

# Bulletin

## A word from the Chairman

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One of the prime objectives of the BSLA was to encourage a truly bilateral relationship with active participation from lawyers working in both countries. So I am happy to report that significant progress has been made towards the creation of a sister association in Spain. In April we had a meeting in Madrid with the president of the Spanish Law Societies Council, Mr. Carlos Carnicer. I was impressed by the degree of interest and enthusiasm shown for the project at the highest level.

As there is no single law association which covers all of Spain, we have been in contact with a large number of regional associations and we are in the process of setting up a meeting with their presidents, or "decanos" as they are known in Spain. Our aim is to look at ways of encouraging membership in their areas. We hope that our efforts will

soon bear fruit and that the Spanish membership may, before long, look as healthy as the British-based membership.



This second issue of the Bulletin includes articles ranging from taxation to personal injury and company law. I would like to thank the contributors and to encourage other members to send in brief articles or notes on matters of interest to our readers. We want the

widest possible range of material, the particular and the general, discussion of points of law and accounts of your own experiences working at the interface between the two legal systems. We want the Bulletin to become a real forum for discussion of Spanish and British legal matters.

This Bulletin also contains details of the Foreign Exchange Programme set up with the Madrid Law Society.

Plans are well advanced for the Annual General Meeting, to coincide with the opening of the Legal Year in England at the beginning of October.

At the back of this Bulletin you will find the form for our next event, a reception bringing together all the bilateral associations set up by the Law Society, with up to 300 lawyers from more than 35 countries from Brazil to China. The event will take place on Tuesday 25 June 2002 in the magnificent grounds of the Honourable Society of the Inner Temple. Places are limited so please book as soon as possible.

Alberto Pérez Cedillo  
Fernando Scornik Gerstein  
Spanish Lawyers

Below: The grounds of the Inner Temple



# Chasing Shadows

## Mark Biddlecombe describes the tax obligations of shadow directors



The decision of the House of Lords, in *R v. Allen* [2001] UKHL 45 is likely to have a significant impact on individuals who own an asset through a company. This article looks at the decision and considers the impact it may have, particularly in the light of *DTI v. Deverell* (2000) 2 All ER 365.

### Shadow directors

Mr Allen's circumstances could be regarded as being somewhat extreme – there was no doubt in the Court's mind that he was a "shadow director". The question before the Court was whether a shadow director was liable to tax under Schedule E of the Taxes Act 1988.

This has been debated for some time. The Revenue position is that the statutory definition specifically includes a shadow director so he is taxed in the same way. Tax advisers argue that tax under Schedule E only arises in relation to duties performed by an individual holding an office or employment – a shadow director holds no such office. Further, there is no territorial limit in the relevant provisions, meaning that shadow directors could be taxed anywhere regardless of their residence or where their duties are performed.

All of these arguments were made to the House of Lords who decided in the Revenue's favour. A shadow director is to be taxed on accommodation and benefits in kind in the same way as an actual director. The territorial limit argument was dismissed on the grounds that such limits are included in the three heads of charge under Schedule E to which the statute refers.

It might be thought that Allen's involvement in the management of his companies was so extreme as to make this case merely academic for the well advised client. Unfortunately, the case applies to anyone who is a shadow director. And that is now of far greater concern than before, because of *DTI v. Deverell*.

### DTI v. Deverell (2000) 2 All ER 365

So what does *Deverell* tell us about shadow directors? Having completed an extensive review of the case law, the Court of Appeal applied a wider test than had previously been the case. A shadow director was held to include anyone who exercised real influence on the affairs of a company. The label attached to communications between an individual and the directors was less important than the effect of such communications on the actions the directors took. Where an individual gives guidance to the directors, and the directors are accustomed to act in accordance with such guidance, then this may well be enough to satisfy the shadow director test.

And if this wider definition works for the purposes of disqualification of a director, then it may well work for tax

purposes as well. In fact, in Allen's appeal, his counsel cited the decision in *Deverell* as a reason for the Court not to apply Schedule E tax to shadow directors. But the Court was unsympathetic. Just as in *Deverell*, the Court decided that if an individual exerts influence on a company's affairs in the same way as an actual director, then he must accept the fiscal consequences that go with the job.

