

IN THE HIGH COURT OF JUSTICE

CLAIM NO. HC11C00546

CHANCERY DIVISION

BETWEEN

Cathal Anthony Lyons

Claimant

and

- (1) Ernst & Young Europe LLP**
- (2) Ernst & Young (EMEIA) Services Limited**
- (3) Ernst & Young LLC**
- (4) CJSC Ernst & Young Vneshaudit**
- (5) Ernst & Young Valuation LLC**
- (6) Ernst & Young Business Advisory Services LLC**
- (7) Ernst & Young Valuation Advisors LLC**
- (8) Ernst & Young (CIS) Limited**
- (9) CIS Luxembourg SA**
- (10) Ernst & Young (CIS) BV Moscow Branch**

Defendants

WITNESS STATEMENT OF JAMES MANDEL

I, **JAMES MANDEL**, lawyer, of 11 Riverside Drive, New York, New York, United States of America, **WILL SAY AS FOLLOWS:**

1. I am a lawyer and was admitted to the Bar in Washington DC in 1982. I was General Counsel to the Ernst & Young CIS ("E&Y CIS") practice based in Moscow from early 2004 until January 28, 2010.
2. I was a partner in E&Y CIS, and my title was "Head of Department, In-House Legal" for the Tenth Defendant in this case, E&Y (CIS) BV Moscow Branch, which I can confirm is the branch of a company incorporated in the Netherlands. According to my Employment Contract of July 3, 2009 with Ernst & Young (CIS) BV Moscow Branch, I no longer had the title "partner" but was to continue working in the In-House Legal

Department as a Director on a full time basis until June 30, 2010, and on a part-time basis until June 30, 2011 with extension, if mutually agreed, to June 30, 2012. The contract was signed by Philipp Turowski, Chief Operating Officer of E&Y (CIS).

3. I make this statement at the request of the Claimant, Cathal Lyons, and to assist the Court. I have set out below my recollections of:

3.1 The background to the negotiation and signing of the agreement in April 2009 between Mr Lyons and E&Y CIS (the "Agreement") in which I acted for E&Y CIS, as in-house lawyer, and which I understand is the subject of this English High Court dispute. (I would note that E&Y have not approached me to make a statement.); and,

3.2 The incidents in late in 2009 and 2010, which I believe led to animosity towards the Claimant on the part of Herve Labaude, General Counsel of the Second Defendant, Ernst & Young (EMEIA) Services Limited. My recollections regarding Mr Labaude's role in this matter differ substantially from Mr Labaude's recounting of his recollections in his Witness Statement.

4. I have exhibited at "JM1" a bundle of paginated documents. References to page numbers in this statement are to those documents, unless otherwise stated.

Negotiation of the Agreement

5. In 2009 I was asked by Mr Turowski to assist E&Y CIS with the negotiation and documentation of Mr Lyons' exit as partner, director and employee from the Ernst & Young businesses. I knew that Mr Lyons had been badly injured in a terrible motorcycle accident while on E&Y business, and this had impaired his ability to work.

6. In 2009 E&Y had considerable sympathy for Mr Lyons, and the tenor of the negotiations was not at all adversarial: The only real issues were:
 - 6.1 fixing an amount to be paid to Mr Lyons for giving up his partnership;
 - 6.2 maintaining Mr Lyons' coverage under E&Y CIS's partner health insurance (which I recall was Mr Lyons' greatest concern) or, if not possible, then providing some monetary sum to compensate him for likely future medical expenses.

7. During the negotiations on behalf of E&Y CIS I was either dealing with Mr Lyons directly or his English lawyer, Mr Tom Custance of Fox Williams LLP. The emails at **pages 4 to 42** show some of the progress of the negotiations.

8. The Court will see repeated references to "EMEIA" meaning Europe, Middle East, India & Africa. This was a relatively new structure for Ernst & Young, whose purpose is to operate Ernst & Young's businesses across the aforementioned regions. E&Y CIS is part of the European region. The top of that structure is E&Y (EMEIA) Services Limited, which is an English company. The diagram of the E&Y CIS structure at **pages 1 to 3** shows the complexity and international nature of the arrangements.

