on the issue of indemnities, which will be extracted from the decision for consideration here.

Lord Brandon, as part of the background to the case before the actual judgments of the judges, included the following declaration; "The starting point is the rule of the common law...the common law regarded a contract of indemnity as sounding in damages rather than debt"<sup>35</sup>. This presentation of the position in the common law regarding indemnities is evidently distinct from the previously considered rulings that present the contrary position that a breach of an indemnity gives rise to a claim in debt. Lord Goff, in his judgment in the Fanti Case, also suggested consistency with the presentation by Lord Brandon, and his words were also significantly relied upon in the judgement delivered by Morris QC in the Durley House Case. Lord Goff stated the following;

*"...a promise of indemnity is simply a promise to hold the indemnified person harmless against a specified loss or expense. On this basis, no debt can arise before the loss is suffered or the expense incurred; however, once the loss is suffered or the expense incurred, the indemnifier is in breach of contract for having failed to hold the indemnified person harmless against the relevant loss or expense."*<sup>36</sup>

These words by the esteemed judge are a clear rejection of the alternative perspective that indemnities give rise to a debt claim, and support the damages claim argument. However, while the Fanti Case 'has been supported in several subsequent cases, it is by no means universally agreed that all indemnities must necessarily imply a promise to "hold harmless", or even that the use of the expression

<sup>32</sup> D Foxton QC 'How useful is Lord Diplock's distinction between primary and secondary obligations in contract?' [2019] *Law Quarterly Review* 249 p 261

<sup>33</sup> *ibid*

<sup>34</sup> [1990] 3 W.L.R. 78

<sup>35</sup> *ibid* p16

<sup>36</sup> *ibid* p35-36

“hold harmless” in an indemnity necessarily results in a construction that a claim is to be characterised as a claim for unliquidated damages in respect of a breach of that promise<sup>37</sup>. The law has not yet definitively resolved this question. Reynoldson appears to go further and states ‘an indemnity is also different to a right to claim damages’<sup>38</sup>. However a deeper analysis of her position suggests that indemnities should not be viewed solely as provisions giving rise to claims for damages, but should be seen as broader than that. This appreciation for the lack of rigidity in determining breach of indemnity claims is important, and has formed the basis of this article. This article has sought to assess the state of play in English law on this matter, and has demonstrated that there are divergent approaches that the English courts have followed on this specific question of whether a breach of indemnity results in an action for debt or damages. There are respected judicial authorities for both positions, often heavily dependent on the facts of the case.

In his article on Lord Diplock’s distinction between primary and secondary obligations in contract, David Foxton QC looks at the application of that distinction in the context of indemnities<sup>39</sup>. A full breakdown and analysis of those terms is beyond the scope of this article, however it is useful to note that the terms primary and secondary obligations were used by Flaux J in his decision in the ABM Amro Case. In essence, Lord Diplock based his development on John Austin’s distinction between rights and duties that are principal or primary, and rights and duties that arise as a result of the violation of other rights and duties (and are therefore to be considered secondary)<sup>40</sup>. Debt claims are deemed to arise as a result of a breach of a primary obligation; a sum is owed under the contract and therefore the party who owes the sum has a primary obligation to pay. Claims for damages are generally perceived to arise as a result of a secondary obligation; a duty is owed under a contract and failure to perform that duty means that the party owes damages as a secondary obligation to make good that failure to perform the primary obligation duty. Foxton recognises that ‘the application of the distinction between primary and secondary obligations has proved particularly fraught in the context of contractual indemnities’<sup>41</sup>. He recognises the difficulty in developing a clear rule on how breach of indemnity claims should be classified under English law, and the rulings from the various cases presented supports this recognition. Although Foxton does then state ‘the dominant approach has been to classify the indemnitee’s right under a contractual indemnity as a secondary right’<sup>42</sup>, as he understands it to mean more a damages type approach. This would be supportive of the decision arrived at in the Durley House Case, and highlights the significance of the comments made as part of the judgment by the most senior court in English law at the time (the House of Lords) in the Fanti Case, as significant in this area. However his reference to a dominant approach doesn’t undermine the view that there is a lack of consistency and is not necessarily contradictory of his earlier statement that this area of the law is ‘fraught’. In fact, Foxton does later state that ‘it is suggested that there is a distinction between claims to enforce indemnities which are in the nature of debt and those which are in the nature of a claim for damages.....However, the practical application of that distinction and the consequences of the classification are not always satisfactory’<sup>43</sup>. Foxton is in essence recognising that English law is unclear on indemnities, and the resolution of the debt-damages distinction by the courts is currently inadequate.

There does not appear to be a clear single approach followed in English law on this question. It is apparent that at present, neither the debt claim approach nor the damages claim approach is always the correct approach for determining party liability for breach of a contractual indemnity. The facts of the case, and the construction of the indemnity are very important in resolving this question, and it is this fact dependent approach that often appears to be the overriding sentiment of the courts in resolving questions regarding indemnities. It is probably fair to say that notwithstanding the lack of consistency

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<sup>37</sup> N D’Angelo op.cit. p103

<sup>38</sup> M Reynoldson ‘Indemnity clauses – what are they, how do they work and how to make them work for you’ [2013] 24 *ILJ* 186 p4 as accessed via LexisNexis on 30 May 2019.

<sup>39</sup> D Foxton QC op.cit. p249. Lord Diplock developed this distinction between primary and secondary rights or obligations under a contract in the case of *Hardwick Game Farm v Suffolk Agricultural Poultry Producers Association Ltd (SAPPA)* [1966] 1 W.L.R 287; [1996] 1 All E.R. 309.

<sup>40</sup> *ibid* see John Austin, *Lectures on Jurisprudence or the Philosophy of Positive Law* (London: John Murray, 1885)

<sup>41</sup> *ibid* p258

<sup>42</sup> *ibid*

<sup>43</sup> *ibid* p259

and the apparent lack of absolute clarity, the courts have not been haphazardly applying the debt or damages remedy to resolve claims for breach.

## Understanding the different approaches

This article has so far demonstrated the different approaches that the English courts have taken with regards to dealing with breach of indemnity claims. There are two general remedies that the courts have applied, the debt claim and damages. What appears clear from reviewing the judgments is that the term indemnity covers a very wide range of different terms, and recognition of that is fundamental to understanding how the courts can arrive at different conclusions when ruling on their breach. The suggestion that ‘as it is a creature of its drafting, the indemnity is capable of infinite flexibility’<sup>44</sup> may appear to be too extreme a view, but it does help underline the difficulty in determining whether there is a correct approach, and further explains why the courts deliver rulings that do not appear to fit within a simple and consistent rule. Interpretation of the indemnity is of utmost importance when determining whether a breach gives rise to a claim in debt or for damages.

There are other instances where the English courts have considered the question of the interpretation of contracts, and this is relevant to consider here with regards to the interpretative approach followed by the courts in dealing with the breach of indemnities. In the case of *Wood v Capita Insurance Services*<sup>45</sup>, the UK Supreme Court considered the question of the interpretation of indemnities in contracts. The case concerned the sale of share capital in a company called Sureterm Direct Limited (“**Sureterm**”) by the owner of the shares Mr Wood, to Capita, who were the purchasers. A Share Purchase Agreement was executed by the parties in 2010, and included an indemnity, given by the purchasers Capita, in favour of Mr Wood. The indemnity effectively stated that Mr Wood would pay Capita for any losses that Capita suffered as a consequence of any action brought against Sureterm due to its selling process prior to the completion date of the sale transaction. An internal complaint was made shortly after the purchase about Sureterm’s sale process, the consequence of which was that Sureterm agreed a remediation plan with the FSA to pay compensation to affected customers. Capita then attempted to enforce the indemnity, which Mr Wood contested on the basis that the incident fell outside of the scope of the indemnity as the compensation had been paid as a result of an internal complaint and not a complaint made by an external party. As a result, Mr Wood claimed, the indemnity could not be said to have covered this sort of situation. The Supreme Court agreed with Mr Wood and dismissed the claim by Capita. Critically, it clarified the approach under English law to interpret indemnities, emphasising the importance of considering the drafting and literal meaning of the words presented, in addition to the commercial context of the indemnities and the nature of the contract in which the indemnities are set out. The indemnity should be considered in the context of ‘business common sense’<sup>46</sup> and in conjunction with the other provisions in the contract which helps shape and clarify its meaning.

This recent decision of the Supreme Court highlights the complexity in the interpretation of indemnities by courts under English law. It is important to note that the case serves as authority for interpretation generally, however as the subject to be interpreted here was an indemnity clause, it is a very useful reference point for the application of those developed contract interpretation rules to indemnities, in English law. The Supreme Court emphasised both the form and context of the indemnity as drafted in determining what it means, and the courts have steered away from rigid rules on interpretation. The decision confirmed ‘the validity of both literal and contextual approaches’ to interpretation<sup>47</sup>. This general approach is relevant in considering how the English courts have approached remedies for

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<sup>44</sup> N D’Angelo op.cit. p107

<sup>45</sup> [2017] UKSC 24

<sup>46</sup> Maitland Chambers case comment *Wood v Capita Insurance Services Ltd* accessed at

<https://www.maitlandchambers.com/information/recent-cases/wood-v-capita-insurance-services-ltd> on 30 May 2019

<sup>47</sup> C Dowling and A Denhom ‘Literal or Contextual? What is the Correct Approach to Contractual Interpretation?’ *Oxford Law Faculty Blog* (26 April 2017) accessed on 5 May 2019

breach of indemnities, as those courts attach considerable significance to the form of the indemnity presented in their analysis. In determining whether the indemnity gives rise to a claim in debt or damages, the drafting of the indemnity is thoroughly reviewed by the court, and ultimately this makes it difficult to argue that English law has developed a single consistent rule that would apply in all cases regarding breach of an indemnity.

The current state of English law appears to support the analysis in *Chitty on Contract*, which states that ‘the scope of the indemnity will therefore depend upon the wording of the particular clause and the intentions of the parties regarding it to be collected from the whole of their agreement’<sup>48</sup>. In response to the question whether breach of a contractual indemnity gives rise to a debt claim or a claim for damages, the position in English law appears to be that ‘the answer depends on how an indemnity is to be construed contractually’<sup>49</sup>. The evidence from the case law analysed in this article suggests that there does not appear to be a clearer response to the question than that.

In an attempt to narrow the scope slightly from a case by case judicial interpretation on the form of an indemnity, in determining whether breach gives a right to debt or damages, there has been some suggestion that the decisions fit within an understanding of indemnities that recognises broadly three groups: a reimbursement indemnity for a clear and specified sum which gives a right to a claim for debt; a reimbursement indemnity for a sum that is unspecified which gives rise to a damages claim; and finally a hold harmless indemnity which also gives rise to a damages claim<sup>50</sup>. This is certainly a useful analysis for practitioners, and could be said to provide parties with some general guidance in understanding indemnities and the consequences of adopting them in a contract. Crucially though, this attempt to develop some structure to understand indemnities is an acceptance that English law often perceives and interprets indemnities differently, which is not necessarily a bad thing, provided the courts are very careful in their analysis about why certain decisions are made.

Courtney emphasises this point, recognising that ‘contractual indemnities do not all possess the same set of characteristics’<sup>51</sup>, and this highlights the difficulty in applying rules about whether breach of those indemnities give rise to debt claims or damages claims. A determination that the courts should make a choice and apply a single view of indemnities as either giving rise to debt claims or damages claims for the sake of consistency is not particularly useful nor desirable. Such a simple approach would fail to capture the complexity of indemnities and would therefore not lead to the correct judicial outcomes in disputes. Courtney eschews the debt-damages approach in reviewing indemnities, and prefers instead to identify indemnities as either: a promise of prevention of loss, or a promise for compensation for loss<sup>52</sup>. The determination of whether an indemnity when breached gives a right to debt or damages should not be the focus of judicial enquiry of indemnity provisions generally, but rather the nature of the indemnity should be the focus. In essence, Courtney is accepting that the debt-damages question is not settled, nor should it necessarily be settled in absolute terms. The courts should not look to resolve the question of whether a breach of indemnity always results in a debt or a damages claim, nor should the courts view indemnities as being debt based or damages based. Both remedies should be available, and their application should be as a result of the interpretation of the indemnity in question. The complexity of the law of indemnities mandates a nuanced approach rather than a simple labelling of all indemnities or a particular type of indemnity as always being remedied by claims for debt or damages when breached. Courtney even accepts that his classification of indemnities as preventative or compensatory, in an attempt to establish a framework for review is ‘a useful schema for analysis but it does have limits’<sup>53</sup>. He states further that ‘some indemnities appear to be composite or, perhaps,

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<sup>48</sup> *Chitty on Contracts* op.cit. at para. 15-018

<sup>49</sup> N D’Angelo op.cit. p102

<sup>50</sup> Blake Morgan *Indemnities: a debt or damages claim?* (1 February 2016) p5

<sup>51</sup> W Courtney ‘The Nature of Contractual Indemnities’ (August 2011) *Sydney Law School Legal Studies Research Paper No. 11/41* p2

<sup>52</sup> W Courtney *Contractual Indemnities* (Hart Publishing 2015) see chapter 2 for a comprehensive analysis

<sup>53</sup> W Courtney n51 above p17

protean<sup>54</sup> and this does cause further complication. His description of indemnities is pertinent, and should highlight further the complex nature of indemnities under English law.

Rafal Zakrzewski, uses different terminology, but is in agreement with Courtney's general analysis. He recognises that 'there may be two different types of indemnity which potentially give rise to two different types of claim'<sup>55</sup>. He breaks this down to different types of primary rights, a 'prevent loss' indemnity which when breached will give a party a right to claim on a secondary obligation to pay damages, and a 'redress loss' indemnity which gives parties a right to a debt claim<sup>56</sup>. His suggestion is that by accepting that indemnities can give rise to these different remedies, 'we may be on our way towards solving the puzzle'<sup>57</sup>. This is consistent with arguments that the focus should be on proper analysis and interpretation of the indemnity to ensure that the appropriate remedy is available for breach, rather than attempting to determine what form of remedy is available for breach of an indemnity clause as a rigid rule in English law. The courts should steer away from judgments that present indemnities as falling into rigidly defined categories, and instead embrace a more nuanced approach that accepts the differences in indemnities and the need for the courts to have some flexibility in determining the appropriate context specific remedy for breach.

Any attempt to describe or understand an indemnity should look to the root of the indemnity and the content, rather than focus on the choice of remedy as its defining characteristic. Certainly there have been some judgments in the English courts prior to *Wood v Capita Insurance Services* that have aided confusion, by failing to sufficiently emphasise how fact dependent their rulings were. The significance of that ruling is that the highest court in the land, the Supreme Court, emphasised the importance of the interpretation of indemnities in determining how they apply, and clarified the approach to that interpretation. It does not appear that there will be any change on the horizon to the current situation in English law to judicially settle matters. The courts should directly address this question, and apply the more flexible and realistic proposals of Courtney or Zakrzewski. This would aid clarity and demonstrate a more logical and less confused understanding of this area in English law. Ultimately the responsibility is with those drafting indemnity clauses in contracts to ensure that they are drafted as clearly as possible and the available remedies are as clearly defined as possible on paper.

## Conclusion

The purpose of this article was to determine whether under English law a breach of indemnity gave a party a right to bring a claim for debt or a claim for damages. It has been shown that there is support for both approaches in the English courts. There have been judgments that recognised breaches of indemnities as giving rise to debt claims, and there have also been judgments that pursued the damages claim approach. The clearest evidence of that apparent judicial division are the High Court rulings in the *ABM Amro Case* and the *Durley House Case*, in the same year. The basis for that lack of judicial coherence appears to be the very complicated nature of indemnities, and the fact that the construction of indemnity provisions within contracts differ wildly. As a consequence, it has been difficult for the English courts to pursue only one approach, and it is ultimately preferable that cases are decided in a manner cognisant of the complexity of this area. What has been missing is direct judicial recognition of that complexity in judgments, and the development of a consistently applied set of rules that attempt to capture that complexity.

The answer to the question whether English law recognises breaches of indemnity as sounding in debt or damages is that it can apply either remedy depending on the situation, and that lack of rigidity is not a bad thing. What has been made clear in this article is the importance of the drafting of the indemnity and the commercial context of the contract and relations between the parties. The Supreme Court has

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<sup>54</sup> *ibid*

<sup>55</sup> R Zakrzewski *op.cit.* p55

<sup>56</sup> *ibid*

<sup>57</sup> *ibid* p70

recently emphasised the importance of context and construction to properly interpret an indemnity clause. The courts generally should now look carefully at these factors in their assessment of the indemnity, and should hopefully more deliberately and audibly use that interpretive exercise to develop rules on this subject.

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# Prest v Petrodel Resources Limited: The veil finally pierced?

Mohammad El-Gendi

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## Introduction

The case of *Prest v Petrodel Resources Ltd & Others*<sup>1</sup> could establish certainty to the doctrine of piercing the corporate veil. Namely, the judgment of Lord Sumption is most enlightening, introducing two principles that allow the distinction between true piercing the corporate veil and mere lifting to be better established.

However, there remain a few unclear, yet fundamental, aspects to the case. In particular, the judgment of Lord Sumption fails to provide sufficient clarity to the overlap and interrelation between the two principles, as well as casting unnecessary doubts over the sham/ façade doctrine. Furthermore, the judgment should have gone further so as to foreclose any further expansion of the doctrine beyond its current boundaries.

The article will begin by introducing the key concepts and mischiefs related to the doctrine. After this, it will examine the judgments of *Prest*, namely Lord Sumption's principles of evasion and concealment. Then it will be necessary to consider the overlap between these principles and the impact of the uncertainty created around the sham/ façade doctrine. Finally, the article will conclude by remarking on the need to prevent any further expansion of the doctrine of piercing the corporate veil beyond its current tenants laid down in *Prest*.

## Salomon v A Salomon & Co Ltd<sup>2</sup>

### Principle and 'mischiefs'

Like with any company law discussion, it is necessary to start at the foundations: *Salomon*.

At its core, and relevant to the question of piercing the corporate veil, *Salomon* represents the tension between the mischiefs of certainty and accountability. On the one hand, shareholders need a sense of certainty at the time of incorporation and throughout the lifetime of the company, knowing that the company possess a distinct legal personality with limited liability to the shareholders. However, equally, the accountability of shareholders in certain situations is also key. Traditionally, this accountability has been to the company's creditors, both voluntary and involuntary<sup>3</sup>. In more recent years, it might also be suggested that this accountability extends to a more societal audience whereby society as a whole demands the accountability of shareholders' actions and behaviour, in a hope for more ethical company practises.

Of course, this is not to say that where there is greater accountability, there is less certainty. Accountability can also be certain, provided there are consistent judicial rulings which outline the scope of this accountability. Thus, in this sense, the antithesis of 'accountability' is certainty of freedom from liability. Freedom from liability is important because it incentivises risk-taking. This risk-taking is a feature of entrepreneurship. Too much red-tape could potentially stifle companies from profitable business – an unappealing prospect as we dive into forging a new path with states.

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<sup>1</sup> *Prest v Petrodel Resources Ltd* [2013] UKSC 34.

<sup>2</sup> [1896] UKHL 1.

<sup>3</sup> This may include groups of people who suffer a tort at the hands of the company. For instance, see *Adams v Cape Industries plc* further in this discussion on the involuntary creditor relationship created between the employees and the subsidiary company, and whether the veil could be pierced between the subsidiary and parent companies.



## Facts

In this case, Mr Salomon was a sole trader<sup>4</sup> in leather specialising in boot manufacturing. In 1892, Salomon incorporated his business as a limited company under the Companies Act 1862.<sup>5</sup> The formalities for incorporation were similar to what is required today but with the main difference being that, under the 1862 Act, there needed to be a minimum of seven subscribers to the company. Now, only one shareholder is needed for incorporation (the one-man company).

To meet this requirement of seven shareholders, Salomon cleverly issued 20,007 shares to himself and six shares to six members of his family (one per person). A key contention in the case, was that this was a fraud due to the practical reality being that Salomon was operating the business singularly.

Salomon went on to sell the company receiving, inter alia, £10,000 in debentures (which he assigned to a third party). Therefore, he was both the company's principal shareholder and secured creditor. By being the principal *secured* creditor, Salomon was entitled to protection to ensure that the liquidator used the remaining company assets to secure the £10,000 in debts before any unsecured creditors.

When the company went insolvent, the liquidator tried to argue that they should not have to pay to Salomon because he was using the company structure fraudulently. Salomon's arrangement of setting up a limited liability company was a sham and therefore the incorporation should be set aside. Consequently, the company (Salomon & Co Ltd) was merely an agent of Salomon (as a person) and so Salomon should be forced to use his assets to indemnify the unsecured creditors.

## High Court (first instance)<sup>6</sup>

At first instances, Vaughan Williams J agreed with this argument. He reasoned that the company and Mr Salomon were one and the same, a single unit, of agent and principal. Therefore, he was liable to pay the unsecured creditors directly as principal.

However, such reasoning was circular and, therefore, troublesome. On the one hand, Vaughan Williams J acknowledged that the transaction was a sham but equally concluded that the shareholder-company relationship could be classed as agency. Therefore, the thing did not exist but existed. More precisely, the incorporation did not exist (because it was a sham) but, equally, the relationship between Salomon and the company was that of a principal and agent.

Also, troubling, but as a matter of law, the company was issued with a certificate of incorporation. As stated in s.15(4) of the Companies Act 2006, the effects of registration is "*conclusive evidence that the requirements of this Act as to registration have been complied with and that the company is duly registered under this Act.*"<sup>7</sup> It would seem clear, from the Act, that a certificate of incorporation is an authoritative legal document confirming the legal status of the company, endowing it with the characteristics found in s.16 (effects of registration). Therefore, it is difficult to understand Vaughan Williams J's reasoning, which would directly contradict these absolute terms.

## Court of Appeal<sup>8</sup>

Though the Court also ruled against Salomon, they did so on different reasoning. They argued that the way in which Salomon made himself principal shareholder of the company violated the true intent and

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<sup>4</sup> On the differences between sole trading and limited company, see Sealy, L. S., and Sarah Worthington. *Cases and Materials in Company Law*. Oxford University Press, 2010, 24.

