

Trilogy Management v YT and Others 22-Aug-12

Jurisdiction:	Jersey
Judge:	Nugee JA
Judgment Date:	22 August 2012
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Text

[2012] JCA 152

COURT OF APPEAL

Before:

J. W. McNeill, **Q.C.**, **President**, C. Montgomery, **Q.C.**, and; C. Nugee, **Q.C.**.

Trilogy Management Limited
Representor
and
(1) YT Charitable Foundation (International) Limited
(2) HM Attorney General
(3) OM – LC2 Charitable Foundation International
(4) The Empowerment Charitable Trust
(5) The Saving Grace Charitable Trust
(6) OM – VC Charitable Foundation
(7) The Well Trust
(8) Mrs C

Respondents

Advocate S. M. Baker for the Representor.

Advocate J. P. Speck for the First Respondent.

Advocate N. F. Journeaux for the Eighth Respondent.

The other Respondents did not appear and were not represented.

Authorities

Trilogy Management v YT and Others [\[2012\] JRC 093](#) .

La Petit Croatie Limited v Ledo [\[2009\] JCA 221](#) .

In Re Internine Trust [\[2005\] JLR 236](#) .

Rainy Sky SA v Kookmin Bank [\[2011\] 1 WLR 2900](#) .

Co-operative Wholesale Society Ltd v National Westminster plc [\[1995\] 1 EGLR 97](#) .

Society of Lloyd's v Robinson [\[1999\] 1 WLR 756](#) .

Arbuthnott v Fagan [\[1995\] CLC 1396](#) .

LB Re Financing No 3 Ltd v Excalibur Funding No 1 Plc [\[2011\] EWHC 2111 \(Ch\)](#) .

Bratton Seymour Service Co Limited v Oxborough [\[1992\] BCLC 693](#) .

Attorney-General of Belize v Belize Telecom Ltd [\[2009\] 1 WLR 1988](#) .

Companies (Jersey) Law 1991.

IFRS Framework for the Preparation and Presentation of Financial Statements.

Trust — appeal against the judgment of the Royal Court dated 10 May 2012.

Nugee JA

Introduction

- 1 This appeal concerns a provision in the Articles of Association of a Jersey company (“JY”) which requires a minimum proportion of the company's profits for the year to be distributed by way of dividend. The Appellant (“Mrs C”) appeals against a judgment of the Royal Court (Samedi Division) given on 10 May 2012 by Birt, Bailiff (assisted by Jurats Tibbo and

Nicolle). In that judgment the Court decided a number of issues but the appeal is limited to the single issue whether they were correct to hold (for the purposes of the application of the mandatory dividend provision) that the profit of JY for the year of account to 31 December 2005 was some \$223.7m. Mrs C contends that they should have held that for the year 2005 JY made no profit but rather a loss of some \$2.1m. (All references are to US \$ and save where exact figures are given are rounded to the nearest \$0.1m). Argument before us was restricted to Mrs C and the first respondent. We granted leave to withdraw to Advocate Speck, as the Charitable Foundation whom he represented was obliged, as before the Royal Court, to adopt a neutral stance: see paragraph 29 below.

Background

- 2 The background is set out clearly in the judgment of the Royal Court, and it is not necessary to give more than a brief summary here.
- 3 Mrs C's husband ("OM") was a successful businessman who had built up a substantial fortune and who wished to establish a charitable structure. In April 1987 he therefore formed JY with two classes of shares: A shares, which carry the control of the company, but no right to participate in dividends or other distributions (save for a return of capital on a winding up of the company); and B shares which entitle the holder to the economic interest in the company, and in particular to receipt of such dividends as are declared.
- 4 OM retained legal or beneficial ownership of the A shares but in May 1987 he established a charitable trust governed by the law of Jersey ("the Foundation") with a corporate trustee ("YT") which has at all times been sole trustee of the Foundation; and the B shares were in due course transferred or issued to YT to hold on the trusts of the Foundation. As set out in the Trust Instrument, these are in effect to pay such parts of the income and capital of the trust fund to such of the Charitable Objects as the trustee should determine, the Charitable Objects being defined as any persons and objects including charitable purposes, institutions and foundations throughout the world as are recognised to be charitable according to the law of Jersey (so long as they would also be recognised as charitable according to the laws of Hong Kong and Australia).
- 5 During his lifetime OM had complete control of this structure. He controlled JY as he held half the 40,000 issued A shares in his own name, and the other half were held by a nominee for him. He controlled YT as he held all but 3 of the 10,000 issued shares in YT in his own name, the other 3 being held by another nominee for him. But as can be seen the economic interest was held by YT on trust for the charitable Foundation which he had established.
- 6 OM died on 10 December 2001, survived by Mrs C and their eight children: two sons (PC and AC) and six daughters (LC, CC, VC, JC, MC and MI). All of them are adult. Four of them (PC, AC, LC and MC) were named as executors in his will together with the partners in Simmons and Simmons, and probate of his will was duly granted by the Royal Court on