9. I recall that Mr Lyons wanted to have the exit arrangements of the Agreement under English law and with English jurisdiction. It was standard for E&Y CIS when engaging foreign consultants, including former E&Y partners or employees, to put the engagements under English law and English dispute resolution if the consultant was not a Russian resident and requested English law. Most consultants do not trust Russian courts.

10. I recall English law and jurisdiction being discussed, and recall that this was agreed by Philipp Turowski, Chief Operating Officer of the Ernst & Young CIS Practice (effectively the second in command after the Managing Partner, Karl Johansson) very early in the negotiations at a meeting in late March/early April 2009.
11. The negotiations involving Messrs Lyons, Turowski and myself were of course conducted in English, and the drafts of the agreement were variously referred to as Letter of Intent, Term Sheet, and Heads of Terms (which are English legal concepts). At no time was there any suggestion that the arrangements governing Mr Lyons' relinquishing his status as partner would be governed by Russian law or subject to Russian dispute resolution.
12. A one page Letter of Intent was emailed to me by Mr Lyons on April 13, 2009 (**pages 4 to 8**) which had been created and signed by Mr Turowski.
13. As I gave consideration to the structure of the deal, it was clear that Mr Lyons would retain some form of employment or consultancy with E&Y, and I realised that we would have to split the arrangement into two agreements: a standard employment contract (which I understand has to be governed by local law if the employee is resident), and second agreement under English Law with English dispute resolution to deal with the issues relating to Mr. Lyons giving up his partnership status, in particular, provision of insurance and other compensation for medical expenses.
14. After I had amended the Letter of Intent on April 14, 2009, I sent a second draft called "Term Sheet" to Mr Lyons (**pages 9 to 13**), stating:

"Cathal

Attached is term sheet:

One is term sheet for EMEIA because it relates to their responsibilities

Second is your labor contract which may have some elements not of concern to EMEIA and also some technical issues on term of the contract, renewal, and termination”.

15. As noted, I was speaking and corresponding by email with Mr Lyons’ English lawyers. Mr Turowski of the E&Y CIS negotiating team was also aware that Mr Lyons had retained English lawyers (see my email of 17:53 April 16 2009 (**page 32**) where I refer to Mr Lyons’ “solicitor” which is not a term I would use for lawyers or counsel in other jurisdictions. This was still going on well into the middle of April 2009 (see **pages 22 and 25**). I would think it would be very odd for Mr Lyons to continue to retain an English lawyer, had his request for English law and jurisdiction been refused.

16. As can be seen in the exchanges on 16 April 2009 (**pages 32 to 34**), I make reference to the Terms Sheet having to be split in two:
 - 16.1 The “summary of terms”, which was to be relevant to “EMEIA” an English company, which was to be under English law and jurisdiction. Unfortunately I see that we did not record that English law would apply, either in the emails, or final “Key Terms” document which became the Agreement, and would be turned into a full contract at a later date.
 - 16.2 The employment agreement (hours worked, hourly rate, termination etc) which would be covered by a standard Russian law agreement.

17. If both agreements were to be under Russian law, there would have been no need to split the agreements into two.

18. It should be noted that it is the policy of the E&Y CIS (and virtually all other companies, foreign or Russian) that all Russian law and jurisdiction documents are drafted either in Russian or as a bilingual document. The practice for bilingual documents is that the Russian language is usually set out on the left hand side of contract, and the matching English is on the right. The Court can see examples of these in the Employment contract at pages 9 of 27 of Exhibit PT1. When I say this is E&Y CIS policy and practice, I cannot recall any E&Y Russian law contract which did not conform to this. In the six years I was General Counsel, it became "second nature" to me that an agreement drafted in English that was to be subject to the Russian courts would be translated into Russian prior to execution. That is exactly what happened with regard the Russian employment contract, but as the "Term Sheet" Agreement was agreed to be governed by English law, there was no need to translate it into Russian.

19. I believe that the Agreement was signed by the parties between 15 to 17 April 2009. Mr Turowski understood that the term sheet represented a binding commitment of Ernst & Young and he told me that he reviewed the terms with Karl Johansson and received Mr Johansson's approval.

20. Contrary to what Mr Turowski says at paragraph 25 of his witness statement, it was always intended that the "Key Terms" Agreement be turned into a proper contract. The references to Letter of Intent (**page 8**), Term Sheet (**pages 10 to 13**), "summary of terms" (**page 32**) and Key Terms (**pages 35 and 37**), reflect this. The last sentence of the Agreement states:

"The parties agree that they are obliged to execute and deliver an Agreement incorporating, and consistent with, the terms set forth above".