<sup>5</sup> Companies Act 1862.

<sup>6</sup> *Broderip v Salomon* [1893] B 4793.

<sup>7</sup> Companies Act 2006, s.15(4).

<sup>8</sup> *Broderip v Salomon* [1985] 2 Ch 323.

meaning of the Act. As Hannigan puts it, “[i]n essence, he was a sole trader screening himself from liabilities and as such [the company] was a device to fraud creditors.”<sup>9</sup>

So opposed to allowing this unconscionable behaviour, Lopes LJ felt positioned to say, “it would be lamentable if a scheme such as this could not be defeated” (emphasis added).<sup>10</sup>

## House of Lords

However, the House of Lords reaffirmed the separate legal personality of the company, endowed with limited liability. It concluded that the company was not an agent for Mr Salomon. Issuing a bulk of shares to one person does not create an agency relationship because the company is absolutely distinct from its shareholders. This is reflected in the (now) Companies Act 2006, section 16(2).<sup>11</sup> The effect of this is that the company is able to possess its own rights and obligations, independently of any shareholder.<sup>12</sup>

It is important to be clear that this was merely a *reaffirmation* of what was already law— not the establishment of a new principle as it can be inaccurately suggested.<sup>13</sup> The law before (and after the House of Lords decision) Salomon was very similar to what is found in the 2006 Act – namely that incorporation created limited liability up to the extent of paid capital on shares.

Arguably, the Court’s reasoning here was sound and right to overturn the decision of the Court of Appeal. As Lord Macnaghten rightly pointed out, the 1862, and even 2006, Acts make no provision for how many shares must be allotted<sup>14</sup> to any individual person.<sup>15</sup> Therefore, there is no basis in the Act to conclude that the allotment of 20,007 shares was against the purpose and intent of the Act (as argued in the Court of Appeal). Returning to the mischief, shareholders need a degree of certainty as to what they can and cannot do. To that end, it would create too much uncertainty for shareholders when allotting shares. Other than what is required in law, shareholders should not have to make considerations on the basis of creditors, secured or not.

This attitude is reflected in the lack of sympathy<sup>16</sup> the House of Lords had for the unsecured creditors who were duly noted that they were no longer dealing with Salomon (the individual) but rather Salomon & Co Ltd (the company). As further pointed out in *MacDonald, Dickens & Macklin v Costello and another*<sup>17</sup>, if A (unsecured creditor) wants to protect themselves against B’s limited liability as shareholders, A should seek personal guarantees from B. Of course, the obvious counterargument is that economic realities often mean that such a bargaining position is not available to A as well as this creating a distrusting tone between A and B.<sup>18</sup>

Though this is not wrong, these economic realities fall to the very specific facts of the case and parties. The general rule of thumb that should be taken is that of limited liability, and seeking to avoid this should be done through personal guarantees. Not to mention, also, that it would be problematic and complicated to try and account for legal rules that protect A. Sometimes, it is necessary for risk to lay where it sits.

<sup>9</sup> Hannigan, Brenda. *Company Law*. Corporate responsibility. 5th ed., Oxford University Press, 2018, 41.

<sup>10</sup> [1895] 2 Ch 323 at 340 – 1.

<sup>11</sup> Companies Act 2006, s.16(2).

<sup>12</sup> *Lee v Lee’s Air Farming Ltd* [1960] UKPC 33.

<sup>13</sup> For instance, Hannigan states, “[t]his fundamental principle of company law [the Salomon principle] was established by the House of Lords in *Salomon v Salomon & Co Ltd*. [emphasis added]” (n.9).

<sup>14</sup> On the distinction between the allotment and issue of shares, see Sealy, L. S., and Sarah Worthington. *Cases and Materials in Company Law*. Oxford University Press, 2010, 509.

<sup>15</sup> [1897] AC at 53.

<sup>16</sup> Hannigan, Brenda. *Company Law*. Corporate responsibility. 5th ed., Oxford University Press, 2018, 42.

<sup>17</sup> [2011] EWCA Civ 930.

<sup>18</sup> A range of judicial and academic arguments have been made in favour of this more interventionist approach. See, for instance *Crossco No 4 Unlimited v Dolan Ltd* [2012] 2 All ER 754 per Arden LJ at 133 and Ben-Shahar and J Pottow, ‘On the Stickiness of Default Rules’ (2006) 33 Florida State UL Rev 651, 682. Both of these are arguments raised in relation to pre-contractual liability but apply equally here on a point of commerciality.

## Conclusion

Therefore, *Salomon v Salomon & Co Ltd* demonstrates the key policy consideration at the core of limited liability and piercing the corporate veil. As shown, the House of Lords were right to turn the tide in favour of Salomon. Creative compliance<sup>19</sup> should not be at the detriment of the incorporator. Otherwise a shareholder would never be able to ascertain what their obligations and liabilities might be when incorporating a company.

This debate forms a key aspect of the rest of the discussion over 100 years on into *Prest v Petrodel Resources Ltd*.

## Prest v Petrodel Resources Ltd

In the judgments of the Supreme Court, it was unanimously agreed that piercing the corporate veil is a legal concept that must be retained. However, to what extent, and in what circumstances, is where the Court was less consistent. For example, Lord Clarke rejected the distinction of evasion and concealment principle<sup>20</sup> and Baroness (then, Lady) Hale<sup>21</sup> questioned whether these two principles alone were sufficient to account for all cases. She queried whether,

*“They may simply be examples of the principle that the individuals who operate limited companies should not be allowed to take unconscionable advantage of the people with whom they do business.”*<sup>22</sup> (emphasis added)

It is interesting to note that Lord Sumption and Neuberger did question whether piercing the corporate veil ever existed.<sup>23</sup> However, they ultimately felt that there was sufficient normative reason for its existence as a means of holding shareholders to account.<sup>24</sup> Whilst it was unnecessary for Lord Neuberger to cast doubt over a doctrine that most accept does exist, as the rest of the Court did, it is good that he highlighted its importance ultimately as a mechanism of accountability. Particularly, acknowledging the existence of the doctrine ultimately acts as a clear deterrence to shareholders from behaving in certain ways that might make them liable.

As was alluded to earlier, Lord Sumption’s judgment provides the greatest food for thought. In this judgment, he presents two principles: evasion and concealment. Evasion constitutes true piercing of the corporate veil, whereas concealment reflects the act of lifting the veil. This article will now turn to evaluate these two principles and their overlap.

## Evasion: the true piercing of the corporate veil

### Pre-existing legal obligation...

Restating many past cases, here, the Court held that it would only pierce the veil where there has been an evasion of a pre-existing legal obligation. In doing so, the judgment of Lord Sumption upheld and maintained a clear notion of corporate veil piercing.

<sup>19</sup> For an interesting discussion on whether creative compliance in the company law setting is sufficient, see Doreen McBarnet, ‘After Enron Will ‘Whiter than White Collar Crime’ Still Wash?’ (2006) 46 Brit. J. Criminol 1091.

<sup>20</sup> [2013] UKSC 34, 103.

<sup>21</sup> Ibid, 92. See more on this at “Foreclosing further expansion?”

<sup>22</sup> Ibid, 506.

<sup>23</sup> For example, see Lord Sumption at 27.

<sup>24</sup> Ibid, 502.

For example, in *Gilford Motor Home v Horne*<sup>25</sup>, Horne was the director of Gilford Motor Home. He had entered into an agreement (restrictive covenant) with his former employer that he would not enter into a directly competing business with the company once he left. To evade this obligation, Horne incorporated a company which was involved in the same market with Horne's prior employers.

As mentioned earlier, the case of Salomon reaffirmed separate legal personality and so, on this basis, Horne was able to avoid his legal obligation by arguing he was distinct from the company he incorporated. Whilst Horne continued to have the restrictive covenant agreement, the company did not. In this respect, the interest of certainty with regard to the legal distinction between the metaphor of the company<sup>26</sup> and the shareholder is key.

However, the Court, in line with the countervailing interest of accountability, held that

*"[t]he purpose of [the company] was to try to enable him, under what is a cloak or sham, to engage in business which, on consideration of the agreement which had been sent to him [...] was a business in respect of which he had a fear that the plaintiffs might intervene and object".*<sup>27</sup>

Equally, in *Jones v Lipman*<sup>28</sup>, Lipman contracted to sell a house to Jones, thus creating a legal obligation between the parties, existing before the incorporation of any company. In order to avoid a specific performance order, Lipman then went on to incorporate a company and transferred the property to that company which did not possess the specific performance obligation. However, the Court saw it fit to pierce the corporate veil as Lipman had sought to evade a pre-existing legal obligation whereby Russell J noted,

*"[the company is] the creature of the first defendant, a device and a sham, a mask which he holds before his face in an attempt to avoid recognition".*<sup>29</sup>

On the other hand, the Court cannot pierce the corporate veil because there was no evasion of a pre-existing legal obligation, which was confirmed *Adams v Cape Industries plc*<sup>30</sup>. Here, Cape Industries was head of a group of subsidiary companies. One of the subsidiaries had caused its employees to develop asbestosis giving rise to a tortious claim. However, as the subsidiary did not have the necessary funds to meet the judgment summary, the claimants sought to join Cape Industries to the proceedings.

The Court unanimously rejected the arguments of the claimants. The Court held that the point of piercing the corporate veil was that the claimant had to be evading an obligation it already owed. The setting up of subsidiaries, in order for a parent company to avoid hypothetical and potential liabilities, was the avoidance of *future* legal obligations. These do not constitute grounds for piercing the veil.

### ... and only pre-existing legal obligation

Further adding to this clarity, Lord Sumption, along with Lord Neuberger, reaffirmed, what had now been settled by previous case law: that there was no piercing of the corporate veil beyond the factual situation of evasion of a pre-existing legal obligation. It was arguably important for the justices of the Supreme Court to provide a firm and final judgment on this, as the case law on the matter has seen a pendulum between judicial interventionism and conservatism.

Over several cases, the courts, in a reaction to the tensions of accountability, introduced greater avenues of piercing the corporate veil. However, arguably, doing so came at the great expense of certainty for companies and shareholders.

<sup>25</sup> [1993] Ch 935, CA.

<sup>26</sup> As capable of possessing legal rights and obligations.

<sup>27</sup> [1993] Ch 935, CA per Lord Hanworth MA.

<sup>28</sup> [1962] 1 WLR 832.

<sup>29</sup> *Ibid*, 836.

<sup>30</sup> [1990] BCLC 479.

## Single Economic Unit (SEU)

It has been argued that the adherence to such a strict notion of companies, as each being its own distinct character, is not suitable for the modern business world. So much so, that Lord Denning in *DHN Food Distributors Ltd v Tower Hamlets LBC*<sup>31</sup>, pointed out that “[t]his case might be called the “Three in one.” Three companies in one.” This has often been referred to as the Single Economic Unit argument. The elaborate mechanisms in which group structures interact with each other is often argued as something could never have been contemplated by the court in the case of *Salomon*. As such, there is some support<sup>32</sup> for Lord Denning’s ability to look beyond technicalities and into the reality of the corporate structure: a single unit of economic activity.

However, ever since this case, the courts have consistently held, and strongly affirmed by *Prest*, that there can be no recourse to piercing the corporate veil by means of an SEU argument. As noted earlier, the claimant in *Adams* made an argument of single economic unit. However, this was rejected by the Court who stated that,

*“[...] save in cases which turn on the wording of particular statutes or contracts, the court is not free to disregard the principle of Salomon v Salomon & Co Ltd merely because it considers that justice so requires. Our law, for better or worse, recognises the creation of subsidiary companies, which though in one sense the creatures of their parent companies, will nevertheless under the general law fall to be treated as separate legal entities with all the rights and liabilities which would normally attach to separate legal entities [...]”*<sup>33</sup>

Clearly, the language of the Court of Appeal acknowledges the mischief of “justice” or accountability and the certainty of saying that a company (parent or subsidiary) is a separate personality. Arguably, the Court was correct to argue against the notion of the SEU, opting instead of certainty through a narrower notion of piercing the corporate veil. To that end, Lord Sumption’s judgment in *Prest* is commendable for putting a clear end to any confusion or uncertainty by reaffirming cases such as *Adams* and *Woolfson*<sup>34</sup>.

## Interests of justice

In addition to the notion of an SEU argument, the case law has experienced judicial back and forth in relation to an ‘interests of justice’ argument. *Prest* is good in that, again, it provides a clear end to a long line of questionable case law. In *Re A Company*<sup>35</sup>, a 1985 case, the Court held “*in our view the cases show that the court will use its powers to pierce the veil if necessary to achieve justice*”. This clearly demonstrates the courts willingness, in cases of clear breaches of justice, to pierce the corporate veil, doing what is necessary to hold shareholders to account.

The danger with opening up the avenues of litigation to notions of interests of justice is that it is unclear, and possibly impossible to define what this phrase means. Whilst it is important to ensure a degree of accountability, that might create open-ended questions about what constitutes accountability, the language of interests of justice is far too wide. It too strongly corrodes the stability of clear language and certainty.

In 1990, with the case of *Adams*, the court held “the court is not free to disregard the principle of *Salomon v Salomon & Co Ltd* merely because it considers that justice so requires”. Thus, clearly on the other side of the spectrum, *Adams* is advocating that justice is not itself a sufficient basis in which to pierce.

<sup>31</sup> [1976] 3 All ER 462.

<sup>32</sup> [1976] 3 All ER 462, 467.

<sup>33</sup> [1990] BCLC 479, 513.

<sup>34</sup> *Woolfson v Strathclyde Regional Council* [1979] 38 P & CR 521.

<sup>35</sup> (1985) 1 BCC 99.

The confusion is then furthered three years later by *Creasy v Breachwood Motors Ltd*<sup>36</sup> where it distinguished from *Adams* by arguing that justice would not be done if the court found in favour of the claimant. However, it did not actually explain why it was distinguishing from *Adams*. Then, in 1998, the court in *Ord v Belhaven Pubs*<sup>37</sup> held, alongside *Adams*, that a company would not face piercing the corporate veil because of some argument of justice.

At this point, one would be forgiven for not knowing what the law was on the point of an interest of justice. However, arguably, *Prest* in reaffirming *Adams* and other cases like *Ben Hashim*<sup>38</sup>, has arguably ended this long saga of confusion. Munby J in *Ben Hashim* clearly stated that,

*“The court cannot pierce the corporate veil [...] merely because it is thought to be necessary in the interests of justice [...] I take the view that the dicta to that effect [...] in In re a Company [1985] [...] have not survived what the Court of Appeal said in Cape”.*<sup>39</sup>

Therefore, *Prest* neatly narrows the scope of piercing the corporate veil to the evasion principle, defined as escaping pre-existing obligations. No other avenues can be open to pierce the veil, neither economic realities nor notions of justice.

## Sham/façade

For all that can be said on the success their judgments brought, the first major issue with *Prest* is how Lord Sumption and Neuberger’s dealt with the issue of the long-standing use of the terms of sham and façade in the case law. For example, in *Woolfson*, the Court held, “[...] *it is appropriate to pierce the corporate veil only where special circumstances exist indicating that it is a mere facade concealing the true facts [...]*”.<sup>40</sup> Also, in *Jones v Lipman*, the Court needed to be satisfied, in piercing the corporate veil, that the company was “*a device and a sham, a mask which he holds before his face in an attempt to avoid recognition in the eye of equity*”.<sup>41</sup>

In *Prest*, Lord Sumption held the view that “[t]he difficulty is to identify what is a relevant wrongdoing. References to a “facade” or “sham” beg too many questions to provide a satisfactory answer.”<sup>42</sup> To that end, the use of such term is “legally banal” and is only a starting point of enquiry rather than a conclusion of facts. At the heart of their concern was that the terms sham and façade are too ambiguous to be used seriously; it is unclear what exactly constitutes sufficient practise to call a company’s circumstances a sham or a façade. Further, they were concerned that any definition of a sham/façade would be too wide, encroaching on the interests of certainty as to the doctrine of separate legal personality.

However, arguably, such a view is not correct. The courts have been very clear, and narrow, in their definition of a sham/façade. As such, they have been able to provide clear guidelines as to when a company’s evasion of pre-existing legal obligations constitutes a sham or façade, cloaking them from such obligations.

## Mere ownership and control

*Ben Hashem* presents a good case that brings together the several case law that has developed the meaning of sham/ façade, providing both a positive and negative account of the doctrine. First, mere ownership and control of the company is not sufficient to suggest the company is being used as a sham

<sup>36</sup> [1993] BCLC 480.

<sup>37</sup> [1998] 2 BCLC 447.

<sup>38</sup> [2008] EWHC 2380, 160.

<sup>39</sup> *Ben Hashem v Ali Shayif and Another* [2009] 1 FLR 115, 160.

<sup>40</sup> [1979] 38 P & CR 521, per Lord Keith

<sup>41</sup> [1962] 1 WLR 832, 836.

<sup>42</sup> [2013] UKSC 34, 28.

or façade. One-man companies such as that of Saloman and many of the other cases cited does not denote, of itself, the company being used for a purpose sufficient to pierce the corporate veil.

## Impropriety

Second, there has to be evidence of impropriety. However, this is narrowly construed as being when the defendant uses the company structure for the purpose of avoiding or concealing an existing legal obligation. As was pointed out in *Trustor AB v Smallbone*, “companies are often involved in improprieties”<sup>43</sup> When

*“[...] it would make undue inroads into the principle of Saloman v Saloman & Co. Ltd if an impropriety not linked to the use of the company structure to avoid or conceal liability for that impropriety was enough.”*<sup>44</sup>

In *Ben Hashem*, the court stated,

*“[...] in each of the cases the wrongdoer controlled the company, which he used a façade or device to facilitate and cover up his own wrongdoing – in the first two cases [Gilford; Jones] as a means of breaching a contract, in the latter two cases [Gencor; Trustor] as a means of receiving money for which he was accountable. In other words, in each of these cases there were present twin features of control and impropriety.”*<sup>45</sup>

The important point here is that the Court is not saying that ownership or control alone is sufficient. Rather, it is the ownership and control used for an improper purpose, namely that purpose being the evasion of a pre-existing legal obligation.

In summarising the claim, Mr Justice Munby stated,

*“[the claimant] asserts that, as a matter of law, control of a company (even if established, which of course she disputes) is not sufficient to permit a court to pierce the corporate veil. There has to be some relevant form of impropriety, that is, [the claimant] says, some impropriety or wrongdoing by an individual – here the husband – in which the company structure is being used by the wrongdoer so as to avoid personal liability for his wrongdoing.”*<sup>46</sup>

Then, His Lordship went on to agree with this summarisation of the law, finding that “I accept both Miss Evans-Gordon’s analysis of the law and her analysis of the facts.”<sup>47</sup> Thus, this demonstrates that ownership, control and/ or impropriety may play a part in finding a sham or façade. However, and importantly, this is not simply a case of finding one or more elements. Rather, the use of ownership or control must be for the aforementioned improper purpose of evading a pre-existing duty.

## Time of the transaction

As a final point to the definitions given to the doctrine of sham/façade,

*“a company can be a façade even though it was not originally incorporated with any deceptive intent. The question is whether it is being used as a façade at the time of the relevant transaction(s).”*<sup>48</sup>

<sup>43</sup> [2001] 2 BCLC 436, 22.

<sup>44</sup> Ibid.

<sup>45</sup> [2009] 1 FLR 115, 171.

<sup>46</sup> Ibid, 190.

<sup>47</sup> Ibid, 192.

<sup>48</sup> Ibid., 164.

Therefore, not only does it seem very clear what a sham/ façade is, it also seems the courts have been wary to ensure that the definition does not respects the line drawn by *Salomon*.

It is a shame, then, that Lord Sumption and Neuberger cast doubt on this doctrine, citing reasons that were unfounded. The consequence of this is, now, uncertainty over the future of the doctrine and its role it should play in such cases. Arguably, it has been demonstrated that the courts have been able to tame such a doctrine, and so it should survive past the questions raised in *Prest*. The courts ought to address this issue directly stating its position one way or another (preferably in favour of the principle) in order to iron out this vagueness.

## Concealment

As the doctrine is referred to as “piercing” the corporate veil, it is no surprise that the concealment principle has not received as much attention as it perhaps ought. In its simplest terms, the concealment principle is when the courts do not pierce the veil as above. Instead, it merely lifts the corporate veil to unmask the true legal relationship. As Lord Sumption put it, “[i]n these cases the court is not disregarding the “facade”, but only looking behind it to discover the facts which the corporate structure is concealing.”<sup>49</sup> For example, in *Prest* itself, the veil was lifted to reveal a trust relationship, whereas in *Chandler v Cape plc*<sup>50</sup>, the legal relationship was tortious. *Prest* does a commendable job of distinguishing the core of this principle from the evasion principle, highlighting its theoretical and practical distinction, keeping in line with previous case law.

In *Chandler*, Arden LJ held that the defendant company has assumed a duty of care over the employees of its subsidiary due to the particular facts of that case. Here, the relevant factors including the fact that the parent company was in the same line of business as the subsidiary, it had long experience in the industry which gave it superior knowledge of health and safety issues, the parent ought to have reasonable known that the subsidiary company’s work environment was unsafe and they ought to have foreseen that subsidiary company would rely on the parent company’s experiences.

Critically, she elucidated that this was not a case of piercing the veil but a reinforcement of *Salomon* by recognising that the parent and subsidiary were separate legal entities such that one could assume duty of care over the other. Therefore, there was no need to pierce any veil. All the Court had to do was lift the veil to reveal the duty of care relationship in tort<sup>51</sup> that gave rise to the liability.

This case strongly represents the clear distinction between the legal taxonomy and economic reality in the organisation of corporate groups where the courts have consistently disregarded the latter. As mentioned earlier, *Adams* firmly rejects the notions of an economic structure capable of undermining the separate legal entities of different companies within a group context. Arden LJ’s judgment reaffirms this idea, strengthening the consistency across case law, by allowing one company to have obligations to another within the same group.