### Practical implications

Let's consider how these cases might effect two different individuals. Mr A is domiciled and resident in Spain, but wants to acquire UK property for his own use when visiting the UK. Mr B is resident and domiciled in the United Kingdom, and wants to buy a Spanish holiday home.

To avoid UK inheritance tax, Mr A buys the UK property through a Jersey company, the shares of which he settles into a trust. The directors of the company – perhaps at the direction of the Trustees of the trust – then allow Mr A to occupy the property rent-free.

In the past, it might have been thought that this arrangement could cause no harm. Mr A would be strictly advised not to meddle in the management of the company and to limit his influence to giving "advice" or "suggestions".

But if, as is likely, the Directors are inclined to act in accordance with such "advice" or "suggestions", then, *prima facie*, *Deverell* applies to treat him as a shadow director. *R v. Allen* then applies to tax him on the benefit he receives, to the extent that he performs "duties" in the UK. Should Mr A become resident in the UK, the possibility of a charge becomes more likely. And if he becomes UK domiciled as well, then it doesn't matter where the "duties" are performed, Schedule E will tax the benefit in full.

In Mr B's case, again the avoidance of foreign death duties may prompt him to acquire the property through a company. But if he is a shadow director as defined in *Deverell*, then the benefit of the property will be taxable under Schedule E, regardless of where any "duties" are performed. Even if Mr B is UK resident but *not* UK domiciled, he could still be taxed to the extent that he can be said to perform "duties" wholly or partly in the UK in relation to the property.

### Conclusion

*Allen* and *Deverell* make it harder to enjoy property held through a company without fiscal consequences. Although both cases actually involved quite extreme facts, the decisions are of general application. There are still practical and fiscal advantages to the use of companies in such situations, but it is necessary to proceed with caution.

Mark Biddlecombe – Rooks Rider

# Implications of Allen and Dimsey for offshore property holding companies in Spain

Following the release on 11 October 2001 of the House of Lords judgements in R v Allen and R v Dimsey, there have been several articles outlining the implications that the case may have when a company is being used to hold the UK home of a director. In our practice we find that to avoid a potential CGT or IHT charge, individuals tend to structure Spanish property acquisitions using offshore schemes.

What are the implications for the UK individual using an offshore property holding company?

Owning Spanish property using offshore schemes has proved to be an excellent UK tax planning idea from the point of view of Inheritance and Capital Gains Tax. However if the client is not thinking of "dying" or transferring the property, the long term consequences of owning property with an offshore company is not an efficient Income Tax planning tool.

The Allen principle would enable a UK Income Tax charge to arise on the domiciled individual using the property located in Spain. The individual behind the company is treated as a shadow director within the meaning of section 168(8), ICTA 1988. Therefore an

employee, chargeable to tax on any benefits provided by the company, i.e. the provision of living accommodation (section 146, ICTA 1988).

The Spanish practitioner will be familiar with the consequences under Spanish non-resident income tax rules. First the offshore company will be taxed in Spain from a Corporate Tax point of view according to a notional income, based on its value. Secondly, the individual using the house may be caught under the non-resident regime by receiving a benefit when using the property in Spain.

It is currently unclear if the Inland Revenue will actively take steps to target such arrangements, however it would be prudent to start thinking on these lines if you deal with clients of this sort.

This is my particular opinion of the case and does not represent my firm's position on this matter. I should be very keen to discuss any particulars with you and should appreciate your views. My phone number is 02380 354 276, e-mail: ldelcanto@deloitte.co.uk

Leon F Del Canto – Deloitte & Touche

## Foreign Exchange Programme

The Madrid Bar Association would like to inform you about our foreign exchange programme for lawyers. Throughout the Exchange Programme for Lawyers, the Madrid Bar Association has aspired to provide lawyers with a training period in legal material in law firms abroad, in collaboration with Bar Associations located around the world, particularly European ones. The Madrid Bar Association regards the educational needs of its members in such a constantly growing field as international law and encourages contacts between Spanish professionals and foreign colleagues.

Lawyers attending the programme will enjoy a minimum of four months training period which will provide a first contact with the professional life in

other countries, with its implications from a human, and professional point of view.

Collaborating firms employ lawyers as trainees who should observe any applicable organisational rules.

Our institution would like to invite to members of the British-Spanish Law Association to participate in this training program and to receive training lawyers from our Bar Association. We consider that this experience would be enriching for all the participants (lawyers and law firms).