21. That long form agreement was to contain English law and jurisdiction clauses but in the event, it does not appear to have proceeded to a long form agreement.

Background to the allegations of bribery

22. I have read the witness statement of Herve Labaude and I believe that Mr Labaude neglected to mention certain additional facts involving the relationship of Mr Labaude with Mr Lyons and myself that explain the actions that Mr Labaude appears to have taken with respect to Mr. Lyons' Agreement.

23. In 2009, I was involved in investigating a possible violation of Ernst & Young's Anti-bribery policy:

23.1 On October 1, 2009, Mr Lyons and David O'Rourke, Deputy Chief Financial Officer of E&Y CIS, notified me of an unusual payment of the Ruble equivalent of Euro 120,000 to a Russian law firm which had been authorized by the E&Y CIS Managing Partner, Karl Johansson.

23.2 The payment was made pursuant to a legal services contract signed on behalf of Ernst & Young by Alexandra Lobova. One of Ms Lobova's principal responsibilities at that time was to handle tax litigation which the Russian tax authorities brought against Ernst & Young in Moscow. Based on that fact and Mr O'Rourke's report of a conversation with her before he contacted me, I had the suspicion that this payment was not a proper payment for legal fees, but was an illegal payment possibly made to facilitate a positive outcome of a tax case.

23.3 In October 2009 I contacted Mr Labaude, General Counsel to the Second Defendant, Ernst & Young (EMEIA) Services Limited, to explain my concerns

and I was authorized by him to investigate. In November and December 2009 I presented Mr Labaude with draft reports (which he will still have) that the principals involved in the payment, Mr Johansson and a tax partner, Alexandra Lobova, could not provide a satisfactory justification for the payment and were concealing its real purpose.

23.4 At the end of January, 2010, Mr Labaude came to Moscow ostensibly to announce my replacement as General Counsel by Alexey Statsenko. (The replacement had been planned long before the investigation.) He also told me that he would meet with Mr Johansson. He informed me that if Mr Johansson confirmed to him that the payment was entirely for legal services, Mr Labaude would accept that at face value and the investigation would be closed. At no time did Mr Labaude question the findings of my report: namely that the payment being for legal services could not be supported by the evidence we had gathered.

23.5 Later the same day I was told by Mr Labaude that he had received the oral "confirmation" he requested and the investigation was closed. I did not believe that this result was in keeping with Ernst & Young's Anti-Bribery Policy (at **pages 43 to 46**) and sometime afterwards discussed Mr Labaude's actions with Mr Lyons.

24. At the end of May 2010, Mr Lyons met with Maz Krupski from Ernst & Young's Global finance department. At that time Mr Lyons contacted me and asked if I would be willing to discuss the payment investigation with Mr Krupski. Mr Lyons stated that this was being handled as a "hotline" matter, in other words, it was being handled under Ernst & Young's special procedures for internal whistleblowing which is designed to protect any whistleblower (see para 5.6 of the policy at **page 46**). I said that I would and communicated this directly to Mr Krupski.

25. A week or two later, on or about June 11, 2010, as I was getting ready to leave for five weeks of vacation plus unpaid leave, I contacted Mr Krupski to see if he wanted to talk about the payment matter before I departed and he said yes. We then had a brief telephone conversation in which he confirmed that this was being handled as a "hotline" matter (although it did not come via the hotline channel) and that he was acting under the direction of the then Global General Counsel of Ernst & Young, Trevor Faure.
26. I explained my concerns about the payment itself and the termination of my investigation. I added that Mr Krupski should speak to Mr Labaude who, I said, would have a different view of the matter, and that Mr Krupski should feel free to get my view on anything Mr Labaude told him.
27. Mr Krupski evidently spoke to Mr Labaude after our call, and almost immediately thereafter I received several very angry phone calls from Mr Labaude. Mr Labaude was particularly curious about how the matter was resurrected and several times asked me to recount how this had happened. Each time I had to tell him that the matter had been initiated by Cathal Lyons in a conversation with Maz Krupski and that Mr Lyons had contacted me to see if I was willing to talk to Mr Krupski.
28. During one of our telephone conversations, Mr Labaude said that I would be "crushed" for what I had done. I understood by that, that he would seek some form of reprisal against me for reopening an investigation that he had tried to suppress. I assume that Mr Labaude succeeded in preventing any investigation that Mr Krupski or Mr Faure were contemplating as I heard nothing further about the matter.