Such a judgment cannot be understated in its importance as it realises that there is a fundamental, conceptual distinction between legal taxonomy and practical reality. To conflate the two, would be to not appreciate the differences whilst also damaging the certainty of the doctrine.

Importantly, though the effects of piercing and lifting the corporate veil may seem similar, particularly in this case, they have clearly defined separate principles.

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<sup>49</sup> [2013] UKSC 34, 28.

<sup>50</sup> [2012] EWCA Civ 525.

<sup>51</sup> *Caparo Industries plc v Dickman* [1990] UKHL 2.



This clear legal distinction was then built upon by *HRH Emere Godwin Bebe Okpabi v Royal Dutch Shell*<sup>52</sup>. Fraser J stated that when looking at the principles laid down in *Chandler*, it was important to consider two further questions.<sup>53</sup>

First, whether the parent company was better placed than the subsidiary to protect the employees of the subsidiary company? In case this question is answered in the affirmative, the second question rises, namely whether it is fair to infer that the subsidiary would rely on the parent company (developing further, also, on the reasonableness test in *Caparo Industries plc v Dickman*<sup>54</sup>). This case clearly accentuates the characteristics of *Chandler* by reaffirming the distinction it recognised.

## Overlap: an unclear distinction

For the many successful aspects of *Prest* and of Lord Sumption's judgment, there is a large issue that remains unresolved. Namely, there is the relationship (or overlap) between the two principles. Considering how the case law, including *Prest*, has struggled with the determining whether the facts are indicative of piercing or lifting, it is surprising more time was not taken to carefully consider the distinction to avoid confusion.

The stakes of this confusion are best seen in the case of *Trustor AB*. In this case, the original decision was that it was an evasion of a pre-existing legal obligation; that obligation being the duty not to misappropriate the property. However, Lord Sumption and Neuberger, in *Prest*, redefined this case as a concealment (lifting) case.<sup>55</sup> They reasoned that the defendant's hiding of the property into the new company made the company an agent of the defendant. Thus, the invoked, pre-existing law that was concealed behind the shrouds of the company was agency law.

Far from resolving this question, *VTB Capital plc v Nutritek International Corporation*<sup>56</sup> heightens the lack of clarity between the two principles. On the one hand, the Court held that *Trustor AB* was a good restatement of the law and, so, reaffirming that it was an evasion case. On the other hand, *VTB* was decided after *Prest* – though in the same year. As the case came after *Prest*, yet seems to contradict in its attitude towards *Trustor AB*. Hannigan sensibly puts the issue in context. She notes that the line between evasion and concealment is hard to distinguish especially considering particularly if evasion can often be achieved through concealment.<sup>57</sup> For instance, in *Trustor AB*, evasion was achieved by hiding (concealing) the whereabouts of the misappropriated property. Consequently, the facts can be easily manipulated to fit the language of either evasion or concealment.

Does this mean that the Supreme Court in *Prest* intended to contradict *VTB* on this fundamental point about *Trustor AB* or does the issue remain open? The answer is simply unclear.

Nevertheless, there is a possible solution that can be found in the judgments of several cases. In *Prest*, Lord Mance stated the following,

*“What can be said with confidence is that the strength of the principle in Salomon’s case and the number of other tools which the law has available mean that, if there are other situations in which piercing the veil may be relevant as a final fall-back”.*<sup>58</sup>

Likewise, in *Ben Hashem*, Munby J refused to pierce the corporate veil on the grounds that the claimant could have alleged a claim in fraud. This position was supported by Lord Clarke in *Prest*.<sup>59</sup>

<sup>52</sup> [2017] EWCH 89.

<sup>53</sup> *Ibid*, 79.

<sup>54</sup> [1990] UKHL 2.

<sup>55</sup> [2013] UKSC 34, 32.

<sup>56</sup> [2013] UKSC 5.

<sup>57</sup> Hannigan, Brenda. *Company Law*. Corporate responsibility. 5th ed., Oxford University Press, 2018, 58.

<sup>58</sup> [2013] UKSC 34, 100.

<sup>59</sup> *Ibid*, 103.

To that end then, piercing the corporate veil, as distinguished in *Prest*, is a tool that should only be called upon by the court as a last resort. Only when other mechanisms have been exhausted, is it then appropriate for the courts to consider the line of enquiry for evasion.

Naturally, such a last resort has the negative effect of meaning that there is little opportunity for successive courts to discuss piercing the corporate veil. Considering the arguments made, whereby there still remain unclear aspects, this may leave such issues unresolved for a while (at least in any *ratio decidendi* case law). As Lord Mance rightly noted, such an approach is likely to create “novel and very rare” cases of true piercing the corporate veil.

Ultimately, however, the last resort principle is appropriate. Most importantly, it shows deference to the mischief of certainty and accountability. The principle allows for the practical effects of accountability without needing the court to flagrantly chip away at the certainty of a more narrowly defined notion of piercing the corporate veil. The clear issues between cases that have sought to widen and restrict the scope the doctrine have represented the ongoing struggle between the two mischiefs. At least with this principle, a balance between the two is more harmoniously met.

It should be stressed that there is a clear difference between this distinction creating rare and novel cases, and it is edging closer towards the abolition of the doctrine.<sup>60</sup> Admittedly, the practical value of the doctrine is reduced and may give off the impression of abolition for all practical purposes. However, there remains a clear public policy reason for this doctrine to exist, as a means of exercising accountability against shareholders who misuse the benefits of separate personality. It is extremely unlikely the Court in *Prest* ever intended to abolish this doctrine, despite remarks questioning its existence, mainly due to the recognition of its important common law role in regulating the activities of shareholders.

## Foreclosing further expansion?

The effect of their Lordships' judgments in *Prest* was to restrict the use of the doctrine to rebalance the mischiefs. That has, by and large, been achieved. However, in doing so, one last major question arises as to the possibility of future expansions of the doctrine.

Baroness Hale seemed also to question the strictness of Lord Sumption's approach but in a much wider way. She queried,

*“I am not sure whether it is possible to classify all of the cases in which the courts have been or should be prepared to disregard the separate legal personality of a company neatly into cases of either concealment or evasion.”*<sup>61</sup>

Here, Hale seems to be suggesting that further expansion is possible as straightjacketing the doctrine into two principles may not be sufficient.

More directly, Lord Mance said, “[i]t is however often dangerous to seek to foreclose all possible future situations which may arise and I would not wish to do so.”<sup>62</sup> Equally, Lord Clarke concurred, “I agree with Lord Mance that it is often dangerous to seek to foreclose all possible future situations which may arise and, like him, I would not wish to do so.”<sup>63</sup>

It is understandable why their Justices would take such a cautious approach. It is ill-advised to foreclose the expansion of any legal doctrine; firmly cementing a rule can lead to rigid and absolutist principles that do not accommodate the changing nature of things. The mischief, as has been regularly referred to throughout, reflects the need for law, and indeed society as a whole, to balance the competing

<sup>60</sup> Mujih Edwin, *Piercing the corporate veil as a remedy of last resort after Prest v Petrodel Resources Ltd: inching towards abolition?* (2016) 37(2) Comp Law 39.

<sup>61</sup> [2013] UKSC 34, 92.

<sup>62</sup> *Ibid*, 100.

<sup>63</sup> *Ibid*, 103.

interests of certainty and accountability. However, those interests and the extent of them are bound to change through time. The case of *Salomon* is testament to this thought; the attitudes that defined that case are not necessarily, or completely, the attitudes of company regulation and accountability in the legal and public sphere now.

Nevertheless, as true as this may be, this arguably does not justify the degree of uncertainty, and freedom to lower courts, leaving expansion open would create. In *Antonio Gramsci Shipping Corporation v Lembergs*<sup>64</sup>, Lord Justice Beatson ought to have gone further than declaring,

*“As to further development of the law, doing so by classical common law techniques may not be easy. [...] Absent a principle, further development of the law will be difficult for the courts because development of common law and equity is incremental and often by analogical reasoning.”*<sup>65</sup>

The law ought to go beyond this hesitant expression to foreclose and completely prevent the further expansion of the doctrine. Subject to the areas in which Lord Sumption's judgment has still left questions, the very fundamental aspects of what constitutes and does not constitute an evasion of a pre-existing legal obligation is clear. To prevent the law from swaying back into judgments of activism and confusion (as has already been seen), the courts should take the opportunity to close further development.

## Conclusion

Finding a balance within the doctrine of piercing the corporate veil has not been easy. This is clearly reflective of several interests and stakeholders that come with the regulation of companies. Nevertheless, something can be said for Lord Sumption's judgment for neatly establishing the distinction between evasion and concealment, whilst remaining consistent with the jurisprudence of law in this area. For the doctrine to develop further beyond the remits outlined by Lord Sumption may jeopardise its future integrity and so should be foreclosed to as it is. It still remains to be seen, however, what the future of the sham/façade principle within this doctrine will be, and how the overlap between evasion and concealment will continue to be defined.

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<sup>64</sup> [2013] EWCA Civ 730

<sup>65</sup> *Ibid.*, 66.

# Do events since 23 June 2016 strengthen or weaken the case for the United Kingdom adopting a written, codified Constitution?

Naseem Khan

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## Introduction

On the 23<sup>rd</sup> of June 2016, the United Kingdom (UK), voted in what was called by the then Prime Minister David Cameron, “a once in a lifetime opportunity” referendum, over the country’s continued membership of the European Union (EU).<sup>1</sup> The referendum ballot asked only whether the UK should “Remain a Member of the European Union” or “Leave the European Union” and by the early hours of the morning of the 24<sup>th</sup> June 2016, it was clear that leave had won by a narrow majority of 51.9% of the 33 million, who turned out to vote, in favour of leaving the EU against 48.1% who wished to remain.<sup>2</sup>

Upon learning the outcome of the referendum, Prime Minister Cameron resigned, and the ruling Conservative party elected Theresa May as successor, tasked with the role of withdrawing the UK from the EU. Immediately, the new Prime Minister and the Government ran into legal, political, and constitutional difficulties in seeking to utilise the Royal Prerogative (the residual powers of the Crown which now reside in Ministers of State) to “trigger” Article 50 of the Treaty on European Union (TEU). The subsequent legal challenge to this decision in the case of *R (Miller) v Secretary of State for Exiting the European Union*,<sup>3</sup> has arguably crystallised some of the long-standing questions that have raged over the extent and limits of the UK’s constitutional foundations. The commonly accepted view of the UK’s constitutional settlement is that whilst the country does in fact have a constitution, it is one which is unwritten, therefore fundamentally uncertain in many respects.<sup>4</sup>

This article will consider whether the events which the EU referendum have now strengthened, or even weakened, the case for the adoption of a written, codified, constitution in the UK.

## The UK’s unwritten constitution

The UK takes some degree of pride with the lack of a codified, written constitution.<sup>5</sup> The fact that the UK’s constitution is unwritten is testament to the ancient, and unbroken nature of, and legal continuity of the State, the Crown, and its subjects. Outside of this, however, the major advantage offered by an unwritten constitution is its flexibility and its pragmatism; an unwritten constitution can change and adapt along with society, and political change itself.<sup>6</sup>

The unwritten constitution which now presides over the UK has developed over centuries and has exhibited this flexibility throughout. Historically, the Crown operated with almost absolute power, subject to continuing support from the feudal barons who formed the military and financial backers. Over time, Parliament slowly accreted powers and privileges, and became responsible for ensuring taxation could

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1 Kylie MacLellan, Elizabeth Piper, ‘Cameron Says No Second EU Referendum if Result is Close’ Reuters May 17 2016, available online at: <<https://uk.reuters.com/article/uk-britain-eu-cameron/cameron-says-no-second-eu-referendum-if-result-is-close-idUKKCN0Y81VK>> accessed 5 August 2019

2 Electoral Commission, ‘Results and Turnout at the EU Referendum’ 29 July 2019, available online at: <<https://www.electoralcommission.org.uk/who-we-are-and-what-we-do/elections-and-referendums/past-elections-and-referendums/eu-referendum/results-and-turnout-eu-referendum>> accessed 6 August 2019

3 [2017] UKSC 5

4 John Baker, ‘Our Unwritten Constitution’ (2010) 167 Proceedings of the British Academy 91, 92

5 Anthony Brudage, Richard A Cosgrove, *The Great Tradition: Constitutional History and National Identity in Britain and the United States 1870-1960* (1st edn SUP 2007) 107

6 Ibid.

be gathered.<sup>7</sup> This operated as a basic check on the otherwise absolute power of the Crown, but it was not until the aftermath of the English civil war and the events of the Glorious Revolution of 1688, that the constitutional settlement in its present form was reached.<sup>8</sup> Following this, the current, accepted position of the constitution is one in which Parliament is regarded as the sovereign, and supreme law-making body in the land.<sup>9</sup>

The position reached by this settlement is known as the doctrine of Parliamentary sovereignty, and, as was noted by constitutional theorist and historian AV Dicey in the 19<sup>th</sup> century espoused that Parliament, as the sovereign body in the land, is free to make any law it sees fit.<sup>10</sup> Under this conceptualisation of the UK's constitution, any body or court can call into question, or review the legality of an Acts of Parliament that have passed both houses and received Royal Assent.<sup>11</sup> In other words, as argued by Bogdanor, the UK's constitution can be summed up as meaning, very simply; "Whatever the Crown in Parliament enacts is law".<sup>12</sup>

By contrast, in countries with a written constitution, such as the United States for example, a written constitution expressly sets out the separation of powers of the different branches of government, and allows the courts particular power to assess the legality, or "constitutionality" of the actions, and laws, made by the legislature and executive.<sup>13</sup>

In the light of the UK's unwritten constitutional settlement, it can therefore be said that there is no way in which certain statutes, or pieces of legislation which are somehow "constitutional" in nature, or in effect, can in fact ever be anything of that kind. If Parliament is truly sovereign, it can always repeal legislation which appears, at first glance, to bind it.

In more recent years, this accepted position has come under increasing threat, as the nature of some types of legislation (such as the Human Rights Act 1998)<sup>14</sup> and the UK's membership of the EU appeared to complicate this picture.<sup>15</sup> This has been furthered by the UK's changing internal relationship between its constituent states, with "Devolution",<sup>16</sup> from the 1990's onwards becoming an ever more important issue as more and more powers are devolved from Westminster to the constituent states of the UK.<sup>17</sup> There are now some who argue that the UK's unwritten constitution is outdated, obsolete, and unwieldy.<sup>18</sup> The extent to which these arguments are fair will now be considered.

## **The Miller Case: The relational architecture of the UKs unwritten constitution under strain?**

One of the main criticisms of the UK's unwritten constitution is that it results in inherent uncertainty as to what the outer-limits of the constituent branches of the UK state are. For example, questions arise to what kind of power the Crown actually retains; or in what areas the executive is entitled to exercise these residual and prerogative powers? Further questions arise as to how far the courts are entitled to review the legality of the executive in cases where legislation granting significant discretion to

7 Anthony Brudage, Richard A Cosgrove, *The Great Tradition: Constitutional History and National Identity in Britain and the United States 1870-1960* (1st edn SUP 2007) 108

8 RC Van Caenegem, 'Constitutional History: Chance or Grand Design?' (2009) 5 ECL Review 447, 447

9 AV Dicey, *An Introduction to the Study of the Law of the Constitution* (First Published 1885 10th edn MacMillan 1965) 44

10 *ibid*

11 *Edinburgh and Dalkieth Railway Co Ltd v Wauchope* (1842) 8 Cl & Fin 710

12 Vernon Bogdanor, *The New British Constitution* (1st edn Hart 2009) 12

13 Mark Garnett, Philip Lynch, *Exploring British Politics* (1st edn Pearson 2007) 84

14 Human Rights Act 1998

15 Taunabh Khaitan, "' Constitution" as a Statutory Term' (2013) 129 QJR 589, 590

16 Alan Page, Andrea Batey, 'Scotland's Other Parliament: Westminster Legislation About Devolved Matters in Scotland Since Devolution' (2002) PL (Aut) 501, 502

17 Jeffery Goldworthy, *Parliamentary Sovereignty: Contemporary Debates* (1st edn CUP 2010) 311

18 *Ibid*.

Government Ministers to adapt, or alter legislation through the use of statutory instruments, are lawful. Many of these issues were raised in the *Miller* case.

In *Miller*, the applicant contended that the Government's attempt to trigger Article 50 through the use of the prerogative was unlawful.<sup>19</sup> This claim was based on the suggestion that by using the prerogative in this manner, the executive would, effectively, be repealing and undermining the effect of an Act of Parliament in the form of the European Communities Act 1972.<sup>20</sup> The Supreme Court, ruling in favour of the applicant, agreed and held that by withdrawing, or beginning withdrawal proceedings from the European Union, the European Communities Act 1972 would in fact be impliedly repealed by the executive, rather than by Parliament itself in a manner which was not lawful as decided in the case of *Laker Airways v Department of Trade* as far back as 1977.<sup>21</sup>

As a case that highlights constitutional issues, *Miller* might have re-affirmed the orthodox Diceyan notion of Parliamentary sovereignty, which states that Parliament, and not the executive, is the sovereign law-making body in the land. The executive could not get around this by withdrawing from the EU without an Act of Parliament authorising this. Whilst this was subsequently achieved through the passing of the European Union (Withdrawal) Act 2018, the UK, some three years after the Brexit vote, remains within the EU, and Parliament has still failed to ratify the draft Withdrawal Agreement negotiated by Theresa May and the EU's negotiating representatives.<sup>22</sup>

More pertinently, even after the *Miller* case, significant issues remain as to how and where, the repatriated powers of sovereignty will reside once the UK do withdraw from the EU entirely. One of the more interesting elements of *Miller* is the intervention of the Scottish Government and the Welsh National Assembly, who asserted that the withdrawal of the UK from the EU in this manner was a breach of the so-called Sewel Convention. That the UK was altering the legislative competence of these bodies without their consent.<sup>23</sup> The potential breach of the Sewel Convention, and the relationship between the devolved Governments and Westminster, is certainly one area in the lack of a written constitutional settlement does lead to some difficulty.

The Sewel Convention, also called "legislative consent motion" is a "constitutional convention" which provides that the devolved Governments of Scotland, Wales, or Northern Ireland must grant their consent to the UK's Parliament before the UK Parliament legislates on matters which have been devolved to them.<sup>24</sup> In *Miller*, the Scottish and Welsh governments argued that no such consent had been given, and that in fact voters in Scotland and Northern Ireland had overwhelmingly voted to remain in the EU.<sup>25</sup>

The Supreme Court, however, confirmed that constitutional conventions are not legally binding on the Government, and are merely political in nature. As such, the Court could not rule on the legality of the alleged breach of the Sewel Convention. The fact that constitutional conventions are not binding is now a well-acknowledged fact of law. Ultimately, this is because the UK's unwritten constitution is built largely (if not exclusively) on the notion of Parliamentary sovereignty, and if a constitutional convention could prohibit Parliament from acting in a certain manner, then Parliamentary sovereignty itself would be undermined. In other words; in a battle between "constitutional" conventions and Parliamentary sovereignty, Parliamentary sovereignty always wins.

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19 R(Miller) v Secretary of State for Exiting the European Union [2017] UKSC 5

20 European Communities Act 1972

21 [1977] 1 QB 643

22 European Commission, 'Draft Agreement on the Withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community, as Agreed at Negotiators' Level on 14 November 2018' available online at: < [https://ec.europa.eu/commission/publications/draft-agreement-withdrawal-united-kingdom-great-britain-and-northern-ireland-european-union-and-european-atomic-energy-community-agreed-negotiators-level-14-november-2018\\_en](https://ec.europa.eu/commission/publications/draft-agreement-withdrawal-united-kingdom-great-britain-and-northern-ireland-european-union-and-european-atomic-energy-community-agreed-negotiators-level-14-november-2018_en) > accessed 6 August 2019

23 R (Miller) v Secretary of State for Exiting the European Union [2017] UKSC 5

24 Jane Munro, 'Thoughts on the 'Sewel' Convention' (2003) 23 SLT 194, 194

25 R (Miller) v Secretary of State for Exiting the European Union [2017] UKSC 5

Therefore, there is no such thing as a “constitutional” restraint to the convention that prevents it from being breached by the Government. Any harm that might be done to the Government or indeed to Parliament if such a convention is breached is merely political, and not legal in nature.