17 October 2002 to those four and one of the partners, Caroline Garnham.

- 7 By clause 5 of his will OM left his residuary estate as to 1% to his widow Mrs C and as to 99% to the trustee of a settlement that he had made in 1993.
- 8 By clause 6 of his will, OM purported to deal with the A shares in JY and the shares in YT by leaving them to the trustees of his will subject to certain directions. Doubts arose as to the validity and effect of this provision, and this and some other matters were the subject of proceedings in the Royal Court.
- 9 It is not necessary to detail these proceedings as they were all compromised by Act of Court dated 11 June 2004. So far as relevant the effect of the compromise, once implemented, was as follows:-
 - (i) The A shares in JY were vested as to 1% in Mrs C and as to 99% in YT as trustee of the Foundation.
 - (ii) The shares in YT were vested as to 1% in Mrs C, as to 3% in the trustee of the 1993 settlement, and as to 96% in the trustee of a new purpose trust ("the Purpose Trust"). The Purpose Trust, which was established under the law of Jersey by a declaration of trust dated 24 June 2004, had among its purposes to procure that the composition of the boards of both JY and YT itself should be in accordance with certain agreed principles; and to promote the purposes of the Foundation and of the eight charitable sub-trusts referred to below.
 - (iii) Resolutions were passed procuring that the Boards of JY and YT (in line with the agreed principles) consisted of the four children of OM who were executors (PC, AC, LC and MC) together with one non-family director, Advocate Alan Binnington.
 - (iv) By 25 June 2004 eight charitable sub-trusts were established, one associated with each of the eight children. Each originally had the relevant child as "Guardian" with a significant role in how the sub-trust was administered. Three of the sub-trusts, associated with CC, JC and MI, now have as trustee the First Respondent, Trilogy Management Limited ("Trilogy"), a company of which they are three of the four directors.
 - (v) On the same date YT as trustee of the Foundation executed an Instrument of Appointment under which it declared that it held the appointed fund (consisting of YT's 99% holding of A shares and 100% holding of B shares in JY) on trust to pay the income thereof, and any capital distributions, to the trustees of the eight sub-trusts in equal shares.
 - (vi) Also on the same date the articles of JY were amended by special resolution. The amendments substituted a new Article 76 under which decisions of the Board have to be unanimous; and a new Article 96 under which a minimum amount of dividend has to be distributed each year. The text of the new Article 96 is set out below.

(vii) The articles of YT were also amended to require decisions of the Board to be made unanimously.

- 10 In addition, although not provided for in the compromise as set out in the Act of Court, a dividend of \$80m was declared on 1 November 2004. This (referred to as a “prime the pump” or “PTP” dividend) was intended to provide initial funding of \$10m to each of the sub-trusts.
- 11 Article 96 of the Articles of Association of JY in its form as substituted on 25 June 2004 (“Article 96”), provides as follows:-

“The profits of the Company available for dividend and resolved to be distributed shall be applied in the payment of dividends to the Members in accordance with their respective rights and priorities. Notwithstanding any other provision of these articles, the Directors shall, in any financial year in which profits of that year are available for dividend, recommend to the Company a dividend of not less than 75% of such profits (or such greater amount as a majority of the Directors shall agree, notwithstanding the terms of Article 76), provided always that if the payment of such dividend would result in the net asset value of the Company, as disclosed in the accounts of the Company for that financial period, reducing to less than 10% of the net asset value of the Company as disclosed in the accounts of the Company for the preceding period, the Directors shall recommend a dividend of not less than 50% of such profits. If the Directors make such a recommendation, the Company in general meeting shall ratify and approve such dividends accordingly.”

It is this provision, and in particular the meaning of the words “profits of that year”, with which this appeal is concerned.

- 12 In summary, the structure as agreed in the compromise and duly implemented was to vest control of JY and of YT in four of the children of OM (together with one outside director); but to oblige them to distribute a minimum amount of the profits of JY (usually 75% of the profits for the year) to the eight sub-trusts, where each of the eight children would have a say in how the relevant funds would be utilised.

JY's accounts

- 13 As already indicated the only issue in the appeal is the correct identification, for the purposes of the mandatory dividend provision in Article 96, of the “profits of that year” for the financial year to 31 December 2005.
- 14 In order to explain the issue between the parties, it is necessary to refer in some detail to the accounts of JY.

- 15 The earliest accounts which we have seen are those for the year ended 31 December 2002 which were signed on behalf of the Board on 12 March 2004 and were the latest accounts available at the time of the compromise in June 2004. They were audited by a Hong Kong accountant and they (and, we are told, all previous accounts) were prepared on the historical cost basis. This means that investments are shown at cost in the Balance Sheet. The corollary of this is that if an investment is sold during the year, the difference between the book value of the investment and the net sale proceeds is the amount of profit (or loss as the case may be) realised on the sale, and will be included in the profit shown on the Profit and Loss Account.
- 16 JY's assets were very substantial. They consisted in effect of (i) investments (quoted shares and bonds); (ii) interests in three subsidiaries (unquoted shares in, and loans to, the subsidiaries); and (iii) cash at the bank. For present purposes what is relevant is the treatment of the investments. In accordance with the historical cost basis these were shown in the 2002 Balance Sheet at cost, namely \$56,196,234. This was the same figure as in the 2001 accounts (the figures for 2001 being included for comparison in the usual way), indicating that there had been no change in the investments for the year. This cost figure was considerably less than their market value: a note to the accounts showed that the market value of the investments had been some \$202.5m at the end of 2001 and was some \$192.1m at the end of 2002.
- 17 The "Profit for the Year" shown on the Profit and Loss Account for 2002 was some \$15.8m. After provision for a proposed dividend of \$1.3m, the effect was to increase the "Unappropriated Profits" carried forward from some \$256.6m to some \$271.2m.
- 18 Annexed to this judgment is a table which shows these figures in tabular form, together with those shown in the accounts for the years ended 31 December 2003 and 31 December 2004, each of which followed the same format and was also audited by the same Hong Kong accountant. In each case the "Profit for the Year" as shown on the Profit and Loss Account (so called in the 2002 and 2003 accounts – the equivalent is called the Income Statement in the 2004 accounts) takes no account of changes in the market value of the investments, although this figure (called "market value" in the 2002 and 2003 accounts and "fair value" in the 2004 accounts) is given in a note to the accounts.
- 19 Had the accounts remained in this form, it is not now in dispute that Article 96 would have required a minimum dividend of 75% of the figure shown in the Profit and Loss Account for each year as the "Profit for the Year".
- 20 However in 2006 JY changed its auditors to KPMG Channel Islands Limited, and the 2005 accounts were prepared in a rather different way. As explained in the Notes to the Financial Statements, they were prepared in accordance with International Financial Reporting Standards ("IFRS"), and the policy in relation to Investments was as follows:-

"Quoted investments are stated at their fair value with movements in fair value

being recognised in the income statement. The 2004 comparative figures have been restated accordingly, as disclosed in the Statement of Changes in Equity.”

