A Ltd v D and H and K

Jurisdiction:	Jersey
Judge:	J. A. Clyde-Smith, Jurats Fisher, Crill
Judgment Date:	05 February 2014
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Date:	05 February 2014

Text

[2014] JRC 32

ROYAL COURT

(Samedi)

Before:

J. A. Clyde-Smith, **Esq., Commissioner and**Jurats Fisher**and**Crill.

IN THE MATTER OF THE REPRESENTATION OF A LIMITED AS TRUSTEE OF THE B TRUST

AND IN THE MATTER OF THE TRUSTS (JERSEY) LAW 1984 AS AMENDED

Between
A Limited
Representor
and
D

First Respondent
H

and

Second Respondent
K

and

Third Respondent

Advocate E. B. Drummond **for the Representor**.

Authorities

Re S Settlement 2001/154 .

Freeman v Ansbacher [2009] JLR 1 .

Lewin on Trusts 18th edition.

Trust — decision of the trustee in relation to sale of investments blessed by the Court.

THE COMMISSIONER:

1 On 11 th December, 2013, the Court blessed a decision made by the representor ("the trustee") as trustee of the B Trust dated 14 th August, 2003, ("the Trust") in relation to the sale by its wholly owned company I Limited ("I") of investments it has in commercial real estate in Germany.

2 The Trust is a discretionary trust settled under Jersey law. The settlor was Miss S who apart from executing the trust deed and two letters of wishes in January and August 2003 respectively has not communicated with the trustee. The beneficiaries of the Trust are the three respondents namely H, his wife K and their son D.

3 I has minority interests in seven companies (referred to as "the M companies") which in turn own commercial real estate in Germany financed by loan facilities from Nationwide Building Society ("Nationwide"). In addition to its minority shareholdings, I has the benefit of shareholder loans made to the M companies which are interest free, limited in recourse and are payable only on a sale of the German properties or the property holding companies.

4 The M companies are managed and administered from Guernsey by a company known as

C Limited (“C”). Financial information on the M companies is produced by Mr BS of the English firm of chartered certified accountants SG & Co. The trustee does not know the identity of the ultimate beneficial owners of the remaining majority shareholding in the M companies save that it believes one of the other ultimate shareholders is Mr BS's brother, Mr HS.

5 The book value of I's investment in the M companies is €2,856,000. SG & Co estimate the current value to be €1,368,946.

6 In or around May 2008, the trustee became aware that H and D were being prosecuted by the Revenue and Customs Prosecution Office in England in relation to an alleged VAT fraud thought to involve hundreds of millions of pounds. In or around June 2011, H was found not guilty and D was convicted and sentenced to seventeen years in prison.

7 Individuals at Grant Thornton UK LLP have been appointed as management receivers for D and the trustee has received advice that restraint and receivership orders made in respect of D do not prevent it from dealing with and/or liquidating the trust assets as it sees fit but nevertheless, Grant Thornton and the Crown Prosecution Service have expressed the opinion that the assets of the Trust are derived from the proceeds of crime.

8 Since April 2013, the trustee has been subject to a *“no consent”* letter from the Jersey Financial Crimes Unit, the effect of which is that (amongst other things) the Trust is not permitted to make any *“dispersal or distribution of assets”* without the specific prior consent of the JFCU.

9 On 16 th October, 2013, C wrote to I stating that the loan facilities for all the syndicated portfolios of the M companies were due to expire on 31 st December, 2013, and that the existing lender, Nationwide, did not wish to renew the facilities.

10 C further stated that securing alternative re-financing was likely to prove difficult if I remained a shareholder for two reasons:–

(i) Any new bank carrying out due diligence would be likely to identify the connection (via I) to D (and his conviction for fraud) and may be unwilling to lend as a result.

(ii) There is likely to be a shortfall between any new lending and the amount required to repay Nationwide. A further investment is needed from shareholders. This is likely to prove impossible for I.

11 Accordingly, C believed it was necessary for I's shareholding to be redeemed before any such re-financing could succeed. It said that if no re-financing is carried out, it appeared unlikely that the Nationwide facility could be repaid. If Nationwide enforced its security and

sold the underlying German properties in a *"fire sale"* scenario, there may be no equity left for other creditors or shareholders, including I, all of whom may lose the entirety of their investment. The situation, it said, had to be resolved urgently, to allow sufficient time for the re-financing to complete before the year end.