## Could a codified constitution help?

If a written constitution were to be drafted in such a way to ensure that the devolved Governments were legally required to give legislative consent, the new UK constitution would, by its very nature, undermine the traditional notion of Parliamentary sovereignty. Given the arguments put forwards by the “leave” side during the EU referendum campaign, many of which were based on returning sovereignty to the UK’s Parliament from Europe, this would be politically difficult to say the least. This is a point made by Craig, who argues that it is difficult to see how a written constitution could help resolve the difficulties that have arisen within the UK’s internal constitutional settlement since the Brexit vote.<sup>26</sup>

On the other hand, it might be suggested that a constitution which set out the specific rights of each of the constituent parts of the United Kingdom would lend greater certainty to the position of each of these states. There has, in recent years, been a significant upswing in nationalist support and sentiment in Scotland. Part of the rationale behind this movement appears to be the disproportionate weight which England carries as part of the Union, by virtue of its greater population making the UK have higher representation in Parliament. This leads to the concern amongst some Scottish nationalists that “what England wants, England gets”, even when the other parts of the UK have seemingly different priorities.<sup>27</sup>

If this was indeed the purpose of devolution, it failed almost completely. The legislation that created the devolved governments is legislation made by Parliament, Diceyan constitutional theory dictates that Parliament will ultimately retain its absolute sovereignty over even a devolved system.<sup>28</sup> Whilst there were, in more recent years, many theorists who suggested that this notion of Parliamentary sovereignty was becoming outdated, or that Parliament now shared sovereignty with the courts who operated in a sort of review role akin to the constitutional courts of the USA, this now appears to have been rejected by the Supreme Court in *Miller*. Historically, the argument that Parliamentary sovereignty was somehow reduced has been made on the back of the growing assertiveness of the courts following the introduction of the Human Rights Act 1998, and the famous decision of the European Court of Justice (ECJ) in *R (Factortame) v Secretary of State for Transport*. In this case the ECJ held that the English courts must disapply Acts of Parliament which contradicted EU law, and apply conforming EU law in their place. This led in turn to some arguing that the courts now “shared” sovereignty with Parliament,<sup>29</sup> and that some statutes were “constitutional” in nature and so could not be so simply overridden (at least impliedly).<sup>30</sup> This approach now appears to have reached its high-water mark in the case of *R (Jackson) v Attorney-General*, and following *Miller* it might be suggested that this approach is no longer one that is based on any real understanding of the UK’s constitutional settlement, which has been re-affirmed by the Supreme Court itself.<sup>31</sup>

On the other hand, it is suggested that even if the doctrine of Parliamentary sovereignty is applied, there are still constitutional issues that remain unsolved due to the lack of a written and codified constitutional settlement. This is something that came up in the statements made by the new Prime Minister, Boris Johnson. The Prime Minister has stated that if changes are not made to the draft withdrawal agreement so far negotiated, the UK would leave the EU without an agreement. In response to this, Members of Parliament have indicated that they would pass a motion of no-confidence in the Government and in

26 Robert Craig, ‘Miller Supreme Court Case Summary’ (2016) available online at: <

<https://ukconstitutionallaw.org/2017/01/26/robert-craig-miller-supreme-court-case-summary/>> accessed 6 August 2019

27 Mark Elliott, ‘The Supreme Court’s Judgment in Miller: In Search of Constitutional Principle’ (2017) 76 CLJ 257, 258

28 Charlie Jefferey, Daniel Wincott, ‘Devolution in the United Kingdom: Statehood and Citizenship in Transition’ (2006) 36 *Publius* 3, 4

29 Jeffery Goldsworthy, *Parliamentary Sovereignty: Contemporary Debates* (1st edn CUP 2010) 311

30 *Thoburn v Sunderland City Council* [2001] EWHC Admin 195 (Laws LJ) [53]

31 Mark Elliott, ‘The Supreme Court’s Judgment in Miller: In Search of Constitutional Principle’ (2017) 76 CLJ 257, 258

the Prime Minister. The Prime Minister has indicated that he would not necessarily resign in such a situation, calling into question what the legal effect of such a position would be. Some have suggested that if the Prime Minister did refuse to “resign” after a vote of no-confidence the Queen could intervene using her reserve prerogative powers to force the Prime Minister to resign.<sup>32</sup>

Whilst this might appear to be a power which the Crown retains, even the exercise of this power would be dependent on Parliament being able to put forwards another potential Prime-Minister who could then form a government within 14 days provided that a motion of confidence can be made under s3(5) of the Fixed-Term Parliament Act 2011.<sup>33</sup>

Ultimately, the UK Parliament retains control over the UK’s withdrawal from the EU, and could simply repeal the Act, and pass a vote of no-confidence to allow a general election to be called. The lack of a codified, written constitution does not appear to impact on this, as the law in this area is relatively clear.

## **The future for the union: A federal UK with a codified constitution?**

Whilst the Brexit saga has reignited concerns about the UK’s unwritten constitutional settlement amongst those in Scotland, Northern Ireland and Wales, there are also many who argue that devolution itself has left England in an asymmetrical position in comparison to these other states of the UK.<sup>34</sup> England is now the only country within the UK that lacks its own national assembly, able to make law affecting only England without the input of Members of Parliament from the other parts of the UK. One-way of correcting this, which preserves the Sovereignty of Parliament, would be to make a unified all-UK Parliament “sovereign”. Exacting law-making powers only over matters affecting the UK as a whole, and for a legislative consent motion to be required legally, instead of merely politically, before the all UK Parliament did make “national” legislation impacting on matters otherwise devolved. A written constitution, at the heart of a new constitutional settlement, perhaps built around a federal-UK system might be better placed to resolve some of these sentiments by creating a more ‘just’ basis of political governance, whereby the largest region (England) in terms of population, is not capable of exerting its will over the rest of the UK combined.<sup>35</sup>

The most obvious difficulty is that the UK would risk diverging in terms of legislative and regulatory standards in a manner which might impact negatively on the UK’s own internal market, or on the UK’s external trade relations. Furthermore, this approach, under which both Federal and State law were found to exist side-by-side would naturally increase the complexity of the law, and its divergence from region to region, potentially further undermining the cultural hegemony of the UK as a whole, and risking increasing support for separatist, nationalist movements which might seek to undermine the Union. Finally, the greatest difficulty faced by such an approach is that the traditional, Diceyan notion of Parliamentary sovereignty itself, would be required to be jettisoned under a Federal system. Whilst Parliament might retain sovereignty over England, under a truly Federal system, it could not retain this authority over the entirety of the UK. In any event, by its very nature, a written, codified constitution would constrain Parliament by setting out the limits of its power.<sup>36</sup> This is entirely inconsistent with the current understanding of the UK and its constitution.

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32 Caroline Davies, ‘Could the Queen Sack Boris Johnson? The Experts are Divided’ *The Guardian* 7 August 2019

33 s3(5) Fixed-Term Parliament Act 2011

34 Pavlos Eleftheriades, ‘The Coming Constitutional Instability’ (2017) *PL* (Jul) 347, 348

35 *ibid*

36 Jeff King, ‘The Democratic Case for a Written Constitution’ (2019) *Current Legal Problems*, available online at <<https://academic.oup.com/clp/advance-article-abstract/doi/10.1093/clp/cuz001/5494555?redirectedFrom=fulltext>> accessed 6 August 2019



## Conclusion

Whilst it is clear that the events following the UK's vote to withdraw from the EU have brought to light some of the most difficult paradoxes and anomalies of the UK's constitutional settlement, it remains difficult to suggest that an alternative, codified, system would resolve any of the problems satisfactorily. This is because, the UK's current system is based fundamentally on the acknowledgement of Parliament as being the sovereign law-making body in the land. Parliamentary sovereignty is defended primarily because it places power in the hands of those who are directly elected by the governed populace. Meaning that democratic consent and legitimacy are placed at the heart of the settlement. This does however stand in the way of a written constitution, which essentially "freezes" the rights of Parliament and the other branches of state at a particular point in time and so a written constitution is incompatible with this approach to sovereignty. Ultimately, if the UK wishes to adopt a written, codified constitution, it must first decide whether or not it wishes to retain the principle of Parliamentary sovereignty itself.

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# The EU response to the 2015 refugee flows: A missed opportunity to use the Temporary Protection Directive?

Lara Krayem

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## Introduction

Since 2011, Europe has had to respond to its largest and most severe asylum seeker challenge since the Second World War.<sup>1</sup> Over one million asylum seekers applied for asylum in the European Union in 2016, but many more asylum seekers lost their lives trying to reach safety by using irregular and dangerous routes to cross the Mediterranean Sea.<sup>2</sup> In 2016, over five thousand migrants lost their lives at sea and the number of missing or dead people reached five thousand as well.<sup>3</sup>

Evidently, there is a significant amount of asylum seekers trying to find refuge in Europe. As a result, some Member States, in particular those at the border of the EU found themselves unable to cope with the vast numbers of asylum seekers.<sup>4</sup> However, it seems that the Union has not done enough to assist these Member States despite having an emergency regulatory tool that deal with exactly this type of situation. The Temporary Protection Directive is the tool that could have been used to assist with the situation however, it has never been implemented.

This article aims to establish that the Temporary Protection Directive was capable of assisting with the situation in Europe but was not activated due to externalisation policies. However, its lack of activation in such severe times renders it obsolete as it is now highly unlikely that it will ever be used. This article consists of three chapters.

Chapter One, provides historical context in regard to how the Temporary Protection Directive was born by explaining the situation during the Balkan War. Chapter One also lays down the aims and objectives of the Directive and explains the procedural steps that ought to be taken if a Member States wishes to activate the Directive. Lastly this Chapter provides a small overview of the Common European Asylum System in order to demonstrate that since the Directive is part of it then all Member States are bound by the same obligation under this framework.

Chapter Two of this article examines the challenges the Temporary Protection Directive faces which prove to be obstacles in its implementation. It is argued that the lack of definition as to what constitutes mass influx is a very significant challenge for the Directive as it makes it ambiguous but supports that the current situation in Europe amounts to mass influx. Furthermore, this Chapter argues that the activation process of the Directive is so complex and lengthy which defeats its primary purpose; to respond to emergency situations. Burden sharing is also a prominent problem the Directive faces as national interests and externalisation policies are more attractive to Member States than showing solidarity and sharing responsibility. Lastly, it is argued that the Directive has not yet been implemented due to the fear of it becoming a pull factor and attracting more asylum seekers on European territory.

Chapter Three examines whether the situation that Europe has faced since 2011 proved to be a good opportunity for the Directive to finally be activated. Chapter Three demonstrates that the events that unfolded could have resulted to the activation of the Directive but the Union's stance to resist activation means that it will be very unlikely that this mechanism will ever be used thus, it is now obsolete.

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1 European Parliament, 'Briefing – EU Legislation in Progress: Reform of the Dublin System', (1 March 2019), 2.

2 Ibid.

3 Ibid.

4 UNHCR, 'Europe Situation', <<https://www.unhcr.org/europe-emergency.html>> accessed 18 February 2020.

## Methodology

Primary materials such as legislation and case law were used to analyse the current situation in the European Union. Secondary materials were also used in the analysis of this article in order to draw spherical conclusions. These secondary materials included journal articles, books, online sources such as newspapers and blogs and a podcast. These materials were used to support and enhance the view and arguments presented throughout this article.

## Chapter 1: How was the Temporary Protection Directive born?

Chapter One of this article will establish the historical background behind the creation of the Temporary Protection Directive<sup>5</sup> by providing, in Section One, an analysis of the events that occurred during the Balkan Wars which ultimately lead to the creation of the Directive. Furthermore, Section Two of this Chapter will engage with the Directive in greater detail and examine its main provisions and aims. Lastly, Section Three will provide a brief analysis of what the Common European Asylum System (CEAS) is, as the Directive forms part of this legislative framework.

### Section One: The events leading to the birth of the Temporary Protection Directive

This section will examine the events that lead to the Balkan War which was the main reason why the European Union introduced the Temporary Protection Directive, as it began receiving significant numbers of asylum seekers due to the violence and conflict in that area. As a result, the EU wanted to create a legal instrument that would allow it to respond to these flows quickly without overburdening the national asylum systems of its Member States.<sup>6</sup>

In the early 1990s, the former Socialist Republic of Yugoslavia was one of the major, developed and diverse countries in the Balkan area, consisting of six separate republics, those of Bosnia and Herzegovina, Croatia, Macedonia, Serbia, Slovenia and Montenegro.<sup>7</sup> There were also two autonomous provinces within the Republic of Serbia, other than the six republics mentions, these being Kosovo and Vojvodina.<sup>8</sup> Therefore, the former Republic of Yugoslavia consisted of numerous ethnic groups as well as religious backgrounds.

With the collapse of the former Soviet Union as well as the rise of nationalism in the Eastern European region during the early 1990s, Yugoslavia found itself in severe political and economic turmoil as its central government became very weak whilst militant nationalism was on the rise.<sup>9</sup> Political groups in the country were strongly advocating for the independence of these republics or the ability for some of the republics within the Yugoslavic federation to receive more powers.<sup>10</sup> A strong nationalist rhetoric was followed to jeopardise the common Yugoslav identity and create suspicion between the different ethnic groups that existed.<sup>11</sup>

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5 Council Directive 2001/55/EC of 20 July 2001 on minimum standards for giving temporary protection in the event of a mass influx of displaced persons and on measures promoting a balance of efforts between Member States in receiving such persons and bearing the consequences thereof, OJ L.212/12, 7 August 2001, thereafter Temporary Protection Directive or Directive.

6 D. Gulns & J. Wessels, 'Waste of Paper or Useful Tool? The Potential of the Temporary Protection Directive in the Current "Refugee Crisis"', 36 Refugee Survey Quarterly (2017), 57-83, 61.

7 United Nations International Criminal Tribunal for the Former Yugoslavia, <<http://www.icty.org/en/about/what-former-yugoslavia/conflicts>> accessed 1 August 2019.

8 Ibid.

9 Ibid.

10 Ibid.

11 Ibid.

Slovenia was the first of the other six republics to leave the former Yugoslav Republic and declaring its independence in June of 1991.<sup>12</sup> This resulted to an armed conflict between Slovenian forces and the Yugoslav People's Army with Slovenia being victorious.<sup>13</sup> Croatia followed Slovenia in declaring independence, however, there was significant conflict in Croatia due to the Serb minority wanting to create a new state which would be another independent Serb state.<sup>14</sup> Croats were violently expelled from that particular territory during an attempt to commit ethnic cleansing.<sup>15</sup>

The deadliest conflict during this war was the one in Bosnia and Herzegovina with an estimation of more than one hundred thousand people being killed and another two million were forced to flee their homes in order to escape persecution.<sup>16</sup> This happened because the population consisted of different ethnic backgrounds (43% Bosnian Muslims, 33% Bosnian Serbs, 17% Bosnian Croats) which resulted in increased tensions between the groups as both Serbia and Croatia wanted to assert power over large parts of this territory.<sup>17</sup>

Kosovo was also an area of conflict during the Balkan War as the Albanian community of Serbia wished for its independence.<sup>18</sup> As a result, the Serb forces attacked civilians and lead Kosovo Albanians to flee their homes to avoid persecution.<sup>19</sup> Moreover, the North Atlantic Treaty Organisation (NATO) got involved in the conflict and carried out air strikes which targeted both Kosovo and Serbia lasting seventy-eight days.<sup>20</sup>

The last conflict that occurred during the Balkan War was that of Macedonia<sup>21</sup> despite living in peace for a decade. In the early months of 2001 the Albanian National Liberation Army, a militant group, found itself in conflict with the Macedonian security forces as it aimed at gaining its independence for the Albanian dominated areas in the territory.<sup>22</sup>

Evidently, these conflicts and the Balkan War altogether was quite a severe event in the Eastern European area. This explains why many asylum seekers fleeing these areas entered the European Union seeking refuge, which subsequently leads to the Union's creation of the Temporary Protection Directive, as a means to accommodate these asylum seekers in cases of such emergency.

## **Section Two: What does the Temporary Protection Directive consist of?**

This section will engage with the Temporary Protection Directive's provisions in greater detail. It will establish its aims and objectives and explain how this mechanism would work should it be activated through its activation mechanism.

As explained in Section Two, the birth of the Directive originates from the 1990s and the Balkan War, as an emergency tool to deal with mass influx of people arriving to the European Union. It is crucial to establish that temporary protection is different to the protection provided in the 1951 Refugee Convention<sup>23</sup>. The Convention is implemented based on the determination of individual status, contrary to temporary protection which is group-based and is used as a tool to avoid overburdening national asylum systems but at the same time providing adequate protection to asylum seekers.<sup>24</sup>

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12 Ibid.

13 Ibid.

14 Ibid.

15 Ibid.

16 Ibid.

17 Ibid.

18 Ibid.

19 Ibid.

20 Ibid.

21 Previously known as Former Yugoslav Republic of Macedonia (FYROM).

22 United Nations International Criminal Tribunal for the Former Yugoslavia (n 7).

23 Convention and Protocol Relating to the Status of Refugees 1951.

24 H. Beirens, S. Maas, S. Petronella. M. Velden (European Commission), 'Study on the Temporary Protection Directive' ICF January 2016, 1-13, 6.

The European Union decided to create the Temporary Protection Directive because prior to the Balkan War there was a lack of a uniform framework for all Member States. Rather instead, Member States used their own temporary protection mechanisms which were different from one another and proved unable to respond to situations of mass influx as they did not seem to distribute the burden of asylum seekers in a fair and even manner between Member States.<sup>25</sup> The aim of the Directive is two-fold, firstly, it aims to establish minimum standards of temporary protection to asylum seekers in mass influx situations and secondly it aims to promote fair sharing of responsibility between Member States when it comes to receiving and asylum seekers in mass influx situations.<sup>26</sup> It is important to note that the Directive is part of the Common European Asylum System which means that it is part of a legal framework which sets common standards in asylum law within the Union and harmonises the interpretation and application of this area among Member States to achieve a uniform system.<sup>27</sup>

The Temporary Protection Directive can only be activated in mass influx situations that need to be established by the EU Council following a proposal from the Commission which is alerted of these situations by the affected Member State.<sup>28</sup> As soon as the Directive is activated, it aims to provide consistent rights to individuals who are in need of temporary protection, as well as assist fellow Member States whose asylum systems may be suffering from the large inflows of asylum seekers.<sup>29</sup> The Directive foresees for the beneficiaries of temporary protection to receive a residence permit, the ability to obtain employment, access to housing and social welfare, access to medical treatment, access to education for minors, family reunification opportunities and guarantees for access to the national asylum procedure.<sup>30</sup> The Temporary Protection Directive also contains provisions which deal with the return of asylum seekers to their countries of origin when protection comes to an end as well as exclusion clauses for people who have committed serious crime or may be a threat to public security.<sup>31</sup> There are also specific provisions for minors who are unaccompanied and for individuals who have suffered traumatic experiences including rape, violence be it physical or psychological.<sup>32</sup>

### **Section Three: A brief background of the Common European Asylum System (CEAS)**

This section will provide a brief analysis in regard to the creation of the CEAS and explain what its role within the European Asylum Law procedures and regulations is. This analysis is important because the Temporary Protection Directive is part of this legislative framework so its implementation will occur under the CEAS rules.

The CEAS was created due to the removal of internal frontiers within the European Union, as a result, the asylum system of the Union as a whole needed to follow a uniform set of rules.<sup>33</sup> The need to develop a common asylum system was born in order to prevent secondary movement of asylum seekers, which suggests that the European Union wanted to regulate asylum seeker movement within the EU and eliminate the possibility of them moving to different Member States due to conditions being better in some States than others.<sup>34</sup>

The CEAS creates mutual obligations for all Member States to provide the same protection to asylum seekers. It ensures that all procedures regarding asylum seekers that are carried within the Union are

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25 Ibid.

26 Ibid.

27 European Asylum Support Office (EASO), 'An Introduction to the Common European Asylum System for Courts and Tribunals – A Judicial Analysis', August 2016, 3-113, 13.

28 H. Beirens, S. Maas, S. Petronella. M. Velden (n 24), 7.

29 Ibid.

30 European Commission, 'Temporary Protection', <[https://ec.europa.eu/home-affairs/what-we-do/policies/asylum/temporary-protection\\_en](https://ec.europa.eu/home-affairs/what-we-do/policies/asylum/temporary-protection_en)> accessed 6 August 2019.

31 Temporary Protection Directive, Articles 21, 22, 23 and 28.

32 Ibid, Articles 13 and 16.

33 European Asylum Support Office (EASO) (n 27), 14.

34 Ibid.

the same in every Member State and are effective.<sup>35</sup> Following the implementation of this legislative framework, a series of secondary legislation followed in order to establish minimum standards of protection to which Member States ought to follow when dealing with asylum seekers.<sup>36</sup> The CEAS established the Eurodac Regulation<sup>37</sup>, the Temporary Protection Directive, the Dublin Regulation<sup>38</sup>, the Qualification Directive<sup>39</sup> and all the key legislation that deals with the arrival of asylum seekers in Europe.

The Temporary Protection Directive is an EU-wide mechanism and falls within the scope of CEAS, this means that it aims to reduce the differences between Member States' own temporary protection policies.<sup>40</sup> However, the Directive has never been activated so far despite being introduced to assist with cases of mass influx that are considered emergency.

## Concluding remarks

Chapter One of this article aims to provide an overview to the reader in regard to the main instruments analysed in this piece. Section One analysed the events that took place prior to the birth of the Temporary Protection Directive. This was done in order to provide the reader with the necessary background information about the situation at the time of the birth of the Directive and to allow for a comparison with the current situation.

Section Two explained the Temporary Protection Directive in greater detail. It established its aims and objectives and it differentiated it from the protection that is offered under the 1951 Convention. Section Two also analysed the steps that need to be taken in order for the Directive to be activated.

Section Three of this thesis briefly explained what the CEAS is as the Directive is part of this framework. Section Three aims to demonstrate that since the Temporary Protection Directive is Part of the CEAS then all Member States are under the same obligations as it forms a uniform legislative framework.

## Chapter Two: The challenges the Temporary Protection Directive faces

This Chapter of the article will analyse the main challenges the Temporary Protection Directive faces. This article will examine whether these challenges could justify not activating the Directive when there were large flows of asylum seekers which overwhelmed numerous Member States. This chapter will be divided in three sectors in order to examine the key issues of the directive. Section One will analyse the mass influx clause<sup>41</sup> used in the mechanism to demonstrate not only the ambiguity in the legislation but also the unwillingness of the EU to activate it. Section Two will examine the activation procedure of the mechanism and argue that its complexity and lengthy requirements undermine the purpose of the

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35 European Commission, 'Common European Asylum System', < [https://ec.europa.eu/home-affairs/what-we-do/policies/asylum\\_en](https://ec.europa.eu/home-affairs/what-we-do/policies/asylum_en)> Accessed 6 August 2019.

36 European Asylum Support Office (EASO) (n 27), 15.

37 Council Regulation (EC) No 2725/2000 of 11 December 2000 concerning the establishment of 'Eurodac' for the comparison of fingerprints for the effective application of the Dublin Convention [2000] OJ L 316/1.

38 Council Regulation (EC) No 343/2003 of 18 February 2003 establishing the criteria and mechanisms for determining the Member State responsible for examining an asylum application lodged in one of the Member States by a third-country national, [2003] OJ L50/1.

39 Council Directive 2004/83/EC of 29 April 2004 on minimum standards for the qualification and status of third country nationals or stateless persons as refugees or as persons who otherwise need international protection and the content of the protection granted [2004] OJ L 304/12.

40 European Asylum Support Office (EASO) (n 27), 54.

41 Temporary Protection Directive, Article 2 (A): "temporary protection' means a procedure of exceptional character to provide, in the event of a mass influx or imminent mass influx of displaced persons from third countries who are unable to return to their country of origin, immediate and temporary protection to such persons, in particular if there is also a risk that the asylum system will be unable to process this influx without adverse effects for its efficient operation, in the interests of the persons concerned and other persons requesting protection".