29. With regards to Mr Labaude's evidence:

- 29.1 Mr Labaude's statement in paragraph 15 of his Witness Statement: "I have never met the Claimant and had no dealings or knowledge of the Claimant prior to the events I describe below." is not accurate. Mr Labaude clearly had knowledge of Mr Lyons prior to his discussions with him in 2011 and there is reason to believe that Mr Labaude's actions were motivated by the desire for reprisal against Mr Lyons for trying to revive the investigation into the illegal payments that Mr Labaude had tried to suppress.
- 29.2 In reference to paragraph 17 of Mr Labaude's witness statement, I worked with Mr Labaude on issues of cost savings. His sole interest was in controlling the costs of outside counsel and, based on my knowledge of his responsibilities, this is the only area in which he would have any responsibility. In 2010, I submitted to Mr Labaude several reports on the use of outside counsel by various EMEIA entities and never received a response from him. To the best of my knowledge, dealing with Mr Lyons was outside the scope of his normal responsibilities.
- 29.3 In my working relationship with Mr Labaude, which included the period of the 2008-2009 economic climate referenced in paragraph 17 of his Witness Statement, there was never any mention by Mr Labaude of his involvement in a "proper cost effectiveness review" except with respect to the engagement of outside counsel. To the best of my knowledge, the only two "consultant" agreements Mr Labaude reviewed were those of Mr Lyons and mine and I believe that was in order to take reprisals against us because of our discussions with Mr Krupski in May and June of 2010 described above. It is unlikely that Mr Labaude could have taken these actions, which clearly

violated Ernst & Young's Anti-Corruption policy, without authorization by Ernst & Young (EMEIA) Services Limited.

29.4 Mr. Labaude's statement in paragraph 20 of his Witness Statement is not accurate. Ernst & Young could include any person it wished on the CIGNA insurance provided it was willing to pay the premium: On or about 2005, Lisa Gialdini, although no longer employed by E&Y was included on the CIGNA policy for a year. It is also my recollection that Mr Gerard Anderson who retired in 2009 as a partner signed a consultancy agreement with E&Y CIS was also included on the CIGNA policy as if he were a "partner".

30. When I returned from my vacation in July 2010, a number of steps in reprisal were taken against me, including:

30.1 I was informed that I would no longer be a participant in the periodic telephone conferences of General Counsel;

30.2 reports that I had done for Mr Labaude on controlling outside counsel fees in EMEIA went unanswered; and

30.3 no further assignments were given to me.

31. Then in November 2010, Mr Labaude came to Moscow and invited me to a meeting with Mr Vitaly Pyltsov, the Chief Operating Officer of E&Y CIS to tell me that E&Y would not honor the July 3, 2009, Agreement described above. Later when I met privately with Mr Pyltsov, to discuss the terms of my termination, Mr Pyltsov stated that he personally thought I should complete my contract but that he had been directed by Mr Labaude to terminate it. The following is an accurate summary of part of that conversation with Mr Pyltsov:

Pyltsov: Looking at your contract it would be better if you stayed until 2012.

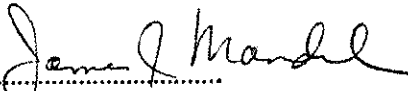
Mandel: Let me ask you something, Vitaly, is this [the decision not to honor my contract] all coming from Herve [Labaude]?

Pyltsov: It is coming from Herve.

32. In the end, I agreed to a termination agreement which reduced the amount originally due to me under the July 3, 2009 agreement by US\$ 100,000. Thus, according to Mr Pyltsov, the decision to terminate me was made by Herve Labaude of Ernst & Young (EMEIA) Services Limited and not E&Y (CIS). I believe it is likely that this also applies to the dishonouring of the arrangements made with Mr Lyons that is the subject of this lawsuit.

Statement of truth

I believe that the facts stated in this Witness Statement are true.

Signed: 
James Mandel
12 March 2012

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Defendants

**EXHIBIT "JM1" TO
WITNESS STATEMENT OF JAMES MANDEL**