Requirements for participating in the schedule of the Madrid Bar Association are the following: to be a practising lawyer and to possess a good knowledge of languages. Participants should attend a personal interview.

Further details:

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# Spanish Holding Companies

## Armando Tomás Vidal explains their advantages as shared service centres ...



The Spanish holding company (*Entidad de Tenencia de Valores Extranjeros – ETVE*) has become a competitive vehicle in canalising foreign investments.

The participation exemption exists both for dividends coming from subsidiaries and capital gains arising from the sale of participating affiliates.

Spain has introduced the Parent-Subsidiary Directive but reduced the degree of participation from 25%, as established in the Directive, to a minimum of 5% (direct or indirect) participation or a minimum investment of six million Euro, irrespective of the existing participation.

On the other hand, the participation exemption is applicable not only to dividends or capital gains deriving from subsidiaries in EU countries, but to any country not considered as a tax haven in Spanish domestic legislation.

The substantial advantage of Spain is that there are no specific rules restricting deduction of corporate expenses which may be classed as wholly or partially relating to the management of foreign investments. Among those deductible expenses it is possible to include interest from loans to the ETVE in order to finance its investments.

Some previous pitfalls, effecting the Spanish ETVE, have already been amended. Currently, it is possible for a Spanish ETVE to carry out not only holding activities and management services, but any kind of service or commercial activity.

This opens the door to new opportunities being possible for a ETVE to work as a shared service centre for the rest of the companies belonging to the same group or for a determined geographic area.

Income for the services rendered to related parties is liable to normal taxation (CIT=35%) and has to be priced following the arm's-length principle. However, the expenses

incurred, including interest from loans and expenses related to the management, acquisition and disposal of participations, can match the income obtained working as a shared service centre and/or rendering management services.

In Spain there are thin capitalisation rules (*ratio de endeudamiento*), being the debt equity ratio 3/1. However, it is possible to increase this ratio based on an APA, consisting of an advanced agreement with the Spanish Tax Administration.

Moreover, that kind of services as a "shared service centre" give more substance to the Spanish holding. It facilitates the proof of existing material and human resources involved in the holding activities and the possibility of deducting input VAT. A company, which had no other activities, would not be eligible for VAT registration and would not be able to recover any of the tax it incurred on purchases.

The normal services as shared service centre, besides a management service, consist of accountancy, accounts payable, invoicing on behalf of third parties, treasury control, etc.

The possibility of using the Spanish holding as a shared service centre makes it more attractive and offers new alternatives to existing vehicles currently included in the list of harmful tax practices (co-ordination centres in Belgium, cost-plus regimes in the Netherlands etc.) and with an uncertain future.

■ Armando Tomás Vidal is a Partner of Pedro Brosa & Asociados and Director of the International Tax Planning Department.

## ... Jose Carlos Narbona looks at some of the other opportunities they present



Spain has one of the EU's best holding's regimes, allowing very favourable tax treatment of capital gains and dividends received from its subsidiaries. This regime is secure, stable, and has a very positive treatment by the Spanish tax authorities in order to encourage its use and development.

As a result, the Spanish holding company is a popular vehicle for investment in Latin America. On one hand, is not subject to taxation in Spain – nor any withholding of dividends – if the parent of the holding is a foreign company (provided it is not a tax haven as listed by the Spanish tax authorities) and the following conditions are met.

■ The shareholding has to be at least 5% of the subsidiary's capital or, at least, is of six million euros.

■ The minimum period of holding in the subsidiary, it had to be of at least one year (any twelve month period qualified). The new regulation states that provided such participation is kept for one year, it would also comply with this requirement.

■ Formal notification to the Spanish tax authorities is required upon incorporation or acquisition of the company.

Jose Carlos Narbona – Levy Gee, Spain

# Looking for Quality

## Nielson Sanchez Stewart's firm recently applied for a Quality Mark



During 2001, my firm went through a very interesting process: obtaining a Quality Mark. It all came, in fact, from reading the *Law Society Gazette* (9805, 1 February 2001).

I found that it was really a challenge to have the quality standards of our small firm, which has been now operating for over twenty years, by a complete stranger.

We were convinced *prima facie*, that the quality of our services was not bad, but we were put in a difficult position when we had to answer to our quality advisor the simple question: Why we were so sure?