12 In that letter and subsequent correspondence during October and November 2013, C have made the following offers:–

> (i) That I's minority shareholdings in the M companies would be purchased and its shareholder loans would be deemed repaid by the boards of each of the seven holding companies for a total payment of €500,000 ("First Offer").
>
> (ii) That I provide additional funding of £1,862,232 as part of a re-financing package, with a view to facilitating an offer of re-financing provided by an unnamed German bank, and on the basis that the beneficial ownership of D can somehow be resolved ("Second Offer").
>
> (iii) The boards of each of the M companies would buy back the shares issued to I at a nominal value, with the shareholder loans outstanding to I to remain in place alongside the other existing shareholder loans in the M companies ("Third Offer").

13 The deadline to respond to these offers was set at 6 th December, 2013, but later extended.

14 As to the First Offer on 7 th October, 2013, the trustee was aware of the potential conflict of interest involving SG & Co (through Mr BS's brother) in relation to the proposed sale of the I shareholdings in the M companies. The trustee has sought, but has not been able to obtain, independent valuation evidence and/or advice in the time available.

15 Nevertheless, even based on SG & Co's calculation of the present value of I's investment, an offer of €500,000 would appear to represent a significant discount. It appears that, in making the First Offer, C did not dispute the valuation of I's shareholdings in the M companies at approximately €1,368,946. C has instead applied a "risk discount" of between 60–68% to reflect the likely complete loss of value if an overall re-financing package is not possible.

16 The Second Offer requires I to provide additional funds to re-finance which, even if it were minded to accept, neither it nor the Trust has.

17 The Third Offer requires I to surrender its shareholdings for nominal value, retaining only an interest in the companies by way of shareholder loans. Were I to relinquish its shareholdings, it would lose its equity stake in the companies and, consequently, any standing or control that it can exert as a minority shareholder. Accordingly, unless there could be a significant negotiation in relation to this offer (for example, converting I's

shareholder loans into facilities for a fixed amount, repayable on fixed terms), this option as currently framed appeared commercially unattractive to the trustee.

18 On 4 th December, I also wrote to C to give an initial response to the offers. The letter made clear to C that I had reserved a court date on 11 th December at 10am to seek guidance from the Court and was canvassing the views of the beneficiaries and the authorities in the meantime. In the letter, I set out the reasons why the Second Offer was considered not viable and the Third Offer was viewed as commercially unattractive. In relation to the First Offer, I set out its considerable reservations and expressed the view that the Court would be unlikely to sanction a compromise for €500,000 since this would appear to significantly undervalue the value of the asset in question.

19 Despite risks which exist for I, the trustee noted that the risks are, in reality, greater for the other shareholders in the M companies and, in those circumstances, I would arguably be justified in seeking a premium for a sale of its interests, not a discount. Accordingly, I invited C to put forward its best offer by no later than 5pm, 6 th December, 2013, in relation to which (if forthcoming) the trustee would endeavour to seek input from the beneficiaries and authorities before seeking the blessing of the Court.

20 On 5 th December, 2013, C wrote to I to give notice that *inter alia* it would be withdrawing its offer in the sum of €500,000 for I's interest in the M companies and threatening legal action against the directors and beneficial owners of I for damages equating to the value of the entire equity in shareholders' loans outstanding to all of the shareholders (with the exception of I) if the re-financing was jeopardised due to the risks posed by retaining I as a shareholder. However, by letter dated 6 th December, 2013, C agreed to keep its offer open until close of business on 12 th December, 2013, being the day fixed for the hearing of the trustee's application.

21 At the time of the hearing on 11 th December no response from C to I's letter of 4 th December, 2013, had been received.

22 Mr Drummond, for the trustee, submitted that the offers from C were predicated on a series of unproven factual assertions:–

(i) That the Nationwide facility of €58m is due to expire at the year end and that Nationwide is not prepared to renew;

(ii) That the involvement of D, a convicted criminal, as a discretionary beneficiary of the Trust which owns I would hinder or prevent a re-financing with a new (probably German) bank;

(iii) The value of the German properties as at 31 st September, 2013, is given in the material supplied to investors as €69m to €70m. C says the real present value is

lower, perhaps €63m.

