

## Nolan v. Minerva: Trustees and Dishonest Assistance

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#### Introduction

In Nolan v. Minerva Trust & Others [2014] JRC 078A, the Royal Court delivered a salutary reminder of the high standards by which professional service providers in Jersey will be judged, and the need for scrutiny, careful reflection and demonstrable independence when taking investment decisions. It also underlined the need to be robust, whatever pressure may be exerted, if there are (or should be) questions about the propriety of a transaction.

#### Background

The factual matrix underlying the claim was complex, relating to eight investment transactions that took place between 2005 and 2006. The Plaintiffs, members of the Nolan family, alleged that they had been fraudulently induced to enter the investment transactions by an individual named Gerard Walsh. They alleged that this behaviour amounted to breaches of trust.

They further alleged that the Defendants, including Minerva (via a predecessor company, PTCL, with whom they had merged and, therefore, assumed liability for), had dishonestly assisted in these breaches of trust by complying with Mr Walsh's instructions to pay money away inappropriately as part of the transactions.

PTCL provided corporate administration services to Mr Walsh's companies, known as the Buchanan Group. Essentially, the Buchanan Group was involved in raising money, identifying investment opportunities, and holding and selling assets.

# Dishonest Assistance

## *First principles*

The Royal Court confirmed a number of principles relevant to dishonest assistance, which repay study in the context of trusteeship. In order to succeed in their claims, the Nolans had to establish:

- the existence of a trust in their favour;
- a breach of that trust;
- that PTCL assisted in that breach of trust; and
- that in rendering that assistance PTCL acted dishonestly.

## *The existence of a trust and breaches*

The nature of the relationship between Mr Walsh, the Buchanan Group companies and the Nolans, and the nature of the eight investment transactions, potentially gave rise to two types of implied trust:

- a "*Halley*" trust, which is a constructive trust arising where there is a "*contract or deal which itself is a vehicle to defraud*". There will be a breach of such a trust where there is a failure to disgorge the trust assets [footnote 1];
- a "*Quistclose*" trust, which is a type of resulting trust arising where money is advanced to a person exclusively for a specific purpose (so that it does not form part of the person's own general property). The trust subsists until the underlying mandate is fulfilled, and is breached if it is applied for other purposes [footnote 2].

Of the eight transactions in question, the Royal Court concluded that six gave rise to breaches of "*Quistclose*" trusts, one gave rise to a breach of a "*Halley*" trust and one amounted to a breach of both. In essence, money was paid away by the Buchanan Group companies in a manner that was inconsistent with the nature of the investment transactions as represented by Mr Walsh to the Nolans (and on which basis the Nolan's were induced to invest).

## *Assistance in that breach of trust*

In providing corporate administration services to the Buchanan Group companies, and in effecting the disbursement of monies in a manner that was inconsistent with Nolans' legitimate expectations, PTCL had assisted in the breaches of trust. The salient question was whether it has done so dishonestly.

## *Dishonesty*

The Royal Court confirmed a number of key principles, relevant in the context of professional service providers:

- honesty is judged by objective standards: *"[H]onesty is not an optional scale, with higher or lower standards according to the moral standards of each individual"* [footnote 3];
- an honest person should never behave recklessly: *"[N]or does an honest person deliberately close his eyes and ears, or deliberately not ask questions, lest he learn something he would rather not know, and then proceed regardless"* [footnote 3];
- honesty always requires careful judgment where matters are not straightforward: *"[A]n honest person would have regard to the circumstances known to him, including the nature and importance of the proposed transaction, the nature and importance of his role, the ordinary course of business, the degree of doubt, the practicality of the trustee or the third party proceeding otherwise and the seriousness of the adverse consequences to the beneficiaries"* [footnote 4];
- circumstances will dictate the honest course of action. This includes: (i) declining to act; (ii) asking further questions; and/or (iii) seeking professional advice;
- account must be taken of an individual's experience, intelligence and state of knowledge. However, *"it is not necessary that he should actually have appreciated that he was acting dishonestly; it is sufficient that he was"* [footnote 5];
- knowledge is judged cumulatively. If an honest trust officer would have made enquiries in relation to a prior transaction, which would then have influenced his/her actions in a later transaction, the two transactions are to be seen as a *"continuum"*.