Directive itself, as an *emergency* mechanism. Section Three will look into the solidarity clause found in the Directive and establish whether it is a good tool or simply a mere clause that is not used by the Member States. Lastly, Section Four will analyse the possibility of the Directive becoming a pull factor which causes Member States to resist its activation in fear of being overburdened with asylum seekers.

## **Section One: Mass influx under the Temporary Protection Directive**

This section will examine the mass influx clause the Directive uses as a key element for its activation. It will be argued that the ambiguity of the mass influx clause leads to the inactivation of the Directive as the definition of a mass influx situation proves to be particularly broad. In addition, this section will demonstrate that the large flows of asylum seekers arriving to the EU post-Arab Spring amounts to mass influx. In order to prove this claim, statistics of the period when the Directive was passed and other mechanisms the EU used to respond to these numbers will be examined.

There are various definitions of mass influx and since the Directive does not give a clear definition it proves to be challenging to assess whether a situation amounts to mass influx. The United Nations High Commissioner for Refugees (UNHCR) defines mass influx as the large-scale arrival of people who are seeking asylum or refuge.<sup>42</sup> UNHCR also states that a mass influx situation includes an increasing rate of arrival which can result to overwhelming the host state's reception condition and impair the ability of the national asylum system to absorb those seeking asylum.<sup>43</sup> A definition for mass influx is not available in the Directive itself however, it can be found in the proposal of the Commission for the Directive in the explanatory text.<sup>44</sup> In the proposal the Commission states that the influx of asylum seekers must come from the same country or geographical area and the gradual arrival of these people must disturb the functioning of Member States' national asylum system making it impossible for the host to absorb the numbers of people seeking refuge.<sup>45</sup> Furthermore the proposal mentions that it is impossible to quantify exactly what numbers amount to mass influx.<sup>46</sup>

The lack of clear definition in the text of the Directive itself could demonstrate motive of intentional creation of ambiguity exactly because the drafters at the time may have wanted to create this mechanism symbolically but not actually implement it in the future. This conclusion can be drawn because, it would be reasonable to assume that a definition would exist in the main text of the Directive especially when it concerns the central criterion for activation. Therefore, it is evident that these definitions are not substantial as to what amounts to mass influx. Both definitions provide some guidance as to how a host state may realise that it is experiencing a mass influx situation by being unable to absorb the asylum seekers but still, there are no numbers to serve as guidance for such situations. As a result, whether a situation amounts to mass influx is up to the Commission to ultimately decide as it plays a central role in the activation process of the Directive.<sup>47</sup>

The European Commission has argued that the broad nature of the mass influx clause in the Directive is a positive aspect of the mechanism as the authors believe that the legislature purposely chose to include such broad definition to ensure flexibility in different types of pressure without being bound by numerical limits.<sup>48</sup> It is further argued that by having this broad definition in the Directive allows for

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42 UNHCR, 'Ensuring International Protection and Enhancing International Cooperation in Mass Influx Situations: Advance Summary Findings of the Study Commissioned by UNHCR', 24 Refugee Survey Quarterly (2005), 118–123.

43 Ibid, 118.

44 Commission of the European Communities (2000), Proposal for a Council Directive on minimum standards for giving temporary protection in the event of a mass influx of displaced persons and on measures promoting a balance of efforts between Member States in receiving such persons and bearing the consequences thereof, Brussels: CEC, 24 May 2000, COM(2000) 303 final 2000/0127 (CNS).

45 Ibid, 14.

46 Ibid.

47 See Chapter 1.

48 H. Beirens, S. Maas, S. Petronella. M. Velden (n 24), 7.

flexibility of the mechanism to respond to various situations of mass influx for example, gradual or sudden arrivals which according to the Commission gives the legislator as large '*action radius*'.<sup>49</sup>

The argument made by the Commission is not supported. Contrarily, this piece supports that the vagueness of the Directive does not result to flexibility rather it results to extreme ambiguity and inability of activation. Instead of achieving a large '*action radius*' the legislature managed to limit the Directive incredibly as such broad definition means that nothing falls within the scope of mass influx. This is further supported by numbers, in 2015 and 2016 alone, more than one million asylum seekers reached European soil,<sup>50</sup> yet the Directive was not activated nor was there any discussion of the situation as mass influx. In fact, in 2011 Italy requested for the activation of the Directive because it was experiencing large flows of asylum seekers arriving at its shores due to the Arab spring conflict where the national asylum system could no longer absorb the arriving people.<sup>51</sup>

Italy's national asylum system was suffering and the country issued a warning stating that it anticipated more people to arrive demonstrating increasing influx.<sup>52</sup> This falls within the scope of Article 2(A) of the Directive however, the request could not be materialised as there was no consensus in the Council in order to activate the mechanism.<sup>53</sup>

No explanations were given by the Commission or the Council as to why the request was rejected, the only available information on the rejection is a statement made by the former EU Commissioner, Cecilia Malmstrom stating that '*at this point we cannot see a mass influx of migrants to Europe even though some of our Member States are under severe pressure*'.<sup>54</sup> Similarly when the author of this article asked the current EU Commissioner, Dimitris Avraamopoulos, why the EU did not activate the Temporary Protection Directive at any point during the large inflows of asylum seekers post-Arab spring, he stated that the Directive was not in a position to respond to the new needs of the situation from 2015.<sup>55</sup> The response received was unsatisfactory as it once again did not provide any reasoning behind the resistance in activating the Directive.

It is argued that the response of both EU Commissioners as well as the EU in general in not defining the situation especially post-Arab spring uprisings, as mass influx is erroneous. As mentioned in Chapter 1 the Directive was born in order to respond to the flows of asylum seekers from the Balkan states after the Balkan war. At that time Europe considered that the inflows constituted mass influx however, it is important to note that by 1992 the number of asylum seekers from the Balkan war reached 604,812.<sup>56</sup> In 2015, the asylum seekers that managed to reach EU territory exceeded one million<sup>57</sup> and in 2011 when Italy made a request for activation, the asylum seekers in Italy alone reached 500,000.<sup>58</sup> The numbers of asylum seekers attempting to enter the EU since the Arab spring uprisings are comparable, if not exceeding, those of the Balkan War.

Therefore, if the Directive was born to serve as an emergency tool to relieve national asylum systems at a time where asylum seekers reached around 600,000; it is only reasonable to assume that with more than one million asylum seekers in the last five years the situation falls well within the scope of the Directive and can be ultimately defined as mass influx.

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49 Ibid.

50 UNHCR, 'Europe Situation', 6 October 2017 < <https://www.unhcr.org/europe-emergency.html>>, accessed 10 July 2019.

51 M. Ineli-Ciger, 'Has the Temporary Protection Directive Become Obsolete? An Examination of the Directive and its Lack of Implementation in View of the Recent Asylum Crisis in the Mediterranean' found in 'Seeking Asylum in the European Union: Selected Protection Issues Raised by the Second Phase of the Common European Asylum System' (BRILL 2015), 237.

52 B. Nascimbene & A. Di Pascale, 'The 'Arab Spring' and the Extraordinary Influx of People who Arrived in North Italy from North America', 13 EJML 2011, 341-360, 342.

53 Ibid, 347.

54 C. Malmstrom, 'Debate on Migration Flows', C. Malmstrom – My Blog, 6 Apr. 2011, <[http://ec.europa.eu/archives/commission\\_2010-2014/blogs/malmstrom/debate-on-migration-flows.html](http://ec.europa.eu/archives/commission_2010-2014/blogs/malmstrom/debate-on-migration-flows.html)> accessed 7 July 2019.

55 LSE Podcast, 'Europe's Response to the Challenge of Migration and Security', 23 January 2019, minute 56:43, <<http://www.lse.ac.uk/lse-player?id=4593>> accessed 15 July 2019.

56 M. Morokvasic, 'Yugoslav Refugees, Displaced Persons and the Civil War' 11(4) Refuge (1992), 3-8, 3.

57 UNHCR (n 50).

58 D. Gulns & J. Wessels (n 6), 63.



Technically, and according to the Proposal, gradual arrivals of asylum seekers could amount to a situation of mass influx so long as these arrivals disturb the smooth running of national asylum systems. However, there is another hurdle in the definition of the Directive. It does not mention how many national asylum systems must be disturbed and incapable of functioning to their maximum capacity in order for a situation to amount to mass influx.<sup>59</sup> Therefore, it could be argued that even if one national asylum system is overburdened due to large inflows of asylum seekers, then the Directive can be activated especially considering that the mechanism itself imposes a solidarity mechanism. Arguably, the solidarity clause exists to assist Member States that may be suffering even if there is only one Member State that is overburdened. It would not be reasonable to expect that the requirements for activation of the Directive require all national asylum systems to be overburdened, this would make the solidarity mechanism redundant as no Member State would be able to assist another.

In theory, and in accordance to the argument made above, the Directive should have already been activated as there were numerous occasions where national asylum systems have been overburdened. This became very evident when the Dublin III Regulation<sup>60</sup> became the main regulatory instrument for asylum seekers. Dublin III and its predecessors operate on a hierarchy criteria basis in order to allow for an easier process of determination and allocation of responsibility between Member States regarding asylum seekers.<sup>61</sup> During these Dublin transfers there were numerous cases against bordering Member States such as Italy and Greece for Article 3 of the ECHR violations.<sup>62</sup>

As a result, Article 3(2) of Dublin explicitly mentions the wording '*systemic flaws*' as a key element in prohibiting transfers to Member States whose asylum systems are known to be systemically flawed. However, if all Member States are fulfilling their obligations under EU Treaties regarding the protection of asylum seekers then the express use of the words '*systemic flaws*' to describe Member States asylum procedures should have never been used. However, the explicit use of these words in the Regulation itself demonstrate that the EU recognises that some of its Members are not safe hosts for asylum seekers exactly because their national asylum systems have been overburdened. Evidently, if the EU is admitting through its regulations that there is a possibility of Member States' asylum systems to be systemically flawed due to large inflows of asylum seekers, it is reasonable to claim that such situations amount to mass influx where the Directive should have been activated.

The EU has been acting on the current situation in ways that indicate mass influx despite not activating the Directive using its broad wording to avoid describing the inflows as mass. An example is the Relocation Scheme 2015<sup>63</sup>. Article 4 of the Relocation Scheme involved the relocation of 120,000 asylum seekers from Greece to other EU Member States while Article 10 establishes financial aid for Italy and Greece. Various Member States resisted this decision, in particular Hungary, Poland, Slovakia and the Czech Republic rejected the plan and amongst other things called for stricter border controls to reduce asylum seekers inflow.<sup>64</sup> Nonetheless, with the adoption of this proposal the EU has technically acknowledged and accepted that some of its Member States' asylum systems have been overburdened due to large flows of asylum seekers.<sup>65</sup> The Relocation Scheme can serve as proof that EU Member States have indeed been confronted with a mass influx situation which falls within the Temporary Protection Directive's scope. Yet again, the Directive has not been activated.

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59 M. Ineli-Ciger, 'Time to Activate the Temporary Protection Directive: Why the Directive can Play a Key Role in Solving the Migration Crisis in Europe', 18 EJM (2016) 1-33, 16.

60 Regulation (EU) No 604/2013 of the European Parliament and of the Council of 26 June 2013 establishing the criteria and mechanisms for determining the Member State responsible for examining an application for international protection lodged in one of the Member States by a third-country national or a stateless person, [2013] OJ L180/31. (hereinafter Dublin III).

61 Ibid, Article 3.

62 J. Mink, 'EU Asylum Law and Human Rights Protection: Revisiting the Principle of Non-Refoulement and the Prohibition of Torture and Other Forms of Ill-Treatment', (2012) 14 EJML 119-149, 121. See also cases of *MSS v Belgium and Greece* (App No 30696/09 (ECtHR, 21 January 2011) and *NS v SSHD and ME v SSHD* (Joined Cases C411/10 and C493/10, N.S. and M.E. (EU:C:2011:865), *Tarakhel v Switzerland* (App No 29217/12 (ECtHR, 4 November 2014), *C.K. and Others v Supreme Court of Republic of Slovenia* (Case C578/16).

63 Council Decision (EU) 2015/1601 of 22 September 2015 establishing provisional measures in the area of international protection for the benefit of Italy and Greece, [2015] OJ L248/80.

64 J. Mitchell, 'The Dublin Regulation and Systemic Flaws' (2017) 18 SDILJ 295. 320.

65 Ineli-Ciger (n 59), 17.

The wording of the Directive in defining mass influx has allowed the EU to avoid its activation for over a decade. Its vague nature and the terms used to define mass influx, such as '*large number*,' are not objective and do not have legal standing.<sup>66</sup> As explained throughout this section, Member States have been in situations where their national asylum systems have been overburdened but the Directive was not activated. Both of the responses of the EU Commissioners show their heavy reliance on the ambiguous wording of the Directive. The vague terms make it almost impossible to quantify what can amount to mass influx despite overwhelming evidence, including a comparing of the numbers of asylum seekers during the Balkan war, Article 3 ECHR violations due to Member States' asylum systems being systemically flawed and the Relocation Scheme, which prove that Member States have experienced mass influx of asylum seekers giving the opportunity to the Directive to be activated.

The resistance of the EU to activate this mechanism indicates that there is unwillingness for fair distribution of asylum seekers within Europe. The denial of mass influx and heavy reliance on the ambiguous wording of the Directive is a clear indication that the mechanism could be implemented post-Arab spring uprisings but it ended up being a missed opportunity.

## **Section Two: The activation procedure of the Temporary Protection Directive – Another obstacle**

This section aims to demonstrate that the complexity of the activation process of the Temporary Protection Directive, which was explained in detail in Chapter 1 of this piece, prove to be another obstacle for its implementation and use to respond to the current situation in Europe. It is argued that the activation process of the Directive undermines its very purpose, to respond to emergency situations, as it proves to be lengthy, complex and ambiguous.

Scholars argue that one of the key reasons for they inactivation of the Directive is the complexity and lengthy process that is required for the mechanism to actually be implemented.<sup>67</sup> As explained in Chapter 1, activation of the process can only be instructed by the Commission on its own accords or by receiving a formal request from a Member State. The key issue here is that the Directive does not explicitly mention the scope of the obligations of the Commission once it receives a request from a Member State.

Article 5 of the Directive simply states that the Commission should assess the request and then decide whether to propose it to the Council for consideration. As a result, the activation of the Directive can be subject to political debates every step of the activation process due to the absence of Commission obligations beyond assessing and deciding.<sup>68</sup> This means that the procedure immediately becomes longer with slim chances of achieving the qualified majority vote in the Council.<sup>69</sup>

It is also reasonable to argue that qualified majority vote will unlikely be achieved in regard to the Temporary Protection Directive because Member States who do not belong to the borders of the EU and are not particularly affected by large inflows of asylum seekers have no reason or incentive to activate this mechanism.<sup>70</sup> It is highly likely that these Member States will not vote for the activation of this mechanism and would prefer to continue using the Dublin III Regulation which distributes asylum seekers to the country of first entry should they not meet the other hierarchy criteria.<sup>71</sup> This means that asylum seekers will continue to be in bordering Member States whose asylum systems are suffering and cannot respond to the numbers of people received.

The activation procedure includes a large number of steps to be followed and debates in the Council which make the mechanism a slower tool to respond to the situation that what is currently implemented.

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66 D. Gulns & J. Wessels, (n 6), 62.

67 Ineli-Ciger (n 59), 13.

68 H. Beirens, S. Maas, S. Petronella. M. Velden (n 24), 2.

69 Ibid.

70 Ineli-Ciger (n 51), 235.

71 Ibid.

This means that the purpose of the Directive in distributing responsibility to all Member States during emergency situations is defeated as the process becomes exceptionally lengthy that the response stops being immediate.

### **Section Three: Is the Solidarity Clause a positive aspect of the Directive?**

Section three will examine the solidarity mechanism the Directive includes. It will analyse the positive aspects of this clause but will ultimately demonstrate that it offers nothing to the Directive, as solidarity has been a fundamental principle of the EU as well as the Common European Asylum System (CEAS) but has not been implemented to its full capacity by Member States.

Articles 24 and 25 of the Directive set out the solidarity mechanism of the legislation should it be activated. These provisions include both financial solidarity through the European Refugee Fund<sup>72</sup> as well as physical solidarity through allowing asylum seekers in Member States' asylum system when another Member State is overburdened.<sup>73</sup>

Upon first glance, the solidarity mechanism present in the Directive seems to be a positive aspect which demonstrates the willingness of the EU to assist its Members when they are confronted with a mass influx situation. However, these provisions are voluntary and it is up to the Member States to decide whether they wish to participate in these measures.<sup>74</sup> This allows for some Member States to choose not to participate in the fair sharing of responsibility clause within the Directive, while others who may volunteer will have to potentially sustain more asylum seekers than possible due to their fellow Member States non-participation.<sup>75</sup>

The solidarity mechanism is again ambiguous as it does not provide for any form of guidance to Member States should they decide to participate. There is lack of information on how the distribution of asylum seekers would take place and under what criteria. However, the Council retains full power to introduce measures regarding the solidarity mechanism therefore, whether these measures are successful depends entirely on the Council and thereafter the implementation by Member States.<sup>76</sup>

Arguably, Member States do not need to be bound by the Directive to exercise solidarity amongst them nor should the council take measures to enforce this mechanism. This is because solidarity is found at the core of the Union as well as CEAS therefore, Member States are already bound by solidarity. Article 80 TFEU highlights that the policies of the Union must be governed by solidarity and fair sharing of responsibility including any financial implications. Article 80 TFEU reads:

*"The policies of the Union set out in this Chapter and their implementation shall be governed by the principle of solidarity and fair sharing of responsibility, including its financial implications, between the Member States. Whenever necessary, the acts of the Union adopted pursuant to this Chapter shall contain appropriate measures to give effect to this principle."*

Solidarity has been an ongoing problem for the Union as Article 80 itself is unclear. The provision has been described as vague because it lacks clarity for Member States therefore, it leaves questions unanswered; can Member States define solidarity differently from one another? Can Member States demonstrate their fair sharing of responsibility differently or should there be a uniform and collective approach as to what article 80 entails?<sup>77</sup>

Karageorgiou states that Article 80 is to be understood in two different dimensions. Firstly, an interstate dimension which allocates responsibility between Member States and secondly a refugee dimension

<sup>72</sup> Article 24, Temporary Protection Directive.

<sup>73</sup> Ibid, Article 25.

<sup>74</sup> H. Beirens, S. Maas, S. Petronella. M. Velden (n 24), 2.

<sup>75</sup> Ineli-Ciger (n 51), 230.

<sup>76</sup> Ibid, 231.

<sup>77</sup> E. Karageorgiou, 'Solidarity and Sharing in the Common European Asylum System: the Case of Syrian Refugees', [2016] 17(2) EPS 196-214, 199.

which provides protection to individuals in need based on the international and European asylum rules.<sup>78</sup>

However, there is a different perspective relating to the meaning of Article 80 and the extent of the provision. It can be argued that one of the European Union's fundamental objectives was to create a barrier-free market that would facilitate free movement of goods and people, which subsequently enables barrier-free movement. Therefore, if there are no internal borders between Member States, a decision for a third country national or an asylum seeker to enter European territory becomes a shared concern of all Member States.<sup>79</sup>

The CEAS is to be carried out in accordance with the fair sharing of responsibility principle however, it has constantly omitted to take into account the different situations and capacities of all Member States in the asylum process. Instead Member States are bound by the same International and European obligations.<sup>80</sup> As a result, some Member States become overwhelmed with asylum seekers and are not receiving adequate help from other Member States. This leads to aggressive policies by particular Member States in order to manage the large flows of asylum seekers.<sup>81</sup>

Evidently, solidarity and burden sharing have been at the core of the Union before the Directive was born, but it proves challenging for Member States to adhere to these obligations when their national interests are conflicted with those of the Union. As previously explained, it is reasonable to assume that Member States who are not experiencing mass influx of asylum seekers have no incentive to volunteer in allowing third country nationals in their territories other than to demonstrate good faith to fellow Member States. However, good faith is not reliable to ensure that Member States will want to participate in this mechanism. CEAS is bound by solidarity nonetheless but there are still Member States whose asylum systems are not functioning due to the large number of asylum seekers and have even been described as systemically flawed. Therefore, if all Member States were interested in upholding their obligations for solidarity they would but so far they have not, thus, implementing the Directive and invoking the solidarity clauses is unlikely to have any effect.

## **Section Four: The fear for the Directive becoming a pull factor**

Section Four will establish that the possibility of non-implementation due to fear from Member States for the Directive to become a pull factor is legitimate. However, this section will argue that should the Directive be activated it is unlikely to become a pull factor. Nevertheless, this fear has caused the Union to resort to externalisation of asylum seekers instead of absorption through Member States' national asylum systems. Two externalisation policies will be discussed in this section; the Italy and Libya Memorandum and the EU and Turkey agreement.

These policies will be examined due to their controversial nature as they do not absolutely comply with international principles such as non-refoulement. Italy is a border Member State that has experienced overburdening of its asylum system, while Turkey is a State that has a proximate geographical location to Europe which allowed for the creation of this agreement.<sup>82</sup>

Numerous Member States believe that the activation of the Temporary Protection Directive will create a pull factor for asylum seekers that are trying to enter the EU, and this is one of the main reasons

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78 Ibid.

79 E. Kucuk, 'The Principle of Solidarity and Fairness in Sharing Responsibility: More than Window Dressing', [2016] 22(4) ELJ 448-469, 449.

80 L. M. Langford, 'The Other Euro Crisis: Rights Violations Under the Common European Asylum System and the Unravelling of EU Solidarity' (2013) 26 HHRJ 217-264, 240.