(iv) There will be a €13m to €15m funding gap between repaying Nationwide the outstanding facility and any new bank lending, which will only be €45m or so.

(v) That if the facility is not re-financed, Nationwide will call a default and enforce its security by selling the underlying German properties, and this might result in a “fire sale” at a low price, resulting in no equity for investors.

23 When pushed as to how they have calculated the €500,000 First Offer, C have not disputed the valuation obtained by the trustee but have applied a “risk factor” discount of between 60 and 68% to reflect these and other risks. The First Offer is well below the current valuation of the investments. The trustee does not have the funds to accept the Second Offer. The Third Offer is not commercially acceptable without a re-negotiation of the terms, something which C is unwilling to do.

24 H and K now reside in Dubai. Service of the representation and the first affidavit of AS, a director of the trustee, had been effected on all three respondents and despite the short notice, all three have responded.

25 Bedell Cristin have received a letter from GBB dated 10 th December, 2013, confirming that the representation and enclosed papers had been forwarded to D at HMP LG, but due to the short notice, they had been unable to receive any instructions or give any advice to him. Accordingly, he could neither agree to the proposed application nor oppose it and therefore reserved his right to appeal any order of the Court pending the ability to consider the application with his legal representatives. On the same day, Bedell Cristin received an email from F, D's wife written on behalf of H and K, saying that they too had not had time to obtain legal advice on the representation and wished to reserve their rights to appeal any decisions made if necessary. H made the suggestion that D should be removed as a beneficiary of the Trust allowing the relevant parties to acquire the necessary funding from financial institutions without having the association of a convicted criminal and therefore eliminating the requirement for a fire sale of the shares.

26 In the light of these circumstances and the deadline imposed upon it, the trustee has made a decision to reject all three offers. The First Offer of €500,000 was the only offer capable of acceptance and, notwithstanding any doubts about the independence of the valuation, significantly undervalued I's investment. There was insufficient certainty in the view of the trustee about the circumstances of the re-financing to warrant a sale at such a discount. In order to build in an element of flexibility the trustee had also resolved to accept an offer, if made, of a purchase of the shareholdings held by I in the M companies for €1,368,946 or a sum within 10% of that figure. We will refer to this as “the decision”.

27 The trustee was not surrendering its discretion to the Court but seeking the Court's blessing of the decision. The application comes within the second category set out in *Re S*

Settlement 2001/154 namely where there is no real doubt as to the nature of the trustees' powers and the trustees have decided how they want to exercise them but because the decision is particularly momentous, the trustees wish to obtain the blessing of the Court for the action on which they have resolved and which is within their powers. Three questions have to be addressed. Is the Court satisfied that:–

(i) The trustee has in fact formed the opinion in good faith that the circumstances of the case render it desirable and proper for it to carry out the steps proposed?

(ii) The opinion which the trustee has formed is one at which a reasonable trustee properly instructed could have arrived?

(iii) The opinion at which the trustee has arrived has not been vitiated by any actual or potential conflict of interest which has or might have affected its decision?

28 It might have been argued that whether or not to accept the offers was a matter for the board of I; in this case, the board comprised two corporate directors which formed part of the A group of companies. I is nothing more than a holding company run and administered by the trustee for the purpose of holding the M shares and the interposition of this company between the Trust and the underlying investments may not eliminate issues which would otherwise arise as to the proper conduct of the trustee. In this case, the trustee has already been threatened by C if it refuses the offer and might arguably be exposed to action on the part of its beneficiaries (see *Freeman v Ansbacher* [2009] JLR 1 paragraph 6 of the headnote). There is support for trustees seeking Beddoes relief in respect of litigation involving companies owned by a trust in Lewin on Trusts 18th edition at paragraph 21–123. The reality here is that the trustee is not leaving the management of the affairs of I to independent directors and we regarded it as appropriate for it to seek the assistance of the Court and for the Court to give that assistance.

29 The Court was satisfied in relation to each of the questions formulated in *Re S*. The trustee found itself in difficult circumstances with commercial deadlines imposed upon it. It had done its best to consult the beneficiaries and its decision was manifestly reasonable. Accordingly the Court blessed it.