In the context of professional service providers, the Royal Court accepted that a person's breach of his/her regulatory obligations and duties formed part of the relevant circumstances in determining whether there had been dishonest behaviour. The Royal Court reminded itself that in such situations a trustee's obligations included:

- to safeguard, properly segregate and identify trust assets (*per* Article 21 of the Financial Services (Jersey) Law 1998);
- to keep adequate records of customer money, so that the money can be identified, traced and reconciled (*per* Paragraph 2(1) of the Financial Services (Trust Company Business (Assets - Company Money) (Jersey) Order 2000 (the CMO));
- to ensure that, in any transaction, customer money is properly transferred with appropriate authority (*per* paragraph 6 of the CMO);
- to conduct its business with integrity, demonstrate that reasonable care has been taken, and maintain systems and procedures to protect customer assets (*per* the Trust Company Business Codes of Practice);
- to avoid any transfer of customer money where the trustee should suspect that it represents the proceeds of crime (Articles 32 and 33 of the Proceeds of Crime (Jersey) 1999).

Finally, the Royal Court emphasised the dangers of acting as a puppet for someone else in a transaction. This may have the effect of imputing the puppet-master's knowledge into the puppet. The puppet would then be judged as if he/she had the same knowledge as the puppet-master: *"[I]f a person allows himself to be the mere nominee of, and acts for another person, he must be bound by the notice which that other person for whom he acts has of the nature of the transaction ... a director acting in a transaction on the direction of a stranger is fixed with that stranger's knowledge of the nature of the transaction" [footnote 6]*.

This underlines the dangers of acting at the behest of a third party in relation to a transaction, without independent consideration of what is being proposed. A trustee who does so leaves themselves as a potential hostage to fortune regarding the third party's knowledge of the transaction. In this case, due diligence at the time had revealed no inherent concerns about Mr Walsh. He had the appearance at that stage of being a successful businessman although the reality was quite different.

## **Were the trustees dishonest?**

The key issue was whether PTCL's behaviour amounted to dishonest assistance in the breaches of trust. In all cases, except two of the Quistclose trusts, the Royal Court held that it did. The essence of the criticism was that PTCL had failed to bring *"independent judgment to bear as to whether any of the Nolan's investments was the right thing to do"*.

Some of the practical points raised were as follows:

- Certain inconsistency in information being provided by Mr Walsh should have been apparent and caused alarm bells to ring.
- Once the alarm bells were ringing, an honest trust officer should have undertaken further enquires regarding the source and purpose of the investment monies. This might have included demanding a full explanation of the inconsistencies and, absent such an explanation, not taking at face value any further information provided.
- An honest trust officer should embargo a transaction until his/her enquiries had been satisfactorily addressed. He/she should also report the transaction to the appropriate people.
- An honest trust officer should reflect independently on the commerciality of a transaction. For example, a disparity between the price paid for an asset historically and the price being proposed now might cause further enquiries to be undertaken.
- If there are concerns about the veracity of the information being provided by a party to a transaction, an honest trust officer should seek corroboration from other parties to the transaction.
- An honest trust officer should inform his/her colleagues of the concerns to preclude inadvertent approval of the transaction by someone else.
- An honest trust officer should look at client activities as a "*continuum*", in order to assess whether concerns in relation to a previous transaction should raise concerns in relation to a current transaction.
- More generally, if there have been concerns about the reliability of information provided in relation to one transaction, then an honest trust officer should proceed cautiously in relation to information provided by the same person in relation to different transactions.
- The fact that there are no reputational or KYC concerns about a client cannot justify a failure to act independently if it subsequently transpires that the client is not what he/she first seemed.

The Royal Court concluded in this case that failures in relation to the above were commercially unacceptable and amounted to dishonest assistance on the part of PTCL [footnote 7].

## Prescription

Article 57 of the Trusts (Jersey) Law 1984 (as amended) says that limitation periods (i.e. the time limits for commencing actions) will not apply for allegations of fraud and/or actions for the

recovery of trust property against trustees. However, the Royal Court has confirmed that those who engage in dishonest assistance are not themselves "*trustees*". Therefore, the provisions of Article 57 do not apply, rendering limitation a relevant consideration. In this regard, the Royal Court noted that a recent decision of the UK Supreme Court and the leading Jersey authority were consistent on the underlying principles [footnote 8].