81 Ibid 244.

82 See page 4.

behind the inactivation of the Directive.<sup>83</sup> Pull factors are elements that may attract asylum seekers to different Member States or host countries<sup>84</sup> which can then result to asylum shopping.<sup>85</sup>

However, this fear is not necessarily true nor will it materialise should the Directive be activated. This is because asylum seekers who are fleeing war or violence do not really search for a wealthier host state than their country of origin, instead they are in need of a safe place where they can protect themselves from conflict or persecution.<sup>86</sup> It is not uncommon that victims of violence and armed conflict do not wish for permanent stay in a host country, the wish to return to their country of origin and that is why they usually choose to flee to neighbouring states to their country of origin.<sup>87</sup> This argument is supported by figures as by 2013 over two million Syrian asylum seekers had fled their country but pursued refuge in neighbouring countries such as Lebanon, Iraq, Egypt, Jordan and Turkey.<sup>88</sup>

These figures demonstrate that pull factors should not be a central consideration when the asylum seekers arriving to Europe are escaping armed conflict and violence, something that proves to be an immediate threat to a person's life.<sup>89</sup> Therefore, even if the Directive is activated, figures show that it is unlikely that the numbers of asylum seekers would suddenly increase but even if they theoretically did, the Council holds the power to introduce measures that would control these pull factors.<sup>90</sup> In addition, the Union introduced other mechanisms to assist with the situation such as the Relocation Schemes, which did not prove to become a pull factor for asylum seekers, there was no significant change in numbers and in fact, the quotas were not met, as mentioned above.

Despite these arguments, it is strongly supported that the fear that asylum seekers will arrive to Europe in large numbers and be eligible to temporary protection to other Member States and not only bordering States creates the externalisation policies that the EU has been following to respond to the large inflows. A prime example of these policies is the Italy and Libya Memorandum.

The relationship between Italy and Libya is not novel, these two countries have been cooperating via various agreements and protocols from 2000 to 2009.<sup>91</sup> These agreements were the prime facilitators for various push backs of refugees that took place between Italy and Libya. Although they may not form the legal basis of the push backs, they establish the legal framework which caused the push backs of asylum seekers mainly in 2009.<sup>92</sup>

During the 2009 push backs from Italy to Libya, the Italian government stated that Libya is considered a safe haven for refugees despite not being signatory to the 1951 Refugee Convention. Not only is Libya not part of the Refugee Convention, these push backs took place during Ghaddafi's regime which was notorious for its ill-treatment of refugees, undermining their basic human rights.<sup>93</sup>

Italy could be held accountable for the push backs that took place in 2009. Italy returned asylum seekers to Libya by patrolling international waters and Libyan coasts and subsequently collecting and boarding refugees trying to illegally travel through sea to reach European soil on Italian boats and taking them back to Libya<sup>94</sup>. Evidently these practices were not compliant with the non-refoulement principle. The

83 A. Klug, 'Regional Developments: Europe' in A. Zimmermann (ed), *The 1951 Convention Relating to the Status of Refugees and Its 1967 Protocol: A Commentary* (oup 2011) 133.

84 Ineli-Ciger (n 51), 233.

85 Asylum shopping is a term used to describe the practice of an asylum seeker applying for protection in different host countries concurrently or attempting to apply for International protection in a particular Member State following her entrance to a different Member State in search for the best reception conditions, procedural standards or recognition rates. See V. Moreno-Lax, 'Dismantling the Dublin System: M.S.S v Belgium and Greece' (2012) 14 EJML 1-2.

86 Ineli-Ciger (n 51), 234.

87 Ibid.

88 UNHCR, 2014 Syrian Regional Response Plan < <http://www.unhcr.org/syriarrp6/docs/syria-rrp6-strategic-overview.pdf#C> > 2004, accessed 3 July 2019.

89 Ineli-Ciger (n 51), 234.

90 Ibid.

91 Protocollo Aggiuntivo Tecnico-Operativo concernente l'aggiuntarsi un articolo al Protocollo firmato a Tripoli il 29/12/2007 tra la Repubblica Italiana e la Gran Giamahiria Araba Libica Popolare Socialista, per fronteggiare il fenomeno dell'immigrazione clandestina (Tripoli, 4 Feb 2009) (Executive Protocol).

92 M. Giuffrè, 'State Responsibility beyond Borders: What Legal Basis for Italy's Push-Backs to Libya' (2012) 24 IJRL 692, 700-701, 705.

93 Ibid, 700.

94 Ibid, 704.

Italian government tried to claim that its actions at sea were 'search and rescue' operations, in which they had to disembark the refugees to a safe place. Italian authorities argued that this did not place the asylum seekers at threat of being tortured or ill-treated.<sup>95</sup> However, Libya cannot be considered as safe place, since it was proven to be inadequate to respond to large migration flows.<sup>96</sup>

Italy and Libya have signed a new Memorandum of Understanding in 2017.<sup>97</sup> The main objective of the agreement is to minimise refugee entries on Italian soil by rapidly securing Libya's borders to prevent asylum seekers from leaving.<sup>98</sup> An interesting point is that the Memorandum does not mention refugees or asylum seekers, it only mentions clandestine or illegal migrants. Palm argues that this is an attempt to create a rhetoric that connects different legal statuses to a uniform category of people that are denied the right to enter Europe.<sup>99</sup>

This agreement is a clear expression of the EU's desire to shift responsibility to third non-EU states<sup>100</sup> but this approach leads to other irregular routes appearing which could be more dangerous for asylum seekers as well as more profitable to smugglers.<sup>101</sup> This defeats the purpose of the Memorandum as one of its aims is to reduce smugglers. On the other hand, Italy has been receiving vast numbers of asylum seekers due to its geographical position driving the country in a 'desperate' situation where it could not sustain asylum seekers.<sup>102</sup> Italy made appeals for assistance from the rest of the EU as well as a request for the activation of the Directive however, it did not receive help from fellow Member States nor EU bodies, leading Italy into entering agreements of this nature.<sup>103</sup>

The EU's externalisation policy becomes evident in the EU and Turkey agreement<sup>104</sup> as well. In March 2016 the European Union and Turkey entered into an agreement, where it was agreed that all irregular migrants crossing from Turkey to Greece would be returned to Turkey, to halt human smuggling and smuggling networks.<sup>105</sup> This agreement consisted of nine points<sup>106</sup> which can be described as incentives for Turkey to hold refugees out of Europe. In particular, the EU promised visa liberalisation for Turkish citizens and an overall amount of six billion euros to take responsibility of asylum seekers who have entered European territory via Turkey.

The argument that the EU entered into an agreement with Turkey to tackle illegal crossings, is unsubstantial. The truth behind this agreement is that the EU was eager to portray an image of a highly involved and active entity in the large flows of asylum seekers post-Arab spring uprisings.<sup>107</sup>

The political nature of the agreement on Turkey's part is evident from statements the Turkish President Tayyip Erdogan has made throughout the negotiations. He openly threatened the Union stating that he

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<sup>95</sup> Ibid, 705-706.

<sup>96</sup> Ibid.

<sup>97</sup> Memorandum of understanding on cooperation in the fields of development, the fight against illegal immigration, human trafficking and fuel smuggling and on reinforcing the security of borders between the State of Libya and the Italian Republic (2 February 2017).

<sup>98</sup> A. Palm, 'The Italy-Libya Memorandum of Understanding: The baseline of a policy approach aimed at closing all doors to Europe?' (Odysseus Blog 2 October 2017) <<http://eumigrationlawblog.eu/the-italy-libya-memorandum-of-understanding-the-baseline-of-a-policy-approach-aimed-at-closing-all-doors-to-europe/>> accessed 3 July 2019.

<sup>99</sup> Ibid,2.

<sup>100</sup> Ibid, 4.

<sup>101</sup> Ibid.

<sup>102</sup> L. M. Langford, 'The Other Euro Crisis: Rights Violations Under the Common European Asylum System and the Unravelling of EU Solidarity' (2013) 26 HHRJ 217-264, 247.

<sup>103</sup> Ibid.

<sup>104</sup> European Council, 'EU-Turkey Statement', 18 March 2016 MEMO 16/963.

<sup>105</sup> Ibid.

<sup>106</sup> Ibid.

1. All irregular migrants crossing from Turkey to Greece to return to Turkey;

2. For every Syrian being returned to Turkey another Syrian will be resettled;

3. Turkey will take any necessary steps to prevent routes of irregular migration from Turkey to the EU;

4. Once irregular movements are minimised a voluntary humanitarian organisation admission scheme will be activated;

5. Visa liberalisation roadmap will be accelerated;

6. Speeding up the disbursement of the 3 billion euros to Turkey;

7. The EU and Turkey welcomed the ongoing work on the upgrading of the Customs Union;

8. When resources are used in full another 3 billion to be given;

9. EU and Turkey will work to improve humanitarian conditions in Syria.

<sup>107</sup> K. M. Greenhill, 'Open Arms Behind Barred Doors: Fear, Hypocrisy and Policy Schizophrenia in the European Migration Crisis', (2016) 22 ELJ 317, 320.

would send millions of refugees to the EU if Turkey did not receive the promised funds by the Union.<sup>108</sup> Arguably Europe is attempting to create a border between itself and the asylum seekers through third countries. Therefore, in the words of Greenhill, Turkey has become a “waiting room for refugees”.<sup>109</sup> Europe is sending a message of deterrence to refugees via the EU-Turkey Agreement while ignoring fundamental principles of refugee law.

This agreement is only beneficiary to two entities, Turkey and the EU. Asylum seekers, who are projected as the centre of this agreement, are at a clear disadvantage by having their international rights infringed to satisfy international political interests. Both actors used displaced persons as bargaining chips whilst instrumentalising human beings for national State interests.<sup>110</sup> Instead of focusing on its territory and tackle the intrinsic problem of the Union’s asylum system, Europe has chosen to focus on an agreement with a third State whilst border states still receive refugees.<sup>111</sup>

Consequently, due to the fear of the Directive becoming a pull factor and ultimately more asylum seekers arriving to Europe, the EU chose to enter into agreements with unsatisfactory legal standing in order to enhance its externalising policies during the large inflows of asylum seekers. These responses are utterly inadequate as the Union could have activated the Directive and allow it to serve its purpose, assisting in emergency situations, without having to compromise its own Members’ asylum systems.

## Concluding remarks

This Chapter focused on the challenges the Temporary Protection Directive faces that could provide reasoning in its inactivation. In addition, this Chapter examined EU responses to the inflows of asylum seekers to demonstrate an externalisation policy development and resistance to activation of the Directive due to fearing it would become a pull factor. To demonstrate these, this chapter was divided in four sections.

Section One analysed Article 2(a) of the Directive which includes the mass influx clause. It was argued that the broad nature of the Article and the lack of clear definition of what amounts to mass influx has allowed the EU to ignore some of its Member’s requests for activation under the pretence of the situation not amounting to mass influx. However, section one demonstrated that the numbers of asylum seekers in 1992 and 2015 are if not higher at least comparable which amounts to an indication of mass influx. Furthermore, it was demonstrated that recognition of systemically flawed asylum systems in the wording of the Dublin III Regulation as well as the Relocation Scheme amount to an acknowledgment by the Union that there is a mass influx situation.

Section Two examined the complexity of the activation procedure of the Directive. It was argued that the length of the process undermines the purpose of the Directive, which is to provide immediate relief to Member States whose asylum systems are overburdened. This section also contended that a qualified majority vote in the Council will be unlikely achieved as Member States who are not major hosts of asylum seekers have no incentives in voting in favour of the activation of the Directive.

Section Three discussed the solidarity clause found in Article 24 and 25 of the Directive and argued that despite this mechanism appearing as a helpful tool in the Directive, in reality it has no legitimate power. This was argued in the light of solidarity as a whole within the Union. Section three examined Article 80 TFEU and established that solidarity is a key element of the CEAS however, it has not been upheld by Member States as there are a number of states with disturbed national asylum systems such as Italy and Greece, and other States who are enforcing stricter controls on asylum seekers.

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108 ‘Turkish President Threatens to Send Millions of Syrian Refugees to EU’, *The Guardian* (11 February 2016) <[www.theguardian.com/world/2016/feb/12/turkish-president-threatens-to-send-millions-of-syrian-refugees-to-eu](http://www.theguardian.com/world/2016/feb/12/turkish-president-threatens-to-send-millions-of-syrian-refugees-to-eu)> accessed 17 July 2019.

109 Greenhil (n 107), 327.

110 I. M. Borges, ‘The EU-Turkey Agreement: Refugees, Rights and Public Policy’ (2017) 18 *Rutgers Race LR* 121, 139.

111 M. H. Zoetewij, ‘The European Agenda on Migration: Let’s Talk Turkey’, (2016) *JIANL* 142-158, 158.

Section Four stated that the Directive has not been implemented yet due to the fear of it becoming a pull factor. However, it was argued that it is unlikely for this event to materialise because asylum seekers fleeing armed conflict or violence do not tend to seek for wealthier host states as they view their stay as temporary. Moreover, the Council could implement measures to control these pull factors but it became clear that the Union is not interested in activating the Directive as it has shifted its focus on externalising policies with regard to asylum seekers. This was proved through two examples of EU externalisation policies; the Italy and Libya Memorandum and the EU and Turkey Agreement.

### **Chapter 3: Were the asylum seeker flows post-Arab Spring a missed opportunity to use the Temporary Protection Directive?**

Chapter three will analyse whether the asylum seeker flows of 2011 and onwards, following the Arab Spring uprising, were a good opportunity for the European Union to finally activate the Temporary Protection Directive. This Chapter will consist of two sections. Section One will provide an overview of the events that lead to the large flows of asylum seekers due to the Arab Spring uprisings. It will demonstrate that it was appropriate to activate the Directive but instead, Member States focused on their national interests rather than respecting EU and CEAS principles of solidarity and fair sharing. Section Two will aim to establish that the Temporary Protection Directive has now become obsolete as the chances of it being activated are slim and the Union prefers to rely on other mechanisms to respond to the current situation of asylum seeker influx.

#### **Section One: The Arab Spring uprisings and the response of the European Union**

This section will provide a synopsis of the events that took place in 2011 during the Arab Spring uprisings which lead to large numbers of people seeking asylum to arrive to Europe. It is strongly supported that these arrivals were a perfect opportunity for the activation of the Temporary Protection Directive since there were Member States whose national asylum systems were overburdened but once again, it was not activated due to Member States' resistance.

The Arab Spring conflicts started to take place in 2011, which was when the border controls of Southern Member States started collapsing. In 2011 there were many arrivals from Tunisia following the conflicts in the country and the subsequent fall of former President Zine el-Abidine Ben Ali.<sup>112</sup> The numbers of asylum seekers in Europe also increased following the fall of Muammar Gaddafi and his regime in Libya along with the intervention from the North Atlantic Treaty Organisation (NATO) which drove many Libyans out of the country.<sup>113</sup> As a result the number of asylum seekers reaching Europe increased dramatically, specifically in May of 2011, twenty six thousand Tunisians arrived to the Italian island of Lampedusa.<sup>114</sup> As discussed in Chapter Two of this piece, the Italian government urged the European Commission to activate the Directive at the time, something that never happened.

Instead of activating the Temporary Protection Directive to assist Italy whose national asylum system was struggling to cope with the arrivals, the EU chose to strengthen its border controls and surveillance around the Mediterranean.<sup>115</sup> Italy was clearly struggling thus in April 2011 as it signed an agreement with Tunisia which aimed to enhance border controls and to facilitate the return of Tunisian asylum seekers who arrived to Italian territory.<sup>116</sup> The Italian Government then proceeded in issuing temporary

<sup>112</sup> S. McMahon, 'North African Migration and Europe's Contextual Mediterranean Border in Light of Lampedusa Migrant Crisis of 2011' (European University Institute 2012) 6.

<sup>113</sup> Ibid, 6.

<sup>114</sup> S. Carrera, E. Guild, M. Merlino and J. Parkin, 'A Race against Solidarity: the Schengen Regime and the Franco-Italian Affair' (2011) *ceps Liberty and Security in Europe Working Papers*, 4.

<sup>115</sup> C. Malmström, 'Debate on Migration Flows' (n 54).

<sup>116</sup> B. Nascimbene & A. Di Pascale (n 52), 352.



residence permits for humanitarian reasons for asylum seekers who arrived to Italy before the fifth of April 2011.<sup>117</sup> Evidently, these permits gave their holders the right to move freely within the European Union<sup>118</sup>. Italy found itself being heavily criticised for issuing these permits by fellow Member States such as France, Germany and Austria.<sup>119</sup> In an act of protest, France shut its borders to Tunisian asylum seekers arriving from Italy on the seventeenth of April 2011.<sup>120</sup> Moreover, Belgium introduced additional entry requirements and even asked people who were holders of Italian residence permits to show evidence of having at least ten thousand euros in their possession, per couple, in order to enter Belgian territory.<sup>121</sup>

The Italian example demonstrates clearly that Member States were not willing to open their borders to asylum seekers, quite the contrary. This further strengthens the argument made in Chapter 2, Section Three, that there is lack of solidarity and trust between Member States. Had there been trust between Member States in regard to each other's asylum systems, France for example, would not have felt the urge to shut its borders to asylum seekers arriving from a fellow Member State who were also residence permit holders. It could also be argued that it is the lack of fair sharing of responsibility and inactivation of the Directive that lead the Italian authorities to issue such permits which allowed for free movement, perhaps to force other Member States to take part in burden sharing.<sup>122</sup> It is therefore, evident that Member States do not adhere to their obligations under fundamental Union Law as well as their obligations according to CEAS because they do not seem to be respecting the principle of solidarity. Therefore, it could be argued that as long as the activation of Temporary Protection Directive does not serve the national interests of Member States it will not be activated.<sup>123</sup>

There is absolute lack of solidarity within the Union especially when it comes to burden sharing as there is no effective mechanism in place to promote fair sharing effectively.<sup>124</sup> It is questionable why such mechanism was added in the Temporary Protection Directive in the first place, since its activation process is lengthy and complicated and no Member State adheres to its obligation of solidarity. It could be concluded that the inclusion of such mechanism is perhaps just symbolic. Therefore, the chance of activation of the Directive is particularly small.

The Arab Spring uprisings, met all the criteria for the activation of the Directive, however, it was not activated because of national interests. These events were much more severe than those of the Balkan War in the 1990s based on numbers, thus the EU had an excellent opportunity to activate this mechanism and assist its Southern Member States but it simply did not, and used other possible solutions to the asylum seeker flows. As a result, one questions is 'if the Temporary Protection Directive has not been activated during the Arab Spring uprisings will it ever be activated?' This question is answered in the negative. It is clear that the European Union wishes to use other instruments to deal with this mass influx situation thus, should there be a similar situation in the future it is highly unlikely that the Temporary Protection Directive will be used.

## **Section Two: The Temporary Protection Directive is now obsolete**

This section will establish that the Temporary Protection Directive has become obsolete because the European Union chose to deal with the large asylum seeker flows through other mechanisms, something that demonstrates clear resistance to the activation of the Directive.

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117 S. McMahon (n 112).

118 B. Nascimbene & A. Di Pascale (n 52), 353.

119 S. Carrera, E. Guild, M. Merlino and J. Parkin (n 114), 11.

120 Ibid.

121 J. Dacey, 'Tunisian Talks Held amid Growing Refugee Crisis' Swissinfo (20 April 2011)

<<http://www.swissinfo.ch/eng/tunisian-talks-held-amid-growing-refugee-crisis/30048800>> accessed 8 August 2019.

122 M. Ineli-Ciger (n 51), 241.

123 Ibid.

124 Ibid, 242.

As established in Chapter Two of this article, the European Union created other emergency responses to the asylum seeker flows instead of activating the Temporary Protection Directive. These responses included the Relocation Scheme and the EU and Turkey agreement. However, the Union responded to the asylum seeker flows through more permanent actions which included the creation of the European Asylum Support Office.<sup>125</sup> EASO was established in 2011 in order to harmonise as well as support common action while helping the asylum and reception systems of Member States which find themselves under particular pressure due to the extremely heavy and urgent demands their national asylum systems may face during emergency times.<sup>126</sup> The creation of this Office demonstrates that the European Union does not want to necessarily activate an emergency mechanism such as the Temporary Protection Directive. Arguably it seems to wish for the creation of more permanent measures which will assist in relieving the pressure off certain Member States, whilst perhaps avoiding the distribution of asylum seekers throughout its territory.

It is evident that the Union continuously dismisses the Directive and does not want to use it. When asked why the Temporary Protection Directive has never been activated, the European Council simply argued that it did not activate this mechanism because the Commission had not submitted a proposal before the Council.<sup>127</sup> The Council also cited the Relocation Scheme to answer about the non-implementation of the Directive in an attempt to demonstrate that European bodies are helping Member States which are in need.<sup>128</sup> However, this is not enough as the avoidance to answer clearly as to why the Directive has not been implemented when it was very fitting for the current situation demonstrates the exact unwillingness of the Union to promote a uniform and fair mechanism to distribute asylum seekers. The Council also noted that the current situation is being dealt under the Dublin III Regulation which demonstrated its inadequacy and is in need of reform.<sup>129</sup>

As mentioned in Chapter 2, Dublin III was not implemented to be an emergency mechanism however, it has become one and this is why the Union is now dealing with systemic flaws within its Member States' national asylum systems.

Moreover, the European Commissioner, Dimitris Avraamopoulos, explicitly stated that the Union does not believe that the Temporary Protection Directive is an appropriate measure to respond to the current situation. Instead, he stated that the only regulatory measure which would be sufficient to deal with the large asylum seeker flows would be the reformed Dublin Regulation, Dublin IV<sup>130</sup>.<sup>131</sup> Therefore, if the European Commissioner explicitly states that the Temporary Protection Mechanism will not be activated for the current situation because of the already implemented Dublin III Regulation and its anticipated reforms through Dublin IV, is a clear indication that the chances of activation are particularly slim. This further strengthens the notion that Union wishes to keep the mechanisms that it has already implemented to respond to the migrant flows whilst continuing its externalisation policies.<sup>132</sup>

It is of key importance to establish the competence of the Dublin Regulation and the reforms it will undergo to emerge as the new Dublin IV Regulation. This is to demonstrate that there are no significant differences between the Dublin IV Regulation and its predecessors therefore, it could be argued that even with the reforms this Regulation will continue to be an inadequate response to the current situation.