I gathered that it was because we had kept most of our clients for a very long time and that they were paying their bills promptly and generally without complaint. However, that was not enough. It was possible that our clients remained with us for other reasons such as their patience, or perhaps because we were less expensive than other firms.

The whole process took us approximately six months and a very good number of hours, especially from the partner in charge, Lorenzo Sanchez-Stewart.

At the end of the performance, it was quite a success, not only for the result – we obtained the quality mark – but also because we had to put in writing everything that we did in the office, from buying pencils to giving legal advice, from the punctuality of appointments to the cleaning and ventilation of the waiting room, from the neatness of the desks to promptness in answering letters.

Fortunately, we were not obliged to change anything, simply to record our methods and we were then ready to pass the examination. Bureau Veritas Quality International, a

reputable firm of auditors, was kind enough to go through all our standards and give us the official documentation that certifies that the quality management system of our firm has been assessed and found to be in accordance with the requirement of the quality standards of ISO 9000:2000 in legal assistance and advice in court and out of court matters.

We are proud of having obtained this goal but, besides that, we are happy to have undertaken this rather time consuming exercise.

It is a landmark that you have, specially when there is an expansion in the firm or an amalgamation or when someone new comes into it. The newcomer knows how he should work, what he should expect and what it is required from him.

We are told that more and more firms of solicitors are going through this process in England, whilst in Spain the experience is very new. We are only aware of three other Spanish firms that have gone through the process and our firm is the only one that has gone through it according to the new norm.

I would encourage all members to go through it and shall be pleased to provide any further information, if this is required, by e.mail: [abogados@sanchez-stewart.com](mailto:abogados@sanchez-stewart.com).

■ Nielson Sanchez Stewart is a partner of Sanchez Stewart Abogados

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## Skirting the Issue

SPAIN's national train company RENFE, demanded that hostesses on their high-speed trains wear skirts "at least" two centimetres above the knee and prohibited them from wearing trousers.

### España in the works

Trade union prudes successfully challenged the regulations in a Barcelona court, which gave the miniskirt rule short shrift. But the action hit the buffers when the Spanish Supreme Court allowed RENFE's appeal and upheld the skirts, so to speak.

According to the Court, the over the knee rule was not below the belt, nor was it "sexist" or "discriminatory". It was a reasonable obligation imposed by a company seeking to project a "high quality brand".

### Spanish thighs

How reassuring, in these PC times, to see the Spanish

legal system protecting the inalienable right of red-blooded *hombres* to a glimpse of thigh while ordering their *cerveza* and *tapas*. Or, should we say, a peek of *patella* while picking their *paella*?

Such a result would be less likely in the UK where, as we know, women wear the trousers. Last year a tribunal upheld Judy Owen's discrimination complaint against the Professional Golf Association for refusing to allow her to wear a "smart trouser suit" to work.

### Be casual but smart

Attitudes to workplace attire are changing and "dress down" policies becoming more commonplace. But employers need to establish proper ground rules that don't apply different standards to men and women unless there is a sound business justification.

Send staff clear signals on what they can wear and you won't go off the rails.

Tony Lorenzo – Lewis Silkin

# Rail Privatisation: The British Experience



## José Antonio Magdalena Anda identifies the pitfalls the Spanish must try to avoid

Growing concern over the events involving the British railway system over the past few months may lead to a complete loss of confidence in the privatisation policies of certain public utilities.

As readers will recall, in October 2001, Railtrack – the company running the UK's railway infrastructure, in private hands since 1996 – was put into administration at the request of the Labour government. In the words of Transport Minister Stephen Byers, it was impossible to continue handing the company "a blank cheque" in light of its disastrous financial situation and the deterioration of the public service.

Before making hasty value judgements, let us see the characteristics of this particular case.

Over the fifty years preceding privatisation, the British railway had been run by a chronically loss-making public enterprise – as were its continental counterparts – and a reform was truly needed. That reform was made possible thanks to Council Directive 91/440/EEC, even though the Directive only encouraged a liberalisation of the industry without imposing specific policies.

In 1993 the then Conservative government embarked on a full reorganisation of the railway. On the one hand, two public bodies were created to regulate rail transport and the granting of franchises and, on the other, the provision of transport by rail services throughout the country was handed over to private companies. The running of the railway infrastructure was entrusted to Railtrack, a company created *ad hoc*, which initially remained within the public sector but became wholly owned by private capital in 1996 when it was listed, attracting a large number of investors.