The Royal Court also helpfully confirmed that the limitation period for claims of dishonest assistance is three years (not ten years). Again, it found English law persuasive. It held that the concept of dishonest assistance had been imported into Jersey law from English law, where it was considered analogous to economic torts such as deceit or knowingly procuring a breach of contract. A similar analogy was, therefore, to be drawn in Jersey, and the analogous torts are prescribed in Jersey after three years.

However, time would not run against a plaintiff if it was practically impossible for him/her to bring the claim (because, for example, he/she was ignorant of the cause of action). In essence, the Royal Court asked itself, applying well-established Jersey principles, whether ignorance of the cause of action was reasonable in all the circumstances.

The Royal Court concluded that the Nolans would not have had the information necessary to plead their claim until documents were disclosed to them pursuant to a Jersey injunction in 2010. The claim was brought in January 2011. Therefore, the Nolans were well within the time for bringing the claim.

## **Conclusion**

Clearly, the nature of the criticisms is instructive in highlighting generally how a trustee should and should not behave. As set out above, the behavioural threshold for a professional trustee in Jersey is high. Standards are set by a mixture of the common law, statute and regulation.

To a layman, the concept of dishonesty might be perceived as preserved for the realm of the criminal. However, a trustee's honesty is inextricably linked to its own professional standards, and a breach of those standards may bring questions of honesty very much into play.

Trustees may be concerned that this sets a dangerous precedent, imposing potentially draconian sanctions for getting decisions wrong. We anticipate that this may be a talking point in the industry. However, there is nothing new in the principles of honesty utilised by the Royal Court, or with the regulatory requirements that have been summarised. Judicial clarification that there is a nexus between them arguably acts only to confirm what must logically have always been the case (in terms of what the reasonable person might expect of a trustee). Exactly what sort of precedent this case will set, and whether it raises the stakes for

trustees, remains to be seen. However, in principle, we do not expect this case to erode the divide between carelessness and dishonesty, or between advertent and inadvertent actions.

It is also a timely reminder that professional duties and obligations subsist in the activities of Associate Directors, Managers and Administrators just as they do for the activities of Directors. The fact that a trust officer is not at the top of the food chain does not absolve him/her from the burden of those duties and obligations. That trust officer may have day-to-day management of the matter, putting them in a very important position.

So what headline points arise out of this judgment, which a trustee should keep in mind? The following is a non-exhaustive list:

- Understand your client, the business and the transactions they are undertaking. Think laterally and logically to ensure that it all makes sense. Think about the source and purpose of funds.
- Act diligently and ensure proper records are kept.
- However important, persuasive or intimidating the client is, do not act as a puppet. Exercising independent judgment is crucial.
- Trust your instinct. If something does not feel right then do not ignore it.
- Communicate appropriately - be it to your colleagues, superiors, MLRO or the Financial Services Commission. When faced with problematic situations a transparent approach is the best approach.

Finally, a prudent trustee might seek external advice on duties, obligations and risks in tricky situations. Being a trustee is a position which bears significant responsibility, out of which comes the pressure of difficult decisions. Often serious issues can be prevented through advice at an early stage. As this case demonstrates, prevention is far preferable to cure.

## FOOTNOTES

1. Halley v. The Law Society [2003] EWCA Civ 97.
2. Barclays Bank Limited v. Quistclose Investments Limited [1970] AC 567.
3. Royal Brunei Airlines v. Tan [1995] 2 AC 378 at page 389.
4. Ibid. pages 390 to 391.
5. Twinsectra v. Yardley [2002] 2 AC 164 at paragraph 121.

6. Selangor United Rubber Estates Limited v. Craddock [1968] 1 WLR 1555.
7. The other Defendants, who were individual directors, were held not to be liable personally for dishonest assistance.
8. Central Bank of Nigeria [2014] UKSA 10 and Bagus Investments Limited v. Kastening 2010 JLR 355.

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