The Dublin III Regulation has been strongly criticised for imposing disproportionate burden on Member States that are located on the external frontiers of the European Union.<sup>133</sup> This argument is supported

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<sup>125</sup> Regulation (EU) No 439/2010 of the European Parliament and of the Council of 19 May 2010 establishing a European Asylum Support Office, OJ L 132/11, 29 May 2010 (thereinafter EASO). <sup>[125]</sup>

<sup>126</sup> *Ibid.*

<sup>127</sup> Council of the European Union, Reply to Parliamentary Questions, 15326/15 (15 December 2015) <<https://data.consilium.europa.eu/doc/document/ST-15326-2015-INIT/en/pdf>> Accessed 8 August 2019.

<sup>128</sup> *Ibid.*

<sup>129</sup> *Ibid.*

<sup>130</sup> Proposal for a Regulation of the European Parliament and of the Council establishing the criteria and mechanisms for determining the Member State responsible for examining an application for international protection lodged in one of the Member States by a third country national or a stateless person (recast) COM(2016) 270 (thereinafter Dublin IV).

<sup>131</sup> LSE Podcast (n 55), minute 57:13.

<sup>132</sup> See Chapter 2.

<sup>133</sup> See Chapter 2.

by the strong adherence of the Union to Dublin and its hierarchy criteria and its constant rejection of temporary protection. It is not unreasonable to argue that non-border Member States reject the possibility of activation of the Temporary Protection Directive because it is substantially easier to use the Dublin III exceptions route under Article 3(2) to relocate an asylum seeker to non-border Member States. Due to Member States resistance of fair distribution of asylum seekers, small-scale relocations within Dublin III are more achievable.<sup>134</sup> Consequently, it proves to be more difficult to mobilise the entirety of the Union into hosting asylum seekers equally therefore, the frontline Member States continue to bear most of the responsibility.<sup>135</sup> The message sent is that the EU is unwilling to create a large-scale, fair system of distributing asylum seekers to each Member State. In the event of failure the Union will have to accept responsibility. Contrary, adhering to the Dublin III rules blindly and constantly highlight that border Member States responsible for the vast majority of asylum seekers need help, proves to be a gateway for EU institutions to shift the blame for the failure of the system on someone else.<sup>136</sup> It could not be any clearer that the Union is not willing to view Dublin III and its flaws as a genuine problem with solidarity in the entirety of the EU. The questions remain whether Dublin IV can respond to the current situation adequately or will it simply bear the same inadequacies as Dublin III.

Essentially, the Dublin IV Regulation will continue to bear the evidently problematic hierarchy criteria for the determination of the Member State responsible for the examination of the asylum application however, a corrective allocation mechanism will be introduced through this new Regulation.<sup>137</sup> The new reforms include an automated system which will monitor the number of asylum application received and the number of persons that were resettled in different Member States, a reference key in order to determine when a Member State's national asylum system is under disproportionate pressure and can no longer function to its full capacity and lastly the fairness mechanism which will work to address and distribute responsibility to relieve the pressure from certain Member States in need.<sup>138</sup> With regard to the fairness mechanism it is proposed that it will be activated when Member States are faced with a disproportionate number of asylum application, if this number exceeds one hundred fifty percent of the reference share, then this mechanism will be activated automatically.<sup>139</sup>

Following the activation of this mechanism, all asylum seekers whose applications were made after the triggering of the mechanism will be distributed and allocated across other EU Member States.<sup>140</sup> The reform also considers the possibility where a Member State does not accept the asylum seekers allocated to it after the activation of the mechanism, and it states that should this occur then that Member State will make a two hundred and fifty thousand euros '*solidarity contribution*' per applicant.<sup>141</sup>

While these reforms may seem promising, the proposal has received criticism criticisms for merely attempting to protect Member States from financial responsibility due to the absorption of refugees.<sup>142</sup> It is argued that this new system will further deepen inequality between Member States whilst continuing to undermine the fair sharing of responsibility principle.<sup>143</sup> Furthermore, the Dublin IV proposal is focused on the improvement of the Member States' capacity systems which would help improve the determination of Member State responsibility for application examination.<sup>144</sup> Therefore, the reforms are not focused on the protection of the individual nor are they particularly humanitarian in nature, instead, they focus on improving the position of the Member States.

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<sup>134</sup> N. B. Selanec, "A Critique of the EU Refugee Crisis Management: On Law, Policy and Decentralisation", [2015] 11 CYELP 73-114, 106.

<sup>135</sup> Ibid.

<sup>136</sup> Ibid.

<sup>137</sup> European Parliament, 'Briefing – EU Legislation in Progress: Reform of the Dublin System', (1 March 2019), 4.

<sup>138</sup> Ibid.

<sup>139</sup> Ibid, 5.

<sup>140</sup> Ibid.

<sup>141</sup> Ibid.

<sup>142</sup> S. C. Young, Dublin IV and EXCOM: 'Aspirational Blunders and Illusive Solidarity' (2017) 19 EJML 370-395, 373.

<sup>143</sup> Ibid.

<sup>144</sup> M. L. Radovic and B. Cuckovic, 'Dublin IV Regulation, The Solidarity Principle and Protection of Human Rights – Step(S) Forward or Backward?', EU and Comparative Law Issues and Challenges Series Issue 2, (2018) 10-30, 14.

Despite the criticisms for the Dublin IV Regulation, it is still a supported mechanism to deal with the current situation in Europe, as affirmed by the European Commissioner. Therefore, the Temporary Protection Directive will highly unlikely be implemented, it has most likely become obsolete. This is because many of the positive elements that are contained in the Temporary Protection Directive are also reflected in the newer instruments of the Union, which makes it difficult for the Directive to be activated if there are similar mechanisms already implemented.<sup>145</sup> These mechanisms may not have proven to be successful, such as Dublin III, but nonetheless the Commission evidently, prefers using mechanisms that are already implemented and activated within the CEAS.

In addition, it would be easier for the Commission to attempt to tackle the current situation by revisiting an older mechanism which has been implemented for years and has obvious problems, and attempt to reform it.<sup>146</sup> In doing so, the Commission as well as EU Member States will not spend additional political capital in an attempt to activate or amend the Temporary Protection Directive, a mechanism which has never been activated and does not provide for certain results.<sup>147</sup>

## Concluding remarks

This Chapter analysed the reasons behind the Temporary Protection Directive becoming obsolete. However, it argued that if there was an appropriate time to activate it, the Arab Spring uprising asylum seeker flows in Europe were a particularly fitting opportunity that was missed. Furthermore, this Chapter argued that since the Directive was not activated during such events as the post-Arab Spring uprising migrant flows, the possibility of it being activated is extremely slim. This Directive will not be activated because the Union suffers from lack of solidarity between Member States, as a result, if a measure does not serve national interests of Member States then it is unlikely to be adopted even if it would help relieve the pressure from a fellow Member State.

Lastly, Section Two of this Chapter demonstrated that the Temporary Protection Directive has become obsolete and will unlikely be implemented through providing examples of the European Union wanting to continue using its current mechanisms. The Union does not want to venture into an uncertain mechanism and prefers to tackle the situation through its already implemented regulations that deal with asylum seeker flows. These being Dublin III and soon to be Dublin IV and the EASO. There also seems to be lack of acknowledgment and responsibility as to why the Directive was not activated, as the Council seems to suggest that the only reason for the non-activation was because the Commission never brought a proposal.

## Conclusion

This article aimed to establish that the Temporary Protection Directive could have been used in these times where Europe is facing a tremendous challenge with the amount of asylum seekers reaching its territory. However, there is constant resistance from non-bordering Member States when it comes to the activation of this mechanism. Instead, Europe has resorted to externalisation policies such as the EU and Turkey Agreements or assisted in the collapse of its own Member States' asylum systems as it failed to provide the necessary help under the solidarity clauses found in CEAS, TFEU and in the Directive itself.

Chapter One provided the reader with context as to how the Temporary Protection Directive was born. It discussed the Balkan War and explained that Europe created this Directive to respond to the flows

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<sup>145</sup> H. Beirens, S. Maas, S. Petronella. M. Velden (n 24), 11.

<sup>146</sup> Ibid.

<sup>147</sup> Ibid.

from the Balkan States. Furthermore, it examined the scope and application of the Directive and analysed its implementation procedure along with giving a brief overview of what the CEAS is.

Chapter Two examined the challenges the Directive faces and argues that its wording is ambiguous perhaps intentionally to avoid implementation. Its implementation procedure is also quite lengthy and complex which defeats its purpose of providing emergency relief to asylum seekers and other Member States. Lastly, the argument that activation of the Directive could become a pull factor is not supported. There is evidence that demonstrates that the intention of asylum seekers is not permanent resettlement.

Chapter Three analysed the 2011 asylum seeker flows and past Arab-Spring uprisings to demonstrate that it was a situation that was exceptionally fitting for the Directive to be activated. However, it became evident throughout this article that the European Union did not want to activate this Directive and wanted to use other mechanisms to deal with the situation such as the Dublin Regulation. As a result, the Directive is now obsolete, it is highly unlikely that it will ever be activated.

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# Can Huawei sue the US government for defamation? A study on the threshold of foreign state immunity from a comparative perspective

Martin Kwan

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## Introduction

Huawei has been criticized by the US government for its 5G products and services. This article raises a hypothetical<sup>1</sup> question: What if the allegations are false, can Huawei sue the US for defamation? If not, does it mean a state can rely on defamation to gain commercial advantage for its companies, or harm the competitiveness of companies from competing countries?

Defamation is particularly interesting and relevant for Huawei for two reasons. First, Jiang Xisheng (chief secretary of Huawei's board of directors), on behalf of Huawei, replied to the allegations that "[w]ith some people... no matter what you say to them, they will only say what they want to say. They won't listen to you."<sup>2</sup> Thus, this indicates that (1) there may be some untruth in the allegations and (2) it is difficult to rebut the allegations merely by words. Secondly, the feasibility of suing for defamation does not seem to have been considered. So far, Huawei has only considered suing the US government in the US arguing the ban in the US on its products is unconstitutional.<sup>3</sup>

This article will assess whether Huawei can sue, and, if yes, where can Huawei sue the US Government. In particular, it evaluates whether it is possible to sue the US government in Canada, England and Wales, Australia, China and the US. The focus of this article is whether Huawei *can* sue at all by lifting state immunity (i.e. a question of the legal threshold for suing the US government). It is not a study of whether a defamation claim will succeed (i.e. a question of the substantive laws) and hence the details of defamation laws is beyond the scope of this article. It will, however, evaluate how some of the allegations may be untrue, thus forming the grounds of a defamation claim.

In terms of academic contribution, it seeks to illustrate the difference in the scope of the foreign immunity laws of the above jurisdictions, through using the facts of Huawei-US controversy as a test case.

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<sup>1</sup> It is unknown with certainty regarding which allegation is true and which is untrue. Obviously only Huawei and the US government know the best, but certainly not the ordinary public when the allegations involve complex technological questions and national security (which means certain information on these matters are not publicly accessible). Thus, this article makes assumptions regarding the correctness of certain allegations for academic discussion (especially when the academic focus is on state immunity, not on defamation). No disrespect is intended to any country, organization, entity and person.

<sup>2</sup> Raymond Zhong, 'Who Owns Huawei? The Company Tried to Explain. It Got Complicated' *The New York Times* (25 April 2019) <<https://www.nytimes.com/2019/04/25/technology/who-owns-huawei.html>> accessed 8 February 2020.

<sup>3</sup> Essentially, it is a challenge on the constitutionality of s 889 of the John S. McCain National Defense Authorization Act for Fiscal Year 2019 (H.R.5515), which expressly bans federal agencies from using Huawei's products. It was reported that Huawei argued that the ban amounts to a "bill of attainder", and is therefore unconstitutional: Raymond Zhong and Paul Mozur, 'Huawei Said to Be Preparing to Sue the U.S. Government' *The New York Times* (4 March 2019) <<https://www.nytimes.com/2019/03/04/technology/huawei-lawsuit-us-government.html>> accessed at 8 February 2020. It was argued that the Congress "is effectively adjudicating on its own whether Huawei is influenced and subject to the Chinese government rather than allowing the executive and courts to make that judgment": Yuan Yang, 'Huawei lawsuit accuses US of 'unconstitutional' equipment ban' *Financial Times* (7 March 2019) <<https://www.ft.com/content/35731f8c-4080-11e9-b896-fe36ec32aece>> accessed at 8 February 2020 (quoting Glen Nager, partner at law firm Jones Day, which filed the complaint on behalf of Huawei).

For clarity, that action would not be blocked by (domestic) sovereign immunity, because it is not a tort action (like defamation) against the government, but is merely a constitutional challenge.

This lawsuit illustrates that Huawei is willing to sue the US. Also, it is interesting to note that the previous lawsuit was supported by China's foreign minister, Wang Yi, who commented that "[w]e support the company and individual in question in *seeking legal redress* to protect their own rights and interests, and refusing to be silent lambs": Yuan Yang, 'Chinese foreign minister Wang Yi backs Huawei's US lawsuit' *Financial Times* (8 March 2019) <<https://www.ft.com/content/176e6dda-4174-11e9-b896-fe36ec32aece>> accessed 8 February 2020 (emphasis added).

## The allegations made against Huawei

A number of allegations have been made against Huawei. The allegations are made by different entities and people from different countries. Notably the US government has been the notable voice against Huawei, and many others (be they authorized or related to the US government or not) expanded on the allegations. The allegations below are derived from various reputable and quality news sources, and only those made by the US government (or by personnel apparently related to or representing the US government)<sup>4</sup> are discussed below.

### Source of Huawei's funds

For example, it was reported that “the CIA had told spy chiefs that Huawei has taken money from the People's Liberation Army, China's national Security Commission and a third branch of the nation's state intelligence network”.<sup>5</sup>

### Allegation on Chinese government's power to influence Huawei

*Beijing could use the Chinese group's technology to conduct espionage or cyber sabotage.”<sup>6</sup> The concern is based on the worry over the Chinese National Intelligence Law of the People's Republic of China (adopted in 2017), where art. 7 provides that (unofficial translation) “[a]ny organization or citizen shall support, assist in and cooperate in national intelligence work in accordance with the law and keep confidential the national intelligence work that it or he knows.”<sup>7</sup>*

In Australia, it was concerned about the “risk that it would give Beijing the ability to shut power networks and other critical infrastructure that will soon rely on the technology”.<sup>8</sup>

### The security of Huawei's products and services

It was reported that “Huawei's 5G mobile phone networks could be hacked by Chinese spies to eavesdrop on sensitive phone calls, gain access to counter-terrorist operations – and potentially even kill targets by crashing driverless cars”.<sup>9</sup> Others said that the “equipment could be used for spying or destructive cyber attacks by China”.<sup>10</sup>

<sup>4</sup> One of the practical and evidential challenges in bringing a defamation claim would be to identify the makers of the allegations and to see if the allegations can be attributed to the US government. For example, sometimes the news reports only said something like “US politicians allege...”, but without really identifying who those politicians are. See, e.g., Rupert Neate, “Companies are seldom treated like this”: how Huawei fought back, *The Guardian* (19 April 2019) <<https://www.theguardian.com/technology/2019/apr/19/companies-are-seldom-treated-like-this-how-huawei-fought-back>> accessed 8 February 2020.

<sup>5</sup> Yuan Yang, ‘Huawei fights back against claims it is government-funded’ *Financial Times* (25 April 2019) <<https://www.ft.com/content/ebe8b0c6-6711-11e9-9adc-98bf1d35a056>> accessed 8 February 2020.

<sup>6</sup> Tobias Buck, ‘German regulator says Huawei can stay in 5G race’ *Financial Times* (14 April 2019) <<https://www.ft.com/content/a7f5eba4-5d02-11e9-9dde-7aedca0a081a>> accessed 8 February 2020.

<sup>7</sup> See ‘Translation of the National Intelligence Law of the People's Republic of China’ (Beida Fabao) (2018 Amendment) <<https://en.pkulaw.cn/display.aspx?cgid=313975&lib=law>> accessed 8 February 2020. The same translation of Art 7 has been used in official publications: see eg ‘Foreign Ministry Spokesperson Hua Chunying's Regular Press Conference on December 3, 2019’ (Ministry of Foreign Affairs of the People's Republic of China, 3 December 2019) <[https://www.fmprc.gov.cn/mfa\\_eng/xwfw\\_665399/s2510\\_665401/t1721187.shtml](https://www.fmprc.gov.cn/mfa_eng/xwfw_665399/s2510_665401/t1721187.shtml)> accessed 8 February 2020.

<sup>8</sup> Jamie Smyth, ‘Australia banned Huawei over risks to key infrastructure’ *Financial Times* (27 March 2019) <<https://www.ft.com/content/543621ce-504f-11e9-b401-8d9ef1626294>> accessed 8 February 2020.

<sup>9</sup> Neate (n 4).

<sup>10</sup> Smyth (n 8).

## HUAWEI'S response

Huawei once said that “[m]ost of what the US government says, as we all know, is not true”.<sup>11</sup> It is worthwhile to note the replies made by Huawei.

### Source of money and Chinese government's control

First, there is no government capital in Huawei.<sup>12</sup> Huawei's bonds are mostly in Hong Kong and overseas capital markets. Huawei claimed that it has not issued bonds in China. For their bank loans, the majority (of about 70%) is in overseas.<sup>13</sup>

Secondly, Huawei averred that it *has never* performed and also promised that it *will never* perform any spying for or handing over any customer data to the Chinese government. Importantly, the Chinese government has *never* made such a request to Huawei.<sup>14</sup>

### Quality, security and cyberattack

The risk of attack through compromising a 5G network “applies to all equipment vendors, not just Huawei”.<sup>15</sup> Furthermore, it has been suggested that technically, communications that pass through the equipment it supplies for telecoms network are typically encrypted, so it would not be able to read them even if they were intercepted.<sup>16</sup> Other commentators support this view. For example, Michael Howard (senior research director at IHS Markit for carrier networks) commented that the “biggest issue is that any and all equipment from any vendor can be compromised by any knowledgeable rogue person”.<sup>17</sup> Others said that it is “about basic engineering competence and cyber security hygiene that give rise to vulnerabilities”.<sup>18</sup>

## Are the allegations defamatory?

Once again, it must be stressed that it would be difficult for the ordinary public to examine the correctness of the allegations with certainty because the allegations concern complex technological and national security questions. This part will analyze how certain allegations can be framed as potentially defamatory, based on publicly available information.

### Certain allegations may be supportable

In terms of the quality of Huawei's products, it may be true that there is room for technological development and betterment. For example, it has been reported that a British report did find design flaws in Huawei's products, and is capable of being exploited.<sup>19</sup>

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<sup>11</sup> Yang (n 5).

<sup>12</sup> *ibid.*

<sup>13</sup> *ibid.*

<sup>14</sup> Arjun Kharpal, 'Huawei says it would never hand data to China's government. Experts say it wouldn't have a choice' *CNBC* (4 March 2019) <<https://www.cnbc.com/2019/03/05/huawei-would-have-to-give-data-to-china-government-if-asked-experts.html>> accessed 8 February 2020.

<sup>15</sup> Yuan Yang, 'What are the main security risks of using Huawei for 5G?' *Financial Times* (25 April 2019) <<https://www.ft.com/content/8b48f460-50af-11e9-9c76-bf4a0ce37d49>> accessed 8 February 2020.

<sup>16</sup> *ibid.*

<sup>17</sup> *ibid.*

<sup>18</sup> Smyth (n 8).

<sup>19</sup> Adam Satariano, 'Huawei Security 'Defects' Are Found by British Authorities' *The New York Times* (28 March 2019) <<https://www.nytimes.com/2019/03/28/technology/huawei-security-british-report.html>> accessed 8 February 2020.



## Certain allegations may not be supportable (and difficult to be proved)

Some allegations against Huawei are clearly direct or indirect criticisms of Huawei's business ethics. Legally, defamation by implication is a recognized ground of action.<sup>20</sup> For example, allegations, such as "Huawei's gear would open a backdoor for Chinese spies"<sup>21</sup> and Huawei will subsume to Chinese government's demand for spying, clearly implies two matters.

First, the allegations imply that Huawei *will* and *can* put national interest over client's interest. It would be evidentially difficult to prove and support this implication. Even if the law requires Huawei to do so, it does not mean Huawei *will* and *can* do so. Regarding Huawei's *willingness* and *tendency* to do so, there is simply not enough evidence. Huawei itself affirmed that it will not create any backdoor. Any allegations would then be unsupported suggestions of Huawei having low business ethics. Regarding Huawei's *capability* to spy, as suggested above, it has been doubted whether Huawei *can* realistically have access to and maintain control over encrypted data and products *after* they are sold to clients (i.e. a question of technology regarding whether it is technologically possible to do something to sold and encrypted products and services).<sup>22</sup> The allegations also illogically assume the purchasers of the Huawei's products would passively keep any natural design flaws open (assuming the flaws can be remedied and this point is talking about the potential flaws that have already been highlighted, such as those outlined in Section II, or those that can be uncovered with reasonable ease).

The second implication is that Huawei *will* betray its clients by exploiting the loopholes in the engineering functioning of its products. Again, this may be very difficult to prove by the US government, because even if there are flaws in the products out of quality reason, it does not necessarily mean Huawei *know* about the flaws and *will* and *can* exploit the flaws. It would be difficult to prove the intention and minds of a company.

Similarly, the allegations on Huawei's source of money are likely to be false when Huawei affirmatively denied it. It is noteworthy that the allegations are also implying the Chinese government *will* hack the 5G infrastructure through Huawei (which is out of the scope of this article, but surely is a relevant consideration).

## Will the allegations affect Huawei's business (losses resulting from the defamation)?

The impact of the allegations of the US government extends to all members of the Five Eyes.<sup>23</sup> For example, Australia, one of the Five Eyes members, follows the US entreaty to ban Huawei.<sup>24</sup> The allegations do have actual influence. It was reported that "Canada, the U.K. and New Zealand -- are deliberating what to do about Huawei", though the UK starts to have a looser stance towards Huawei and allows to compete for 5G contracts, such as England (but only for non-core technology<sup>25</sup>).