- 21 The practical effect of adopting this policy is to present both the Balance Sheet and the Income Statement differently from how they had been presented in the previous years' accounts. So far as the Balance Sheet is concerned, the figure for investments now reflects the fair value of the investments, or as it is called they are “marked to market”. In a case like the present where the current market value of investments is significantly in excess of the historical cost, this will mean a significant increase in the net assets, matched by an equal increase in the retained earnings, over the figure shown in the 2004 accounts. In the case of the Income Statement, changes during the year in the fair value of investments will be included in the calculation of profit or loss even if none of the assets is sold.
- 22 This can be illustrated by comparing the restated 2004 accounts (included in the 2005 accounts for comparison) with the audited 2004 accounts, as shown on the table annexed. The value of investments shown in the 2004 Balance Sheet was some \$41.5m but in the restated accounts is shown as some \$267.3m; there is a similar increase in the retained earnings from some \$239.5m to some \$465.3m. This is broken down in the Statement of Changes in Equity which has the following figures for retained earnings:

As shown by the Income Statement for 2004 as restated, the figure of \$54.5m for “Profit for the Year” includes some \$19.5m for “gain on investments at fair value”. In other words this \$19.5m was not realised during the year by a sale of investments but simply reflects an increase in fair value during the year. This has the effect of increasing the “Profit for the Year” from the \$35m shown in the original 2004 accounts to the \$54.5m shown in the restated accounts.

Retained earnings

Balance as at 1 January 2004 (previously stated)	284,422,247	Prior period adjustment to fair value of quoted investments	206,348,264
Balance as at 1 January 2004 (restated)	490,770,511	Profit for the year	54,541,896
Dividend paid (<u>80,000,000</u>)		Balance as at 31 December 2004	465,312,407

- 23 The 2005 accounts, prepared in accordance with these principles, show in the Income Statement a loss of \$2,082,149. This is despite the fact that during the year investments were sold which realised a gain over their initial cost of over \$104m (mainly if not exclusively due to the sale of a substantial holding of HSBC shares); this was more than offset by a decline in fair value of the other investments of over \$111m. As a result the Retained Earnings shown on the Balance Sheet declined from some \$465.3m at the beginning of the year to some \$463.2m at the end.

24 In this appeal Mrs C's contention is the simple one that for the purposes of the mandatory dividend provision in Article 96 JY's "profits of that year" are the "Profit for the Year" shown in the Income Statement included in JY's audited Financial Statements for the year in question. There is no such profit shown in the Financial Statements for 2005 as the Income Statement shows JY as having made a loss not a profit during the year.

25 Trilogy seeks to uphold the judgment of the Royal Court in which the Court held that the "profits of that year" for 2005 should include a figure of \$225.8m, made up as follows:-

In essence the reasoning of the Royal Court was that these sums were "profits" within the meaning of Article 96; these profits were first recognised in the 2005 accounts; and they must be regarded as "profits of" the year 2005 as that is the only year in which they were recognised in the accounts. They are therefore caught by Article 96. When the \$225.8m profit is added to the \$2.1m loss shown in the Income Statement for 2005, the net profit of the year for the purposes of Article 96 is some \$223.7m – the precise figure being \$223,730,540.

Revaluation of investments as at 1 January 2004 \$206.3m

Increase in fair value in 2004	<u>\$ 19.5m</u>
	\$225.8m

26 In the remainder of this judgment we will refer to the \$225.8m figure as "the revaluation profit".

Proceedings below

27 On 10 August 2007 the Board of JY considered whether to declare an interim dividend for 2005. The audited accounts for 2005 had been circulated prior to the meeting. The directors noted that Article 96 required JY to distribute not less than 75% of the profits for that year; that JY had made a loss for 2005 and that the relevant figure was nil; and therefore that there was no requirement for them to make a dividend distribution for 2005. The same individuals, acting as the Board of YT, then considered whether to procure JY to make an interim dividend and resolved to procure a dividend of \$16m; and the Board of JY then signed a written resolution to that effect. This is the only dividend that has been declared for 2005.

28 The present proceedings were commenced by Trilogy by Representation dated 3 November 2010. This raised a number of issues but prominent among them was Trilogy's contention that Article 96 had been incorrectly applied and that far larger sums should have been distributed under that Article than had been. By Act of Court dated 12 August 2011 the

Bailiff directed that there be the trial of a preliminary issue as to:-

- (i) the correct construction of Article 96 as to the mandatory requirement for a payment of a dividend of not less than 75% of the profits of JY and the meaning of the words “profits of that year”;
- (ii) in the light of such construction the sums (if any) that should properly have been recommended pursuant to the said mandatory requirement for dividend to the company by the directors under Article 96 in relation to the 2003, 2004, 2005, 2006, 2007, 2008 and 2009 years of account; and
- (iii) the sums (if any) due to the eight charitable sub-trusts of the Foundation arising from the determination of (a) and (b).

29 This preliminary issue was tried by the Royal Court. The only parties who appeared were Trilogy, YT and Mrs C (who had been given leave to participate in the proceedings). At the hearing YT adopted a neutral position as its Board was split on the issues before the Court and its articles required the Board to act unanimously. The effective argument was therefore between Trilogy on the one hand and Mrs C on the other.

30 The Court had the benefit of evidence from expert accountants: Mr Robert Drennan of Rawlinson & Hunter, instructed on behalf of Trilogy, and Mr Patrick Maher of Deloitte LLP, instructed on behalf of YT. The Court recorded in its judgment that both were extremely well qualified as expert witnesses, and expressed their gratitude to both of them for their ability to explain matters in clear and simple terms; and in particular for a joint report which set out their points of agreement and disagreement in exemplary fashion. Having ourselves read their reports and been taken through the relevant parts of the transcript of their oral evidence, we agree that their evidence was both clear and helpful; and that the area of difference between them was, as the Royal Court said in its judgment, a very narrow one.

