JFSC v Equity Trust and Others

Jurisdiction:	Jersey
Judge:	The Deputy Bailiff
Judgment Date:	05 December 2007
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Text

[2007] JRC 229

ROYAL COURT

(Samedi Division)

Before:

M. C. St. J. Birt, **Esq.**, Deputy Bailiff, **and** Jurats Bullen **and** Newcombe.

In the Matter of the Collective Investment Funds (Jersey) Law 1998 As Amended.

And in the Matter of the R2R Bulgaria Property Fund, The R2R Croatia Property Fund, The R2I Montenegro Property Fund and Equity Trust (Jersey) Limited and Equity Trust Services Limited.

Between
Jersey Financial Services Commission
Representor
and

(1) Equity Trust (Jersey) Limited
(2) Equity Trust Services Limited
(3) Burlington Associates Limited
(4) Injaz Mena
(5) Ready2Invest (International) Limited
(6) Equity Trust (Jersey) Limited ("ETJL") as Trustee of the Proteus Factoring Services Trust and the Bacchus Factoring Services Trust
Respondents

Advocate D. S. Steenson **for Representor**.

Advocate M. L. A. Pallot **for the First and Second Respondents**.

Advocate S. M. Baker **for the Third Respondent**.

Advocate M. H. Temple **for the Fourth Respondent**.

Advocate G. S. Robinson **for the Fifth Respondent**.

Advocate M. J. Thompson **for the Sixth Respondent**.

Advocate T. J. Herbert **for Walbrook Trustees (Jersey) Limited (invited by the Deputy Bailiff to attend)**.

No Authorities

The Deputy Bailiff

1 This is an application by the Commission for an order that Equity Trust (Jersey) Limited and Equity Trust Services Limited should be removed as trustee and manager respectively of the three funds known as the Bulgaria Fund, the Croatia Fund and the Montenegro Fund.

2 The application has been adjourned on a number of occasions with a view to finding a replacement functionary and an independent firm of reporting accountants, who would carry out an investigation into whether the interests of the investors in these funds would be best served by some form of restructuring, as suggested by the promoters, so as to allow the envisaged property developments to be taken forward, or whether a winding up would be in their best interests.

3 After these various adjournments it has now been agreed that Walbrook will take over as functionary and Grant Thornton will carry out the investigation. We have before us a draft agreed order. However this requires the provision of certain monies and if these are not forthcoming Walbrook's appointment as functionary will not take effect. Part 3 of the draft order provides that in these circumstances Ernst & Young Appointed Functionaries (Jersey)

Limited would be appointed as trustee and manager of the three funds in place of the Equity entities and that Ernst & Young would also carry out the accounting investigation.

4 Equity are quite happy to be replaced by Walbrook. However Mr Pallot submits on their behalf that if for any reason, including non payment of the specified monies, Walbrook does not take up its appointment, it would be preferable for Equity to remain in place until Grant Thornton have completed their report, rather than Ernst & Young taking up the appointment as envisaged in Part 3 of the draft. The Commission opposes that application and we have been asked to rule on the matter at this stage.

5 The Commission submits that Equity has various conflicts of interest which render it inappropriate for Equity to continue as trustee and manager of the funds. We would summarise them very briefly as follows:

(i) As well as its position in connection with the funds, Equity is also trustee of certain Factoring Services Trusts, known as “FSTs”. These are indebted to the funds. They are also co-investors in some of the underlying investments which are held through Special Purpose Vehicles, (“SPVs”), and in turn Property Development Companies, (“PDCs”). There is said to be some uncertainty as to whether the respective interests of the funds and the FSTs have been fairly allocated and/or accurately recorded. The position of the FSTs is clearly potentially adverse to that of the funds.

(ii) Equity is also trustee of the Ditare Fund, which has also co-invested in the underlying investments. It is said that Ditare has been allowed to invest on more favourable terms than the funds. As Equity is trustee of both it would clearly be impossible for it to resolve any potential conflict between them.

(iii) Because of the various different interests there is an issue as to who, if anyone, should have control of the SPVs. Equity cannot resolve this because it, in effect, represents all three competing interests.

(iv) It is said that many of the difficulties have arisen because of poor record keeping and uncertainty as to the respective interests of the various parties in the various underlying investments. It is said that Equity may be at fault in this regard and that claims may lie against Equity for any resulting losses. Whilst the role of the investigating accountants will not focus specifically on this aspect, they may well find it necessary, as part of their role, to make observations or recommendations in relation to this aspect and it is said that it would be difficult for the accountants to be seen to be clearly independent if they were reporting to one of the parties who they may wish to blame for some of the problems which beset the funds.

6 Mr Pallot, on behalf of Equity, does not dispute that these potential conflicts of interest exist but he submits that they are all manageable. Firstly he says that Equity has given certain undertakings to the Court which mean that it will be fulfilling a very passive role pending receipt of the accountants' report, and in effect will be no more than safeguarding the assets

in the meantime. He says there is therefore little scope for the conflicts actually causing problems. Secondly, he says that the report by Grant Thornton will clearly be prepared by wholly independent accountants who will be reporting to the Court as much as to Equity.

7 He submitted that there were a number of advantages to Equity continuing if Walbrook could not be appointed. First there would be a cost saving because the handover would clearly incur costs. Secondly, he said that employees of Equity were very familiar with the books and records and could therefore help the reporting accountants with any queries on those matters. Thirdly, he said that the Equity personnel were familiar with the structure generally and therefore could assist the accountants more generally in relation to any queries which they might have. Fourthly, he said that if Equity remained there would be no delay in Grant Thornton getting going, whereas delay might well be caused by a handover.

8 In summary Mr Pallot says that there will only be a short period of time until the report is completed and that leaving Equity in place would be satisfactory and more in the interests of the investors. It would also avoid the problems of perception with Ernst & Young referred to by the Court in its judgment of 28 th September.

9 We have carefully considered these points. We accept that they are put forward by Equity in the genuine belief that this would be in the interests of the investors. We are satisfied they are acting from entirely proper motives in putting this forward. However, we are in no doubt that if Walbrook cannot take up its appointment, Part 3 of the draft order should come into play and Ernst & Young should be appointed, both as functionary and to carry out the investigation. Even allowing for the limited nature of the role which the trustee and the manager of the funds will be undertaking until the accountants' report is produced, we think that the interests of the investors require there to be a trustee and manager who are looking solely after their interests and are not conflicted by owing duties to others with a potentially adverse interest. Furthermore we are not happy that the accountants should be reporting to a functionary in circumstances where they may find it necessary to make findings or observations which are critical of that functionary.

10 We acknowledge the perception point concerning Ernst & Young to which we referred in our judgment of 28 th September. However, since then we have received an affidavit from a partner on behalf of Ernst and Young who has stated that the firm fully understands that its role is to reach its own independent conclusion. For the avoidance of any doubt we state that Ernst & Young are to ignore any preference for a winding up which the Commission may be thought to have. Ernst & Young are to reach their own independent conclusion on the best way forward in the interests of the investors whose interests are paramount. If it is their opinion that reconstruction offers the best prospects for these investors, and that such a reconstruction is practicable and achievable, then that is what they should recommend. If on the other hand, they conclude that there is no alternative to a winding up, then that is what they should recommend. It is entirely a matter for them and we are confident that Ernst & Young will act with complete independence.

11 In all these circumstances we therefore approve Part 3 of the order.