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<sup>20</sup> Canada: See, e.g., *Miller v. Squires & Pro-Dive Marine Services et al*, 2008 NLTD 25 [15]; *Laufer v. Bucklaschuk* [1999] 181 DLR (4th) 83 [26]; *Novus Entertainment Inc. v. Shaw Cablesystems Ltd.*, 2010 BCSC 1030 [45]. England and Wales: *McAlpine v Bercow* [2013] EWHC 1342 (QB) [48]-[49]; *Jones v Skelton* [1963] 1 WLR 1362, 1370. Australia: See, e.g., *Rush v Nationwide News Pty Ltd (No 7)* [2019] FCA 496 [94]; *O'Reilly v Edgar* [2019] QSC 24 [32].

<sup>21</sup> Stefan Nicola, 'Trump Blockade of Huawei Fizzles in European 5G Rollout' *Bloomberg* (19 March 2019) <<https://www.bloomberg.com/news/articles/2019-03-19/trump-blockade-of-huawei-fizzles-in-european-5g-rollout>> accessed 8 February 2020.

<sup>22</sup> Yang (n 15): "Huawei has responded that communications that pass through the equipment it supplies for telecoms network are typically encrypted, so it would not be able to read them even if they were intercepted."

<sup>23</sup> Josh Wingrove, 'Canada Puts Huawei 5G Decision on Back Burner With Allies Split' *Bloomberg* (8 May 2019) <<https://www.bloomberg.com/news/articles/2019-05-08/canada-puts-huawei-5g-decision-on-back-burner-with-allies-split>> accessed 8 February 2020.

<sup>24</sup> Smyth (n 8).

<sup>25</sup> Dan Sabbagh, 'May to ban Huawei from providing 'core' parts of UK 5G network' *The Guardian* (24 April 2019) <<https://www.theguardian.com/technology/2019/apr/24/may-to-ban-huawei-from-supplying-core-parts-of-uk-5g-network>> accessed 8 February 2020.

Outside the Five Eyes, the impact was lesser. For example, in March, it was reported that “not a single European country has banned Huawei”. Germany has even said it will allow Huawei to compete for contracts.<sup>26</sup>

However, logically and inevitably, the severe allegations from the US government would have some negative impact on the business image of Huawei all over the globe, especially when the allegations are widely reported everywhere. The impact would not be limited to Huawei’s business image in the eyes of the governments, but may also affect the sales of other services and products (e.g. phones) to the general public.

## Does Huawei have a legal recourse against the US?

In summary of the analysis below, it is possible to bring a defamation claim against the US government in Canada. It would be extremely difficult to lift the foreign state immunity in England and Wales (and this article offers insights on how Huawei could formulate its case in English courts). It is impossible to sue in Australia. Legally, the US government cannot be sued in the US, because it is protected by sovereign immunity.<sup>27</sup>

To be absolutely clear, one should not mix up (domestic) sovereign immunity with foreign state immunity. The former is about whether a government can be sued in its own jurisdiction; whereas the latter is about whether a foreign country can be sued in a different jurisdiction. For example, suing the US in the US would be the former; whereas suing the US in Canada would be the latter. It is also helpful to note that both sovereign and foreign state immunities extend to the government of a country.<sup>28</sup>

### Foreign State immunity

The biggest obstacle<sup>29</sup> would be the doctrine of foreign state immunity<sup>30</sup>, which provides that a foreign state cannot be sued.<sup>31</sup> However, state immunity is no longer absolute in most common law jurisdictions, and exceptions lifting the state immunity are applicable when (1) a country is acting in the commercial capacity<sup>32</sup>, or (2) injury or property damage<sup>33</sup> is involved.<sup>34</sup> Only the “commercial activity”

<sup>26</sup> Buck (n 6). The European Union has not imposed a blanket ban on Huawei. Instead, the EU issued guidelines to its members to take measures to deal with any potential security risk: Julia Horowitz, ‘Europe moves to secure 5G networks but won’t ban Huawei’ *CNN* (29 January 2020) <<https://edition.cnn.com/2020/01/29/tech/european-union-5g-huawei/index.html>> accessed 8 February 2020.

<sup>27</sup> In particular, 28 U.S.C § 2680(h) expressly carve out the waiver of sovereign immunity under 28 U.S.C § 2674 for libel and slander actions. Thus, the US government cannot be sued.

<sup>28</sup> For foreign state immunity, England and Wales: section 14 of the State Immunity Act 1978 expressly included government in the definition of “State”. Canada: State Immunity Act R.S.C., 1985, c. S-18, s 2. Australia: Foreign States Immunities Act 1985, s 3(3). For domestic sovereign immunity, see n 25.

<sup>29</sup> The doctrine of non-justifiability is not relevant (because it asks whether a political question, e.g., whether a part belongs to which country). The “act of state” doctrine concerns its validity, so it is also irrelevant.

<sup>30</sup> Canada: State Immunity Act, R.S.C., 1985, c. S-18. England and Wales: State Immunity Act 1978. Australia: Foreign States Immunities Act 1985.

<sup>31</sup> *Holland v Lampen-Wolfe* [2000] UKHL 40; [2000] 1 WLR 1573, 1583, where Lord Millett said it is “an established rule of customary international law that one state cannot be sued in the courts of another for acts performed *jure imperii*”.

<sup>32</sup> Canada: State Immunity Act, s 5 (“A foreign state is not immune from the jurisdiction of a court in any proceedings that relate to *any commercial activity* of the foreign state”). England and Wales: State Immunity Act 1978, s 3 (“A State is not immune as respects proceedings relating to a commercial transaction entered into by the State”. “Commercial transaction” includes “any other transaction or activity (whether of a commercial, industrial, financial, professional or other similar character) into which a State enters or in which it engages”). Australia: Foreign States Immunities Act 1985, s 11.

<sup>33</sup> See, e.g., Canada: State Immunity Act, s 6.

<sup>34</sup> *Bedessee Imports Ltd. v. Guyana Sugar Corporation, Inc.*, 2010 ONSC 3388; *Re Canada Labour Code*, [1992] 2 SCR 50. Both cases quoted Lord Wilberforce in *I Congreso del Partido* [1983] A.C. 244 (H.L.), who said:

Over time, however, as governments increasingly entered into the commercial arena, the doctrine of absolute immunity was viewed as an unfair shield for commercial traders operating under the umbrella of state ownership or control. The common law responded by developing a new theory of restrictive immunity. Under this approach, courts extended immunity only to acts *jure imperii* [public acts], and not to acts *jure gestionis* [private acts].

exception is relevant here, but not the latter.<sup>35</sup> It will be seen below that although the commercial activity exception is present in Canada, Australia and England and Wales, their exact scope is different.

Huawei could choose to sue in various jurisdictions (of course depending on the private international law rules<sup>36</sup>). The guiding principle for classifying whether an act is sovereign or commercial would typically ask:

*whether the defendant's conduct was properly characterized as jure imperii (sovereign or public conduct), in which case the immunity would apply, or jure gestionis (commercial or private conduct), in which case it would not.*<sup>37</sup>

“In order for the exception to apply, it is necessary to investigate the *fundamental nature* of the activities entered into by the foreign power.”<sup>38</sup> It requires “the court to consider the entire context and adopt a contextual approach and explained that [r]igid adherence to the nature of an act to the exclusion of purpose would render innumerable government activities *jure gestionis*.”<sup>39</sup> The test is more or less the same under English law.<sup>40</sup> It does not matter that often a state activity possess a hybrid nature, namely it is both public and commercial in nature.<sup>41</sup> The court would also consider the purpose of the activity.<sup>42</sup>

Thus, it would depend on whether the allegations were made in the sovereign capacity, or in a commercial capacity. Some of the allegations belong clearly to the former category (and hence subject to state immunity), because they involve issues on national security, privacy and spying.

However, other allegations, regarding the quality and security of Huawei's services and products, can be argued as being made in a commercial capacity. This is because, in terms of the context, there may be considerations regarding trade war, 5G technology competition and patent rivalry. From this perspective, the comments are made in the context of a commercial race, and they can be arguably analogized as something like ‘my 5G services and products are better, and customers should not use our competitors’ ones (i.e. Huawei) as they are not good enough or are faulty’. Therefore, it is more arguable that both the *nature* and *purpose* indicate that the allegations are commercial.

This argument is particularly reinforced by the British government's recent approach in framing the concern against Huawei as merely concerning the quality and security of its products (as opposed to any political concerns or any governmental attempt to spy).<sup>43</sup> Thus, it supports the argument that the allegations are about commercial quality, and are not about sovereign matters.

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See also Marek Martyniszyn, ‘Avoidance Techniques: State Related Defences in International Antitrust Cases’ (2011) CCP Working Paper No. 11-2 <<http://competitionpolicy.ac.uk/documents/8158338/8253131/CCP+Working+Paper+11-2.pdf/19c82b30-4fe0-458f-a901-a62e32d5d225>> accessed 8 February 2020.

<sup>35</sup> In Canada, it was held in *United States of America v. Freidland*, [1999] O.J. No. 4919, 46 O.R. (3d) 321, (C.A.) [24]-[25] that an action for defamation was not a proceeding that related to “any death or personal injury”.

<sup>36</sup> The legal rules determining the place of the tort of defamation are more or less the same in Canada, Australia and England and Wales. It is the place where the defamation is heard, read or downloaded that is relevant, but not the place where the defamation is “composed, posted on the Internet, or stored, or where the damage to the plaintiff's reputation occurred”. See Matthew Castel, ‘Jurisdiction and Choice of Law Issues in Multistate Defamation on the Internet’ (2013) 51(1) *Alberta Law Review* 153 at 155 (quoting authorities such as *Ecosociété Inc v Banro Corp*, 2012 SCC 18; [2012] 1 SCR 636 [34] and *Dow Jones & Co Inc v Gutnick*, [2002] HCA 56; 210 CLR 575 [25]-[27] as support).

<sup>37</sup> *United Mexican States v. British Columbia (Labour Relations Board)*, 2014 BCSC 54 (Canada).

<sup>38</sup> *Bedessee* (n 34).

<sup>39</sup> Original quotation marks omitted.

<sup>40</sup> *Holland* (n 31) 1577: Lord Hope held that “it is the nature of the act that determines whether it is to be characterized as *jure imperii* or *jure gestionis*. The process of characterization requires that the act must be considered in its context”.

<sup>41</sup> *Re Canada Labour Code* (n 34). *Holland* (n 31) 1580: Lord Clyde held that “[t]he line between sovereign and non-sovereign state activities may sometimes be clear, but in other cases may well be difficult to draw”. Lord Clyde further observed that “[i]n some cases, as was noticed in *United States v. Public Service Alliance of Canada* 94 I.L.R. 264 at 283, even when the relevant activity has been identified it may have a double aspect, being at once sovereign and commercial, so that it may then have to be determined precisely to which aspect the proceedings in question relate”. See also Edward Chukwuemeke Okeke, *Jurisdictional Immunities of States and International Organizations* (OUP 2018) 99.

<sup>42</sup> Canada: *Re Canada Labour Code* (n 34); *Homburg v Stichting Autoriteit Financiële Markten*, 2017 NSCA 62. England and Wales: *Congreso del Partido* [1983] A.C. 244, 267 (per Lord Wilberforce). However, note that the US law does not allow the purpose to be taken into account (and the focus has to be on the nature). See Foreign Sovereign Immunities Act 1976 (US), s 1603(d): “The commercial character of an activity shall be determined by reference to the nature of the course of conduct or particular transaction or act, rather than by reference to its purpose”. See also *Texas Trading & Mill. Corp. v. Federal Republic of Nigeria*, 647 F.2d 300 (1981).

<sup>43</sup> *Satariano* (n 19).

Besides, the allegations regarding the willingness and tendency to spy for the Chinese government can be argued as commercial. Whilst they surely can be argued as about national security (and hence subject to state immunity), however, equally, they can be argued as unsupported criticisms of Huawei's business ethics. See the discussion at Part IV (B) above. By analogy to the Canadian case of *Bedessee Imports* (which will be discussed below), the US allegations can be seen as intentionally undermining the competitiveness of Huawei for commercial reasons.

## **The exact scope of “commercial activity”: Canada, England and Wales and Australia**

To lift the state immunity, it is not enough for the allegations to be commercial in nature. It is still necessary to see if the allegations fit within the scope of “commercial activity” as defined by the statutes of various jurisdictions.

In Canada, the statute provides for a broad exception covering “any commercial activity”.<sup>44</sup> Thus, there is more scope for Huawei to frame its claim in Canada. A case law will be discussed below to reinforce the feasibility of suing the US government in Canada.

By contrast, in England and Wales, the exception for lifting state immunity will only apply if there is a “commercial transaction” with the US government. There is no contractual arrangement between Huawei and the US government that is related to the allegations.

Even though the definition of “commercial transaction” under English law extends to commercial “activity” engaged by the US government, this exception is still unlikely to be applicable. Lord Millett (in obiter) took a restrictive reading of the term “activity” under s.3(3)(c) State Immunity Act 1978. He commented that for there to be a “commercial activity”, there must be “a commercial relationship akin to but falling short of contract (perhaps because gratuitous) rather than a unilateral tortious act”.<sup>45</sup> If there must be a “relationship” akin to a contract, it would be difficult for Huawei to formulate a claim, when there is nothing contractual or quasi-contractual with the US government.

It is noteworthy that Lord Millett's obiter is the only available guidance on s.3(3)(c), and thus it is unknown if a broader interpretation of s.3(3)(c) is possible. If Huawei insists on suing in English courts, it may try to argue that Lord Millett's interpretation is too restrictive. Instead, the US government has “engaged” in “commercial activity” through downplaying the quality of the Huawei's products (and securing commercial and competitive advantage for companies from other countries). However, two English cases will be explored below and it can be seen that English courts maintain a very restrictive stance against the commercial exception in defamation cases.

State immunity cannot be lifted in Australia, as the exception was expressly and clearly restrictive. Section 11 of the Foreign States Immunities Act 1985 provides only for a “commercial *transaction*” exception (as opposed to the Canadian broad “activity”-based exception). Although “commercial transaction” is defined to include “like activity” under s.11(3), it is similar to (and arguably even stricter than) the position in English law.

## **Has there been incidents that common law courts allow defamation actions?**

There were litigations at various common law courts on defamation actions against state. The results are mixed. Some held that state immunity was inapplicable; some did not.

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<sup>44</sup> State Immunity Act (Can.), s 5.

<sup>45</sup> *Holland* (n 31) 1587. See also Hazel Fox and Philippa Webb, *The Law of State Immunity* (3rd edn, OUP 2013) 194; Martin Dixon, *Textbook on International Law* (7th edn, OUP 2013) 199.

### The case law in Canada

In the Canadian case of *Bedessee Imports Ltd. v. Guyana Sugar Corporation, Inc.*, the government of Guyana made statements that promoted the interests of its wholly-owned state company Guysuco.<sup>46</sup> It was held that the “statements promoted Guyana’s ‘brand’ and disparaged the brand of a competitor. To permit a lawsuit by Bedessee in relation to such activity is neither an affront to the dignity of the Guyanese state nor an interference with its sovereign functions”. “The statements were directed at activities undertaken by a commercial competitor and had to do with the protection of Guysuco’s brand – a plainly commercial activity”.<sup>47</sup>

Whilst certainly this case has distinguishing features from our present analysis, the key is that in *Bedessee*, it was seen that disparaging the brand of a competitor is capable of amounting to a commercial activity of the state. Thus, by analogy, it can be argued that the US government is making the statements against Huawei for disparaging its commercial competitiveness.

### The case law in England and Wales

For Huawei to lift the state immunity in English courts, it has two considerable hurdles. First, it has to argue against Lord Millett’s restrictive interpretation of “commercial activities” under s.3(3)(c) (which would be very difficult as already discussed above). Secondly, even if it passes the first hurdle, it would still face considerable difficulty in establishing that the US allegations are not sovereign but commercial in nature, when the English courts are demonstrably restrictive.

In *Holland v. Lampen-Wolfe*, the claimant-professor provided education to the US military.<sup>48</sup> The government employee (the defendant) was from the US Department of Defense and he sent memorandum headed “Unacceptable Instructor Performance” to the claimant’s home university complaining about the claimant’s quality of teaching. The claimant sued for defamation. It was held that “the standard of education which the United States affords its own servicemen and their families is as much a matter within its own sovereign authority as is the standard of medical care which it affords them.” Therefore, state immunity was applicable.

The lesson from *Holland* is that just because an allegation is about *quality* of service, it does not mean the English courts will see it as *jure gestionis* (commercial or private conduct). In the words of the English court:

*At first sight, the writing of a memorandum by a civilian educational services officer in relation to an educational programme provided by civilian staff employed by a university seems far removed from the kind of act that would ordinarily be characterised as something done iure imperii. But regard must be had to the place where the programme was being provided and to the persons by whom it was being provided and who it was designed to benefit - where did it happen and whom did it involve?*<sup>49</sup>

Huawei can try to distinguish its case from *Holland*. The English court was heavily influenced by the fact it concerned the US military. But for the involvement of the military, the English court may have reached the opposite decision. Therefore, Huawei could argue for two distinctions. First, Huawei’s action did not concern the military. Secondly, Huawei’s 5G services and products presumably would not be specifically serving the government departments only, but would also serve the general public (so it would be more commercial and less sovereign in nature).

Nevertheless, in another English case *Grovit v De Nederlandsche Bank & Ors*, the claimant sued the Dutch Central Bank and its officers for defamation.<sup>50</sup> The claimants applied to the Bank for registration

<sup>46</sup> *Bedessee* (n 34). Application for leave to appeal to the Supreme Court of Canada denied: 2011 CanLII 20808 (SCC).

<sup>47</sup> *Bedessee* (n 34) [57] (not disputed on appeal).

<sup>48</sup> *Holland* (n 31).

<sup>49</sup> *ibid* 1577 (Lord Hope).

<sup>50</sup> [2007] EWCA Civ 953.

in the Netherlands. The registration was refused and the letter “included assertions that the directors and executives [related to the claimant] were untrustworthy in a number of respects”.<sup>51</sup> It was held that state immunity applied, because the defendants “were performing the role of an administrative authority carrying out governmental supervisory functions which had been delegated to the Bank by the Dutch Government to protect the integrity of the financial system in the Netherlands”.<sup>52</sup> “The fact that incidentally the letter contained libelous material did not deprive it of its essentially public law character.”<sup>53</sup>

*Grovit* is a demonstration that when the defamation is only an incident part of a sovereign public act, state immunity is applicable. However, *Grovit* can be distinguished from our Huawei situation. This is because in *Grovit*, the defamation and the sovereign act of supervising the banking system are inseparable (the defamation arose out of the process of screening registration applications); whereas in our Huawei situation, the allegations against Huawei were made separately. Some were about national security; but some were separately about the quality of Huawei’s services and products.

## Suing in China?

It is interesting and helpful to consider the position on foreign immunity in China. In China, there is not a specific state immunity law. However, the Chinese government is in support of *absolute* immunity (i.e. with no exceptions at all).<sup>54</sup> In *Democratic Republic of Congo v FG Hemisphere Associates LLC*, Congo was sued in Hong Kong and the Office of the Commissioner of the Ministry of Foreign Affairs of China in Hong Kong (hereinafter OCMFA) reiterated the approach taken by China.<sup>55</sup> OCMFA said:

*The consistent and principled position of China is that a state and its property shall, in foreign courts, enjoy absolute immunity, including absolute immunity from jurisdiction and from execution, and has never applied the so-called principle or theory of ‘restrictive immunity’. The courts in China have no jurisdiction over, nor in practice have they ever entertained, any case in which a foreign state or government is sued as a defendant or any claim involving the property of any foreign state or government, irrespective of the nature or purpose of the relevant act of the foreign state or government and also irrespective of the nature, purpose or use of the relevant property of the foreign state or government. At the same time, China has never accepted any foreign courts having jurisdiction over cases in which the State or Government of China is sued as a defendant, or over cases involving the property of the State or Government of China. This principled position held by the Government of China is unequivocal and consistent.*<sup>56</sup>

OCMFA further added that despite China is a signatory to the non-binding *United Nations Convention on Jurisdictional Immunities of States and Their Property* (which supports restrictive immunity), “the position of China in maintaining absolute immunity has not been changed, and has never applied or recognized the so-called principle or theory of ‘restrictive immunity’”.<sup>57</sup>

Thus, Huawei cannot sue the US government in China (though it may not be serve any useful purpose to sue in China when the aim of a defamation action is to protect the reputation of Huawei overseas).

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<sup>51</sup> *ibid* [4]-[5].

<sup>52</sup> *ibid* [16].

<sup>53</sup> *ibid* [17].

<sup>54</sup> See, e.g., JS Mo, ‘Issues of Sovereign Immunity in the Australia-China Trade and Investment’ (1991) 7 QUT Law Review 57, 59-61; Dahai Qi, ‘State Immunity, China and Its Shifting Position’ (2008) 7(2) Chinese Journal of International Law 307. See also *Jackson v China*, 794 F.2d 1490, 1494 (11th Cir. 1986).

<sup>55</sup> [2011] HKCFA 42; (2011) 14 HKCFAR 95; [2011] 4 HKC 151.

<sup>56</sup> *ibid* [44].

<sup>57</sup> *ibid* [45]-[46].

## Conclusion

It is interesting to note that different countries have different scope of foreign state immunity law. It has been concluded that it is possible to sue the US government for defamation in Canada, but a claim is very likely to be defeated by foreign state immunity in England and Wales. It is also impossible to sue in Australia, China and the US. Thus, despite the allegations having worldwide impact; Huawei has limited legal protection and recourse.

Thus, the commercial implication is that a government from any country can make allegations to undermine the commercial competitiveness from competing countries, whilst it may not have any legal consequence. Thus, foreign state immunity could be used as a strategic tool for competition purposes.

**Martin Kwan**

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