31 In its judgment the Royal Court considered first the question of what were the profits of 2005 for the purposes of Article 96. It accepted Trilogy's case that the profits of 2005 were some \$223.7m (for reasons which we summarise below). It then went on to consider two other matters (whether Article 96 applied to the profits of 2003 or not; and whether the PTP dividend could be taken into account for the purposes of calculating the dividend that should be declared for 2003 and 2004). Neither of those matters is raised on this appeal which is concerned solely with the question as to what were the profits of 2005 for the purposes of Article 96.

32 The reasoning of the Royal Court on this issue can be summarised as follows:-

- (i) “Profit” for the purposes of Article 96 is to be ascertained in accordance with generally accepted accountancy principles.

This meant that the Court did not agree with the view taken by Mr Victor Joffe QC who had advised that Article 96 required a yearly revaluation of all the assets of JY, including its interest in its subsidiaries. Both the experts agreed that this was not required by either the historical cost basis or the IFRS basis of accounting and none of the parties sought to uphold Mr Joffe's analysis.

(ii) Both experts agreed that it was perfectly proper for the Board to have adopted either the historical cost basis or the IFRS basis for the company's accounts, and the Court concluded that "profit" in Article 96 is to be construed as meaning the profit as ascertained by generally accepted accounting principles as applied by the company in its preparation of its accounts from time to time.

(iii) It followed that the profits for 2004 (and if applicable 2003) were the figures prepared under the historical cost basis, being the generally accepted accounting principle in fact used for JY's accounts for those years.

This meant that the Court did not agree with Mr Maher who had taken the view that Article 96 required the IFRS basis to be applied retrospectively to 2003 and 2004, a view that Advocate Journeaux on behalf of Mrs C did not put forward as his primary case below and did not seek to support on this appeal.

(iv) It also followed that the profits for 2006 and later years must be calculated on the IFRS basis being the generally accepted accounting principle now adopted by JY.

The Court noted that there was no dispute on this and both experts agreed with the figures put forward by KPMG.

(v) That left the question of the figure for 2005. The relevant question was whether the \$225.8m revaluation profit was a profit of 2005 or not; in the Court's judgment it had to be treated as a profit of 2005 as it had not been recognised in any of the years prior to 2005 and was first recognised in 2005. If it were not treated as profit of that year, it would not be treated as a profit of any year, which would be wrong.

(vi) The Court recognised that the \$225.8m was not taken through the profit and loss account (or income statement) for the year, but pointed out that it was reflected in the accounts: if one compares the net asset figure as at 31 December 2004 as shown in the 2004 accounts (\$240m) with that as at 31 December 2005 as shown in the 2005 accounts (\$463.7m), the difference is \$223.7m. This is the revaluation figure of \$225.8m less the loss for the year 2005 of \$2.1m.

(vii) The Court therefore concluded that the profit of 2005 for the purposes of Article 96 was the revaluation profit of \$225.8m less the loss for the year of \$2.1m making a total of \$223.7m, the exact figure being \$223,730,540.

33 By Act of Court dated 10 May 2012 the Royal Court therefore declared, among other things, that for the year of account to 31 December 2005 JY's profit was \$223,730,540; that JY should have declared a dividend under Article 96 of \$167,797,905; and that JY having distributed \$16m by way of dividend, a further dividend of \$151,797,905 should be declared

for the year. It ordered that YT as trustee of the Foundation procure that JY declare such a dividend and procure payment of one-eighth of such dividend to each of the sub-trusts.

- 34 It is against those parts of the Act of Court that Mrs C appeals, seeking instead a declaration that for the year of account to 31 December 2005 JY's profit was a loss of \$2.1m or thereabouts and that no mandatory dividend was therefore due for 2005 under Article 96.
- 35 We announced after the conclusion of the oral argument that we would allow the appeal for reasons to be delivered later. This is the judgment of the Court in which we give our reasons for allowing the appeal.

Principles of construction

- 36 There was no dispute between the parties as to the principles applicable to the construction of the Articles of JY and we can therefore summarise them quite briefly.
- 37 *In La Petit Croatie Limited v Ledo* [\[2009\] JCA 221](#) this Court considered the approach in this jurisdiction to the construction of documents generally. It endorsed the principles set out in the judgment of Commissioner Page in *In Re Internine Trust* [\[2005\] JLR 236](#) at paragraph 62. At paragraph 11, Martin JA, with whom the other members of the Court agreed, summarised those principles as follows:-

“The aim is to establish the presumed intention of the parties from the words used; but the words used must be construed against the background of the surrounding circumstances, which means the circumstances that must be taken to have been known to the [parties] at the time. These circumstances include anything that would have affected the way in which the language would have been understood by a reasonable man, except that evidence of subjective intention is ordinarily inadmissible. The words must also be read in the context of the document as a whole, and should so far as possible be given their ordinary meaning; but a different meaning may have to be given to them if a reading of the document as a whole and common sense so require.”

- 38 This summary is consistent with views recently expressed in the United Kingdom Supreme Court in *Rainy Sky SA v Kookmin Bank* [\[2011\] 1 WLR 2900](#): see paragraph 14 in the judgment of Lord Clarke of Stone-cum-Ebony JSC, with whom the other members of the Court agreed.
- 39 To the summary by Martin JA the following supplementary points can be added:-

(i) First, where parties have used unambiguous language the Court must apply it: (per Lord Clarke in *Rainy Sky SA* at paragraph 23). The Court cannot rewrite the language

which the parties have used in order to make it conform to business common sense (per Hoffmann LJ in *Co-operative Wholesale Society Ltd v National Westminster plc* [1995] 1 EGLR 97, cited in *Rainy Sky SA* at paragraph 23). Loyalty to the text of a commercial contract, instrument or document read in its contextual setting is the paramount principle of interpretation (per Lord Steyn in *Society of Lloyd's v Robinson* [1999] 1 WLR 756, cited in *Rainy Sky SA* at paragraph 25).