However, the results, both financial and in terms of customer satisfaction, were not as expected. Not only did customer complaints rise by 100 per cent, but the British government itself admitted that the service had got worse.

This led to a reform of the railways in 1999, only six years after privatisation, a true record by all accounts. The reform consisted of the creation of a new public body with wide powers in the transport industry: the Strategic Rail Authority.

However, that reform was not sufficient. Poor business management coupled with several accidents in which dozens of people were killed – which were linked to an inadequate investment policy on safety and maintenance – caused a redefinition of the investment plans and a further worsening of Railtrack's financial situation (more

money was needed to accomplish the reforms required to improve safety and the quality of the service).

It is here that the essential failure of the system can be found: in spite of the fact that Railtrack was 100 per cent privately owned and had to operate by the rules of the market, approximately two thirds of its income came directly from the public sector. Based on such a ratio we cannot speak strictly of a true privatisation. That never happened, but instead a strange set-up, whereby public funds were handed over to the private sector through a company whose main concern was to keep its shareholders happy but which had no actual economic, financial and administrative autonomy.

This situation reached breaking point in October of last year when, faced with a new multi-million request for public funding, the Transport Minister decided to put the company into administration and announced its replacement by a new company without shareholders and unable to trade on the Stock Exchange.

Leaving aside the fury of the shareholders, who see their investment under serious threat, a fiasco of such magnitude has undermined the private sector's confidence in any investment in large public works or services proposed by the public sector.

The new railway policy has even been described as a disguised re-nationalisation in so far as a privatised enterprise is being returned to the public sector. However, as mentioned above, something which actually never ceased to be directly dependent on the State cannot be re-nationalised. The problem lies somewhere else, i.e. in not understanding that, if it is sought to introduce the private sector into certain economic sectors (described as natural monopolies), a very rigorous and effective system of business control, compatible with realistic expectations of a profit in the medium- to long-term, should be put in place. Otherwise what emerges is the worst of both the public and the private systems.

The British experience should serve as an example to other countries, in particular to Spain, where an imminent liberalisation of the railways has been announced. Everything suggests that, unlike Britain, Spain will proceed gradually and the infrastructure will be kept in the public sector (as is traditional in our legal-administrative system).

The liberalisation of freight and passenger rail transport may be beneficial, but in order to ensure

Continued on following page

# Restructuring Spanish Companies

Angela Toro examines the changes as they relate to labour relations



The restructuring of companies has undergone important changes during the last few years, as a result of their present concept. First of all, companies have stopped being local and now have a national or multinational nature. Market needs have forced companies to establish their businesses so that they can face operations on a large scale, a distinctive trait of the global market.

The impact of the new company on restructurings effects both the focus of the decision and the reasons on which it is based. The focus of decision-making is no longer in the work centre, near to the group of effected workers. On the other hand, the decisions are not based on limit situations that take the company to irremediably make an inevitable decision. At present, the losses imply a negative change in the situation of the company in such a way that, for example, the reduction of the shares in the stock market in the United States can take to a reduction in a work-force in Spain.

On the other hand, from a workers' point of view, the degree of union affiliation has fallen, possibly because of the speed at which the companies have changed. The traditional unionisation seems surpassed and nowadays the needs of the represented are diverse.

The employer-worker relationship has also changed. There is no longer a patron relationship and the culture of human resources has put the workers in a main role in the company management. The social culture is more and more individualistic. As opposed to the collective movements years ago, at the present time it is difficult to find cohesive groups, probably because labour conditions have improved and the fight for "minimum conditions" has been replaced by one for an improvement of the conditions of work.

In the past, the workers' representatives' position was more radical in collective redundancy cases. The situation of the company was also more complicated since the decision to reduce personnel was adopted before an irreversible situation. Things could even end in a violent confrontation. In these circumstances, the task of the Labour Administration as a mediator or as a decision-making device had a much more relevant role.

Nowadays, the procedure has been reasonably moderated. The fact that, in many cases, the external decisions are taken by the parent company, with various limitations at the time of making decisions, means that more agreements are reached in shorter periods of time.

