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Data protection in corporate transactions: key issues

As our economy emerges from the recession, and the number of business transactions increases, organisations and their advisers should ensure that data protection responsibilities are addressed at an early stage. Bridget Treacy and Purdey Castle, of Hunton & Williams, illustrate the key data protection issues arising from corporate transactions and provide practical tips for businesses on how to deal with such issues.

Which corporate transactions raise data protection issues?

In short, most corporate transactions will raise data protection issues. The definition of 'personal data' is very broad and includes any information that relates to an identified or identifiable living individual. Typically, businesses will process the personal data of their staff, customers (including contact details of corporate customers) and vendors. In the UK, the Data Protection Act 1998 (DPA or 'the Act') imposes obligations on data controllers (i.e. businesses) which collect and process personal data. Business transactions that are most likely to raise data protection issues are those which involve the transfer of employees' data (under the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), the transfer of customer databases, or the transfer of personal data abroad.

Key Data Protection Principles

Fair and lawful processing

The principle of fair and lawful processing is perhaps the most important data protection principle in the context of a corporate transaction. It applies to all processing activities, including to the seller's disclosure of personal data to the buyer, whether during due diligence or at completion. To satisfy this principle, the seller must ensure that the data processing activity satisfies a permitted condition, and that it provides appropriate fair processing information to individuals.

The permitted conditions for data processing are set out in Schedule 2 of the DPA. In the context of a corporate transaction, a seller will usually rely on consent or legitimate interests as the basis for transferring personal data to the buyer, or prospective buyer. Consent must be specific, informed and freely given. In the context of a corporate transaction, consent is usually difficult (if not impossible) to obtain. It is usually impractical to allow individuals to opt out of allowing their data to be processed as requested and, if the data are employee personal data, it is difficult to establish that consent has been freely given. Accordingly, legitimate interests is more commonly relied upon. This condition requires the controller to balance its interests against the risk of prejudice to the rights of individuals.

When providing fair processing information, the controller must provide details of its identity, the purposes for which the data may be processed and any other relevant information that will enable the processing to be fair. Typically, the seller will have provided fair processing information to its employees, customers and vendors at the point of data collection. Sometimes this information will reference the possibility of disclosure to a prospective acquirer of the business, but will not include specific details. It then falls to the parties to consider how to comply with this obligation in the context of a transaction, typically during due diligence. Usually, the parties will seek to minimise and, where possible, anonymise personal data disclosed at this stage, thereby avoiding the application of the DPA. If disclosure of personal data is necessary at this stage, the parties should focus on minimising the volume of data disclosed and ensure that a confidentiality agreement is signed.

Where data are transferred at completion, the need to provide fair processing information will depend on whether the transaction involved a transfer of the business, or a transfer of shares. Regarding the latter, the data controller does not change and new fair processing information is not required, unless the purposes for which the data are to be processed will change following completion. Where the transaction involves a transfer of assets, the controller will change and individuals must be informed. Usually the buyer will provide the updated fair processing information on behalf of both parties.

In practice, parties frequently do not provide fair processing notice where data are transferred during due diligence and often provide notice only after completion of the transaction. While not strictly in compliance with the DPA, the parties may decide that commercial sensitivities preclude earlier notification. Any decision not to comply with the requirements of the DPA must be very carefully weighed, with particular consideration given to any likely harm to individuals.

Processing for specified purposes

Data collected for one purpose cannot be processed for additional purposes without reference back to the individual. This principle is

relevant in a transactional context where a buyer wishes to process acquired data for additional purposes. A seller should ensure that the scope of the permitted processing is clear to the buyer and that the buyer takes responsibility for obtaining individuals' consent for any additional processing activity. The seller will also wish to limit its liability for the subsequent data processing activities of the buyer.

Accurate and kept up to date

The seller must also ensure that personal data relevant to or forming part of the transaction are accurate and current.

Transferring personal data abroad

The Act prohibits the transfer of personal data outside the European Economic Area (EEA) unless there is an adequate level of protection. There are well established bases for ensuring adequacy and, in the context of transactions, standard contractual clauses and the US Safe Harbor are the most commonly used. Perhaps of more practical significance is the fact that in corporate transactions the parties may not identify the transfer issue until late in the day. In particular, the need to transfer data may arise prior to and in preparation for completion. The possibility that personal data may need to be transferred internationally should be explored early during due diligence.

The risks of non-compliance

Breach of a Data Protection Principle may result in the Information Commissioner issuing an enforcement notice requiring the controller to comply with the relevant principle or to cease processing the data in question. Any failure to comply with an enforcement notice is a criminal offence. The Information Commissioner is increasingly proactive in bringing enforcement proceedings and adept at using the media to publicise breaches of the Act. Further, the Commissioner's powers to impose monetary penalties on controllers for serious breaches of the Act are expected to come into effect in April 2010. The maximum penalty is likely to be £500,000. The risks of non-compliance are therefore serious but with proper planning and due diligence, companies can successfully navigate the data protection requirements that arise in the context of a corporate transaction.

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Practical tips

Preparation

At an early stage, the seller must identify the personal data that may be impacted by the proposed transaction. The seller should ensure that all current processing is compliant with the DPA - e.g. registrations must be current, data must not be processed beyond permitted purposes and data should be accurate, current and secure.

Due diligence

Determine whether personal data need to be disclosed. If so, provide data subjects with fair processing information or anonymise the data. Where anonymisation is impractical:

- limit the categories of data disclosed (i.e. remove any sensitive personal data);
- limit the purposes for which the disclosed may be used, for example, obtain contractual undertakings to restrict the use of the data to conducting due diligence activities;
- prevent further disclosure of the data, for example, obtain contractual undertakings naming specific individuals to whom data may be disclosed and requiring the return of the data if the parties fail to complete the transaction.

Sellers should make buyers aware of the purposes for which data have been collected and obtain undertakings from the buyer that the data will be used in accordance with these purposes only. The buyer must obtain individuals' consent to process the data for any other purposes. Ensure that the data is kept secure. For example, if documents containing personal data are uploaded onto a virtual data room, restrict access to specific users, implement access control measures and restrict the ability of users to print documents containing personal data. Where it is necessary to transfer the data outside of the EEA ensure there is an appropriate mechanism for conducting the transfer (e.g. standard contractual clauses).

Post-completion

Where there has been an asset transfer, consider whether to inform data subjects of a change in identity of the data controller, and update registrations.

Where there has been a share transfer (and therefore no change in the identity of the data controller), but there is a change in the data processing activity, consider whether to update the fair processing information provided to data subjects.

The buyer should review the data held and ensure that data is retained only to the extent necessary to fulfil the purposes for which the data will be used.

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