(ii) Second, however, the Court should be astute to remember that, language being a flexible instrument, if the words used are capable of more than one construction that which appears most likely to give effect to the commercial purpose of the agreement should be chosen (per Hoffmann LJ in *Co-operative Wholesale Society Ltd v National Westminster plc*); the Court ought generally to favour a commercially sensible construction over technical interpretations and undue emphasis on niceties of language (per Lord Steyn in *Society of Lloyd's v Robinson*). If therefore there are two possible constructions, the Court is entitled to prefer the construction which is consistent with business common sense and to reject the other: see *Rainy Sky SA* at paragraphs 21, 23 and 25.

(iii) The exercise of construction is therefore essentially one unitary exercise (per Lord Clarke in *Rainy Sky SA* at paragraph 21), “neither uncompromisingly literal nor unswervingly purposive” (per Sir Thomas Bingham MR in *Arbuthnott v Fagan* [1995] CLC 1396).

40 Advocate Journeaux also submitted that cases where the Court is asked to depart from the natural meaning of the language used by the parties fall on a spectrum. The clearer the language that the parties have used, the slower the Court should be to displace that meaning by reference to considerations of the commercial consequences. He relied on the recent statement by Briggs J in the English High Court in *LB Re Financing No 3 Ltd v Excalibur Funding No 1 Plc* [2011] EWHC 2111 (Ch) at paragraph 46:-

“Commercial absurdity may require the court to depart even from the apparently unambiguous natural meaning of a provision in an instrument, because “the law does not require judges to attribute to the parties an intention they plainly could not have had”: see per Lord Hoffmann in the ICS case at page 913. Questions of commercial common sense falling short of absurdity may however enable the court to choose between genuinely alternative meanings of an ambiguous provision. The greater the ambiguity, the more persuasive may be an argument based upon the apparently greater degree of common sense of one version over the other.”

We accept this submission (which Advocate Baker did not dispute) and have found it a helpful statement of the appropriate approach. The corollary of the last sentence in the passage we have cited is that the less ambiguous the provision in question is, the less persuasive is an appeal to an argument that a different interpretation appears to make more commercial sense. We agree.

41 One other point of principle should be noted, although again it was not disputed before us.

In the construction of the Articles of Association of an incorporated entity there are severe limits on the admissibility of surrounding circumstances. Evidence of surrounding circumstances is probably admissible only to the extent of identifying persons, places or other subject matter referred to in the Articles; extrinsic evidence is not admissible for the purposes of implying a term based on business efficacy. To allow reference to extrinsic circumstances for such a purpose would permit the notional possibility that different implications would arise between the company and different subscribers: see *Bratton Seymour Service Co Limited v Oxborough* [1992] BCLC 693, 698 (Steyn LJ, as he then was) and 699 (Sir Christopher Slade). That decision was in terms addressed to a question of implication, but the reasoning applies equally to construction of the express terms of the articles. The essence of the reasoning is that the Memorandum and Articles of a company, once registered, constitute a statutory contract the terms of which are available to any member of the public, and as such cannot be affected by extrinsic matters known only to certain persons. As it was put by Lord Hoffmann in delivering the opinion of the Privy Council in *Attorney-General of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988 at paragraph 36:-

“Because the articles are required to be registered, addressed to anyone who wishes to inspect them, the admissible background for the purposes of construction must be limited to what any reader would reasonably be supposed to know. It cannot include extrinsic facts which were known only to some of the people involved in the formation of the company.”

The same principles apply to a Jersey company. Under the *Companies (Jersey) Law 1991* the Memorandum and Articles of a company are required to be registered (as are special resolutions), constitute a statutory contract between the company and its members, and are open to inspection by the public: see Articles 5, 10, 100 and 202 of the Law.

- 42 In the present case this means that none of the background to the introduction of Article 96 – the terms of OM's will, the litigation between the parties and the terms of compromise – is admissible in construing Article 96. Article 96 must be interpreted by reference to the terms of the Articles as a whole and such facts as any reader of the Articles would reasonably be supposed to know.

The natural meaning of Article 96

- 43 It is now possible to construe Article 96 by reference to these principles. Advocate Baker very helpfully commenced his address to us by listing what was not in dispute, as follows:-

(i) It is not in dispute that the \$206.3m shown in the Statement of Changes in Equity as the “prior period adjustment to fair value of quoted investments” was a profit (as indeed was the \$19.5m shown as the gain on investments at fair value in the Income Statement for 2004 as restated).

(ii) It is not in dispute that the \$206.3m (and the \$19.5m) constituted profits available for dividend.

(iii) It is not in dispute that these profits were recognised for the first time in the 2005 accounts; they were not recognised in the 2003 or 2004 or indeed any other accounts.

(iv) It is not in dispute that “profits” in Article 96 needs to be interpreted by reference to generally accepted accounting principles.

44 As this demonstrates the issue of construction between the parties is indeed a very narrow one. It can be summarised as whether, as Advocate Baker submits, the “profits of that year” for 2005 are the sums first recognised in the 2005 accounts as profits of the company; or whether, as Advocate Journeaux submits, the “profits of that year” are those recognised in the 2005 accounts as profits for the year 2005.

45 The construction of Article 96 must start with the language used in the Article. We repeat the relevant words for convenience:-

“...the Directors shall, in any financial year in which profits of that year are available for dividend, recommend to the Company a dividend of not less than 75% of such profits”

46 There is no difficulty over the identification of the financial year in question: JY made up its accounts to 31 December in each year, and the relevant financial year is the year to 31 December 2005. Article 96 requires the profits of that year to be ascertained, as it is 75% of such profits that are the subject of mandatory distribution.

47 Nor is there before us any dispute as to what “profits” means for this purpose. The parties are agreed that “profit” is to be ascertained in accordance with the generally accepted accounting principles as adopted by the company at the relevant time: see paragraphs 49, 52, 56 and 58 in the judgment below. As disclosed in those paragraphs, the Royal Court were unable to find any inconsistency with subject or context which should lead the word “profit” for the purpose of Article 96 to be ascertained otherwise than in accordance with generally accepted accounting principles, as provided for in Article 114(4)(d) of the Companies (Jersey) Law 1991, as in force at the relevant time. As the learned Bailiff stated at paragraph 52:-

“In our judgment, the natural conclusion is that “profit” in Article 96 must be construed as meaning the profit as ascertained by the generally accepted accounting principle applied by the company in the preparation of its accounts from time to time. The whole purpose of accounts is to show the financial position of a company, including its profits and its assets and liabilities. It would be surprising if the word “profit” in the Articles of Association dealing with dividends were to bear a different meaning from the profit as ascertained from the company's accounts. In our judgment, it would require some clear wording to conclude that “profit” for the purposes of distributions under Article 96 was to be ascertained using a different accounting principle from that used for the preparation of the company's financial accounts.”