In these situations, an effort is made to return to normality as quickly as possible and to continue thinking about the business. This is clear on many occasions from the difficulties that arise when formalising a collective dismissal file with economic documentation, when this information must be found externally, implying a greater investment of time, not only for the management of the company in Spain, but also for its English, French or American colleagues.

The consequences are well-known by the two parties where, on counted occasions and only in very clear situations, the Labour Authority has decided to authorise the termination of the labour relationships. The files conclude with agreements in which it is assumed that the compensation barriers established by law are going to be exceeded. The conclusion is that the parties follow the tendency to solve their differences out of the intervention of third parties.

Angela Toro – Baker & Mackenzie

## Rail Privatisation

Continued from previous page

success the role of the existing public enterprises should be redefined, or new ones should be created to take care of overseeing the sector and access to the infrastructures.

In conclusion, a small piece of advice: stay away from multiple regulators, which only lead to confusion, a slovenly service and unnecessary bureaucracy. If we want liberalisation, let us act accordingly, let us learn

from other people's mistakes and lay down a clear, effective and efficient system, with a clear separation between what is public and what is private.

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# Foreign Accidents: Recent Developments

Four recent cases show that the courts are busy deciding foreign accident claims, two cases concerning holiday accidents (in Spain!), and two concerning jurisdiction.

## Holiday Claims

*Codd v. Thomson Tour Operators Limited* (CA, 7th July 2000) concerned a claim against the tour operator where it was accepted that the Defendant would be liable if it were found that the persons responsible for running and managing a hotel in Majorca were negligent. The accident concerned a 10 year old boy trapping his fingers in a lift door. What standard should be applied to assess breach of duty? Held: (not surprisingly) Spanish.

*Edmunds v. Simmonds*, (High Court, 4th October 2000) concerned a road traffic accident in Spain where the driver and the injured passenger were both English, the car was a locally hired vehicle, with Spanish insurance. Garland J. applied the Private International Law (Miscellaneous Provisions) Act 1995 to determine what law was applicable. His Lordship held that the applicable law for the assessment of damages should be English law, by either of two routes: that the assessment of damages is procedural and a matter for the law of the forum, or that Spanish law should be displaced under Section 12 of the Act.

## Jurisdiction

*Lubbe v. Cape plc* [1 WLR 1545 concerned a multi-party action against an English domiciled company by South African domiciled Claimants concerning failures in relation to the operation and running of a South African subsidiary company mining and processing asbestos. The Defendant was sued as of right but argued that South Africa was the more appropriate place for the proceedings. The Claimants argued successfully that the complexity of the legal issues and of the expert evidence, in conjunction with the lack of means of the Claimants, meant that substantial justice would not be achieved in South Africa and that a stay on proceedings should be refused.

In *Lubbe*, the Defendant argued that the ordinary conflicts of law principles of the appropriate forum were applicable (*forum non conveniens*).

Lord Bingham considered that the question of whether the Brussels Convention applied to prevent English Defendants arguing that a foreign court was a more appropriate venue was suitable for a reference to the European Court of Justice (had a reference been necessary, which it was not). A European case, *Universal General Insurance Co. v. Group Josi Reinsurance Co. SA*, (Case C-412/98) [2000] 3 WLR 1625, suggests that English courts, no matter where the accident or injury had taken place. This is now the subject of an appeal to the Court of Appeal in *Owusu v. Jackson and others*, to be heard in May

Philip Mead – Chambers of John Hendy QC

## BILATERAL ASSOCIATIONS' SUMMER RECEPTION

I would like to attend the Bilateral Associations' Summer Reception on 25 June 2002 at 7.30 for 8.00pm at the Honourable Society of the Inner Temple, London EC4Y 7HL

Name ..... Telephone .....

Bilateral ..... Fax .....

Address .....

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E-mail .....

Please return, together with a cheque for £30, payable to the British Spanish Law Association, to BSLA, 32 St. James's Street, 3rd floor, London SW1A 1HD.

Upon receipt of your cheque we will send you an invitation.

Further details from the British Spanish Law Association at 0207 930 3593.

## Members' news



Ann-Marie Hutchinson (above), from Dawson Cornwell Solicitors, a founding member of the BSLA, was awarded an OBE in the Queen's 2002 New Year's Honours List for her services to child abduction and adoption.



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