(emphasis added).

We entirely agree with this reasoning, and the conclusion.

- 48 As already stated the parties are agreed that on this interpretation the \$225.8m revaluation profit is a “profit”; the parties are also agreed that it is a “profit ... available for dividend”.
- 49 That leaves the remaining question whether it is a “profit of” the relevant financial year, namely the year to 31 December 2005. We have given this question careful consideration in the light of the judgment given by the Royal Court, and the arguments addressed to us, but we have reached the clear view that the revaluation profit of \$225.8m is not a profit of 2005.
- 50 The natural meaning of the “profit of” a period is the profit earned or made during that period. Since there are different ways of assessing the profits made during a period, the question emerges as to how the profits attributable to a particular period are to be ascertained. In our judgment however this question is not difficult to answer. It is accepted that the “profits” of JY for the purpose of Article 96 are to be ascertained by reference to the generally accepted accounting principle applied by the company in the preparation of its accounts from time to time. But once this has been accepted (as we have said in our view rightly), then the natural answer to the question “which of those profits as so ascertained are attributable to the year 2005?” is “the profits which, in accordance with the generally accepted accounting principle adopted by the company for that year, are to be regarded as profit of that year.” In other words if one looks (as we agree one does) to the accounting principles in fact adopted by the company for the year in question to ascertain what profits the company made, it seems to us to be obvious that one should also look to the same accounting principles to ascertain which of those profits are to be regarded as made by the company in the year in question.
- 51 Indeed the reasoning of the Royal Court for adopting their interpretation of the word “profits” (in paragraph 52 of their judgment, set out above) applies in our view with equal force to the interpretation of the phrase “profits of that year”. This can be seen by reproducing the passage replacing references to “profit” with “profits of that year”:-

“In our judgment, the natural conclusion is that “profit[s of that year]” in Article 96 must be construed as meaning the profit[s of that year] as ascertained by the generally accepted accounting principle applied by the company in the preparation of its accounts from time to time. The whole purpose of accounts is to show the financial position of a company, including its profits [of the year] and its assets and liabilities. It would be surprising if the word[s] “profit[s of that year]” in the Articles of Association dealing with dividends were to bear a different meaning from the profit[s of that year] as ascertained from the company's accounts. In our judgment, it would require some clear wording to conclude that “profit[s of that year]” for the purposes of distributions under Article 96 was to be ascertained using a different accounting

principle from that used for the preparation of the company's financial accounts.”

52 In our judgment therefore the natural meaning of the phrase “profits of that year” in Article 96 is “profits of that year as ascertained by the generally accepted accounting principle applied by the company in the preparation of its accounts from time to time.”

53 We do not think there is any doubt about what the profits of the year are as ascertained by the IFRS basis of accounting in fact adopted by JY for 2005. The profits of the year are shown on the Income Statement where there is found the line:-

(LOSS) / PROFIT FOR THE YEAR

US\$ (2,082,149)

(Advocate Baker confirmed in answer to a question that he was not suggesting that there is any difference between the profits “of” a year and the profits “for” a year).

54 We agree that the \$225.8m revaluation profit is treated by IFRS as a profit; and shown as a profit in the 2005 accounts. But it is not treated as a profit for 2005. This is particularly stark when considering the way in which the \$19.5m, which makes up part of the \$225.8m revaluation profit, is treated. As explained above this is the increase in the fair value of the investments between 1 January 2004 and 31 December 2004. It therefore appears in the Income Statement, as one would expect, as part of the profit for the year 2004 (as restated); and, as also explained above, it forms part of the \$54.5m shown as profit for the year (that is for the year 2004) in the Statement of Changes in Equity. This makes it abundantly clear that the 2005 accounts drawn up on the IFRS basis do not treat the \$19.5m as a profit of 2005; they treat it as a profit of the (restated) year 2004. The same applies to the prior period adjustment of \$206.3m shown in the Statement of Changes in Equity: we consider it clear that the 2005 accounts do not treat this as a profit of 2005 – it is an adjustment in relation to years before 1 January 2004.

The relevant accounting principles

55 We were helpfully taken through the relevant accountancy standards. These demonstrate that the way in which the revaluation profit was dealt with in the 2005 accounts was entirely in accordance with the relevant standards, and that the 2005 accounts were correct in not showing it as a profit for the year. The relevant provisions are as follows:-

(i) The IFRS Framework for the Preparation and Presentation of Financial Statements provides (at paragraph 74) that the definition of income encompasses both revenue and gains; and (at paragraph 76) that this includes unrealised gains, for example those arising on the revaluation of marketable securities.

(ii) International Accounting Standard 1 (IAS 1), which covers the Presentation of Financial Statements, provides, under the heading “Profit or loss for the period”, as

follows:-

“78 All items of income or expense recognised in a period shall be included in profit or loss unless a Standard or an Interpretation requires otherwise.

79 Normally, all items of income and expense recognised in a period are included in profit or loss. This includes the effects of changes in accounting estimates. However, circumstances may exist when particular items of profit or loss may be excluded from profit or loss for the current period. IAS 8 deals with two such circumstances: the correction of errors and the effect of changes in accounting policies.”

(iii) IAS 1 further provides (at paragraph 96) for the presentation of a statement of changes in equity showing:-

“(a) profit or loss for the period and

...

(d) for each component of equity, the effects of changes in accounting policies and corrections of errors recognised in accordance with IAS 8”

and (at paragraph 100) as follows:-

“IAS 8 requires retrospective adjustments to effect changes in accounting policies, except when the transitional provisions in another Standard or an Interpretation require otherwise. IAS 8 also requires that restatements to correct errors are made retrospectively, to the extent practicable. Retrospective adjustments and retrospective restatements are made to the balance of retained earnings, except when a Standard or an Interpretation requires retrospective adjustment of another component of equity. Paragraph 96(d) requires disclosure in the statement of changes in equity of the total adjustment to each component of equity resulting, separately, from changes in accounting policies and from corrections of errors. These adjustments are disclosed for each prior period and the beginning of the period.”

(iv) International Accounting Standard 8 (IAS 8), which covers Accounting Policies, Changes in Accounting Estimates and Errors, provides (at paragraph 19) that an entity shall account for a change in accounting policy resulting from the initial application of a Standard in accordance with the specific transitional provisions, if any, in that Standard, and if there are no such specific transitional provisions retrospectively. Paragraph 22 provides:-

“Subject to paragraph 23, when a change in accounting policy is applied retrospectively in accordance with paragraph 19(a) or (b), the entity shall adjust the opening balance of each affected component of equity for the earliest prior period presented and the other comparative amounts disclosed for each prior

period presented as if the new accounting policy had always been applied.”

(v) The relevant Standard here is International Accounting Standard 39 (IAS 39), which covers Financial Statements: Recognition and Measurement. This does contain specific transitional provisions (at paragraph 104) as follows:-

“This Standard shall be applied retrospectively except as specified in paragraphs 105–108. The opening balance of retained earnings for the earliest prior period presented and all other comparative amounts shall be adjusted as if this Standard had always been in use unless restating the information would be impracticable.”

56 There was no dispute that the 2005 accounts had been correctly drawn up in accordance with these standards. The standards draw a distinction between income recognised in a period and profit for a period. Normally all income recognised in a period is to be included in profit for the period (IAS 1 paragraph 78) but there are exceptions where particular items of income may be excluded from the profit for the current period (IAS 1 paragraph 79). One particular example is where IAS 8 requires the effect of changes in accounting policies to be shown by making retrospective adjustments to prior periods (IAS 8 paragraphs 19, 22), which is the case here (IAS 39 paragraph 104). In such a case the gain is not recognised in the profit or loss for the period, but is recognised by way of a retrospective adjustment to the balance of retained earnings shown in the Statement of Changes in Equity (IAS 1 paragraphs 96(d), 100).

57 To our minds what this demonstrates with complete clarity is that the \$225.8m revaluation profit, although a “gain” and hence “income” and (correctly) recognised as such in the 2005 accounts, was (equally correctly) not treated as “profit for the period”, and hence not shown as such in the Income Statement for the year. It appears instead in the Statement of Changes in Equity where it is shown as a retrospective adjustment to prior years.

58 It follows that if, as we have suggested, the natural meaning of the words “profits of that year” in Article 96 is “profits of that year as ascertained by the generally accepted accounting principle applied by the company in the preparation of its accounts from time to time”, then the \$225.8m revaluation profit is not a profit of 2005.

Commercial common sense

59 In accordance with the principles we have summarised above, however, the Court is entitled to reject this interpretation and prefer another if that other is more commercially sensible or consistent with business common sense. It is therefore necessary to consider whether there is anything in the admissible background or the commercial consequences which would cause us to depart from the natural meaning of the language.

60 We do not consider there is. The admissible background is, for the reasons explained

above, severely limited. Other than that which is apparent from the Articles themselves, and evidence admitted to explain matters referred to in them, the admissible evidence is restricted to that which every reader of the Articles would reasonably be expected to know. What the reader of the Articles would see is that Article 96 had been amended to provide for a mandatory distribution of 75% of the profits of each year. We do not see anything in this which would cause the reader to conclude that the profits of the year should be anything other than the profits of the year in question as shown in the relevant accounts.

- 61 It is true that the effect of the change from the historical cost basis to the IFRS basis is that the revaluation profit is not caught by Article 96. If it is not a profit of 2005 for Article 96 purposes, it will not be a profit of any year for Article 96 purposes. This was a consideration which weighed with the Royal Court. But in our judgment it cannot displace the natural meaning of Article 96 unless it produces such an unreasonable result as to enable the Court to conclude that it cannot have been intended. We do not consider that it does. It is only if one starts by assuming that the purpose of Article 96 is to catch all profits thereafter recognised that there is anything unreasonable or uncommercial in the result that certain profits are not caught by it. But Article 96 itself does not give any reason for thinking that the purpose of the provision was to catch all profits not already recognised. All that one can derive from Article 96 is that the purpose is to impose a mandatory dividend of 75% of the profits of each financial year. If, in accordance with the generally accepted accounting principles adopted by JY for the year in question there is no such profit, there does not seem to us to be anything uncommercial or unreasonable in the conclusion that no mandatory dividend is payable.
- 62 Trilogy's complaint is actuated by the understandable desire of the three sisters associated with Trilogy to have as much as possible of the profits of JY distributed to the charitable sub-trusts, including the three sub-trusts with which they are associated. We accept that the effect of not treating the \$225.8m revaluation profit as a profit of 2005 is that this sum will not be subject to the mandatory distribution provision of Article 96 and so will not (unless the directors of JY resolve otherwise, which they can do by a simple majority) be distributed to YT and hence down to the sub-trusts. But we do not consider that this can affect the construction of Article 96, for two reasons.
- 63 First, the particular terms of the compromise and of the Instrument of Appointment under which the dividends paid to YT on the shares in JY are paid on to the eight sub-trusts are not in our judgment admissible in construing the Articles as they would not be known to the reader of the Articles.
- 64 Second, even if the structure set up by the compromise were admissible to construe the Articles, all it would show is that it was agreed that certain minimum dividends would be declared. These dividends would then be available for charitable purposes in accordance with the terms of the eight sub-trusts. But we cannot conclude that this means that a construction which reduces the amount of mandatory dividends is for that reason uncommercial or contrary to business common sense. The entire economic interest in JY is held for the benefit of charity. To the extent that dividends are not declared, the profits of JY

will be retained in the company where they will ultimately benefit charity. The dividend policy therefore does not determine whether charity will benefit from the profits in the company, but only when it will do so. Subject to the requirements of Article 96, it is a matter for the directors of JY to determine when the profits are distributed. The effect of an interpretation of Article 96 under which the revaluation profit is not caught by the mandatory dividend provision is not therefore to deprive charity of such profits. It is to leave to the directors of the company the decision when to distribute such profits. We consider it impossible to regard this as so outlandish or uncommercial a result as to require some other interpretation to be placed on Article 96.

65 Thus although we accept that the effect of the change from the historical cost basis to the IFRS basis is that the revaluation profit is not, and will not be, brought into account for Article 96 purposes, this does not cause us to revise the view we have reached on the interpretation of Article 96.

66 It may be noted, although this does not affect the question of construction, that the change from the historical cost basis to the IFRS basis may in other respects lead to higher dividends being declared under Article 96 than would otherwise have been the case. This is for at least two reasons:-

(i) First, under the historical cost basis, there would be no profit in a year at all unless investments were sold, so that the directors could by choosing not to sell investments in effect prevent dividends being declared and postpone distribution almost indefinitely. Under IFRS however a profit will arise if the fair value of the investments rises in the course of a year, and a dividend will have to be declared whether or not investments have in fact been realised.

(ii) Second, fluctuations in market value may lead to dividends being declared even where the overall value of the investments remains unchanged over a period of two or more years. Suppose for example that the market value of investments is \$400m at the beginning of Year 1, falls to \$300m at the end of Year 1, and rises again to \$400m at the end of Year 2. Assuming no changes in investments and no other profits in the period, the profit for Year 1 will be nil, but the profit for Year 2 will be \$100m of which \$75m will be required to be distributed by Article 96 despite the fact that over the two years there has been no overall change in value. Under the historical cost basis there would have been no profit for either year.

67 What this second example illustrates is that the operation of Article 96, tied as it is to the profit for each financial year, will not necessarily result in the distribution of 75% of the cumulative profits over a longer period. Similarly, for the reasons we have given, the fact that Article 96 does not catch the revaluation profit as it is not a profit of 2005 does not mean that what we regard as the natural meaning of Article 96 should be displaced or distorted to avoid this result. It is simply another consequence of the fact that Article 96 is tied to the profits of each financial year and this necessarily requires the profits of a year to be ascertained. We see no reasonable alternative to those profits being ascertained as the

profits which are recognised as the profits of the year in question in accordance with the generally accepted accounting principles in fact adopted by the company for the year.

68 There is one other point we should deal with. Advocate Baker submitted that the Royal Court had had the advantage of seeing the expert witnesses give evidence and that since they had said (see paragraph 46 of the judgment below) that the evidence of Mr Drennan was to be preferred, we should be slow to substitute our own view. We do not consider this is right. The evidence of the expert witnesses was, as we have said, very helpful in explaining to the Court the technical aspects of the way in which the accounts were drawn and the matters which were and were not agreed. Where they differed was in their understanding of what Article 96 required. We agree with Advocate Journeaux that in this part of their evidence they were giving the Court their own views of how Article 96 was to be interpreted. This was again no doubt a helpful exercise in enabling the Court to choose between the rival interpretations. But it is trite law that questions of construction are questions of law for the Court, and in the end the views of the witnesses, however eminent, could not be determinative. On an appeal raising a question of construction, the Court of Appeal will no doubt, as in all matters of law, give careful consideration to the views expressed by the Court below, but it must itself decide what as a matter of law the relevant words mean.

Conclusion

69 For the reasons we have given, in our judgment the proper meaning of the words “profits of that year” in Article 96 of the Articles of Association of JY is “profits of that year as ascertained by the generally accepted accounting principle applied by the company in the preparation of its accounts from time to time.” For the year 2005, there were no such profits and there was therefore no mandatory dividend required by Article 96. It is for these reasons that we allowed Mrs C's appeal.

70 At the end of their judgment the Royal Court added a postscript (paragraphs 142 to 145) pointing out that all the assets which were the subject of the case were destined ultimately for charitable purposes, that the litigation would have incurred enormous legal and accountancy costs and that to the extent that any costs were paid out of the assets it would mean that money intended for charitable causes would have been diverted into the hands of lawyers and accountants. They urged the parties to put litigation behind them.

71 We agree. Although we have allowed Mrs C's appeal, we unhesitatingly endorse the views expressed by the Royal Court. We are conscious that all that has been determined so far in this litigation is a preliminary issue and that other issues remain between the parties, but we cannot believe it is in the interests of charity for this litigation to continue.

ANNEX TO JUDGMENT

(all figures in \$)

Accounts for y/e:	31.12.02	31.12.03	31.12.04	31.12.04 (restated))	31.12.05
Balance sheet					
Investments (at cost)	56,196,234	41,501,659	41,501,659		
Investments (fair value)				267,316,443	285,834,237
Net assets	271,628,590	284,897,081	239,974,552		463,705,092 ₂
Total assets				470,026,633	465,362,708
Represented by					
Share capital	474,834	474,834	474,834	474,834	474,834
Unappropriated profits	271,153,756	284,422,247			
Retained earnings			239,499,718	465,312,407	358,725,572
Other reserves					104,504,686
Profit and loss account	Income Statement				
Profit (Loss) for the Year	15,824,836	15,068,491	35,077,471	54,541,896	(2,082,149)
Unappropriated profits / retained earnings b/f	256,628,920	271,153,756	284,422,247	490,770,511 ₁	
Proposed dividend	1,300,000	1,800,000	80,000,000	80,000,000 ₁	-
Unappropriated profits / retained earnings c/f	271,153,756	284,422,247	239,499,718	465,312,407 ₁	
Notes to accounts					
Market value / fair value of investments	192,060,995	247,849,923	267,314,348		

1 These figures are not shown in the Income Statement but in the Statement of Changes in Equity.

2 This figure is not shown as such but is Total Assets less Liabilities.