Finance, Property and Business Litigation in a Changing World

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Organisers:

Finance, Property and Business Litigation in a Changing World

Plenary Session 2
Trusts and Proprietary Remedies

Chairperson

Mr Timothy Fancourt QC, *Falcon Chambers*

Speakers

The Honourable Judicial Commissioner
Vinodh Coomaraswamy, *Supreme Court of Singapore*

Professor Yeo Tiong Min SC, *School of Law,*
Singapore Management University

Mr Paul McGrath QC, *Essex Court Chambers*

PROPRIETARY REMEDIES AFTER *SINCLAIR V VERSAILLES*

PAUL McGRATH Q.C.
Essex Court Chambers

CHANCERY BAR
SINGAPORE ACADEMY OF LAW

PROPRIETARY REMEDIES IN FRAUD

- Litigation about commercial fraud increases in downturn in markets: Madoff, Stanford etc
- Availability of proprietary remedies crucial part of armoury of litigator
- In seeking to impose restrictions, CA decision in *Sinclair v Versailles* is disappointing
- Also sets English law on a different path

What did it decide?

- Rejected PC in *A-G of Hong Kong v Reid* in favour of CA in *Lister v Stubbs*
- "...a beneficiary of a fiduciary's duties cannot claim a proprietary interest, but is entitled to an equitable account, in respect of any money or asset acquired by a fiduciary in breach of his duties to the beneficiary, unless the asset or money [A] is or [B] has been beneficially the property of the beneficiary or [C] the trustee acquired the asset or money by taking advantage of an opportunity or right which was properly that of the beneficiary." per Lord Neuberger MR
- Need [A], [B] or [C] to be present for proprietary relief.

Paul McGrath Q.C., *Essex Court Chambers*

Ignores importance of fiduciary

- Status of Fiduciary diminished in commercial context: little more than technique to kick-start equity's rules on tracing or other relief e.g. thief
- Danger of losing sight of core value and importance of fiduciary: special relationships engendering a high degree of trust and confidence by one party in another
- CA in *Sinclair*: ascribed little or no value to the status of fiduciary: all about the relationship between claimant and asset
- Directly leads to requirements [A], [B] or [C]: unnecessarily complex factual inquiries

Paul McGrath QC, *Essex Court Chambers*

Ignores importance of fiduciary (2)

- **Better approach: all about the relationship between the Defendant Fiduciary and the asset:**
- **Directly leads to one question only: was the asset obtained in breach of the fiduciary duties**
- **If so, proprietary remedy: fiduciary not permitted to set up own wrongdoing to deny beneficiary's claim.**
- **P Millett:"Proprietary Restitution" in Degeling & Edelman, *Equity in Commercial Law***

  The defendant [in **Reid**] was a fiduciary. As Lord Templeman explained, a fiduciary must not make a profit for himself out of his fiduciary position. If he does, Equity insists on treating him as having obtained it for his principal; he is not allowed to say that he obtained it for himself. He must not accept a bribe. If he does so, Equity insists on treating it as a legitimate payment intended for the benefit of the principal; he is not allowed to say that it was bribe intended for himself."

Wrongly rejected precedent

- **HL in *Keech v Sandford***
  - ***not limited to leases***
  - ***Maitland's Lectures on Equity***
- **HL in *Boardman v Phipps***
  - CT over (innocent) secret commission
  - Inconsistent with no CT over dishonest bribe

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Wrongly accepted precedent

- **Little authority in supporting *Lister v Stubbs***
  - **One case cited**
- ***Metropolitan Bank v Heiron***
  - **No case cited in support**
  - **Contrary cases not cited**
- **Both employ language of remedial CT**

Paul McGrath QC, ***Essex Court Chambers***

Wrongly interpreted precedent

- "Revival" of HL ***Tyrrell v Bank of London*** (1862)
  - But no prop claim because unsold portion was irrelevant to the fiduciary relationship between Bank and solicitor.
- Misinterpretation of ***Paragon Finance*** and limitation cases

Paul McGrath QC, ***Essex Court Chambers***

Sinclair: retreat begins?

- ***FHR European Ventures LLP v Mankarious*** [2013] EWCA Civ 17
- It throws into clear relief, however, the very considerable difficulties inherent in the analysis in Sinclair Investments and the decision in Lister in marking the borderline between cases in Category 2 and those in Category 3. This has made the law more complex and uncertain and dependant on very fine factual distinctions. If the law is to be made simpler and more coherent, but Sinclair Investments and Lister correctly represent the law, then that suggests a need to revisit the very many longstanding decisions in Category 2 cases and to provide an overhaul of this entire area of the law of constructive trusts in order to provide a coherent and logical legal framework. If that can be done at all by the courts, rather than Parliament, it can only be accomplished by the Supreme Court. That indicates a need for informed debate and ultimately determination by the Supreme Court: (1) whether Sinclair Investments was right to decide that Lister is to be preferred to Reid ; (2) in terms of constructive trusts and proprietary relief for breach of fiduciary duty, what are the principles to distinguish opportunity cases within Category 2 and those within Category 3; (3) what is the true jurisprudential nature of the constructive trust in this (and by necessity other) areas of the law, including whether it is — or should be — an institutional trust at all or something else.

Paul McGrath QC, *Essex Court Chambers*

Sinclair: retreat begins?

- ***FHR European Ventures LLP v Mankarious*** [2013] EWCA Civ 17
- In considering those matters, there are important issues of policy, and the relative importance of different policies, to assess, including deterring fraud and corruption; the ability to strip the fiduciary of all benefits, including increases in the value of benefits, acquired by breach of duty, and vehicles or third parties through which those benefits have been channelled; the importance attached to the protection of those to whom fiduciary duties are owed; and the position of other creditors on the fiduciary's insolvency who may be prejudiced by a constructive trust or proprietary relief in favour of the fiduciary's principal but who, in the absence of such a trust and relief, would benefit from increases in value of assets acquired by the fiduciary's fraud, corruption or wrongdoing. It will also be necessary to bear in mind the international perspective applying to this area of trust law and equity, to which I have referred earlier in this judgment.

Paul McGrath QC, *Essex Court Chambers*

Sinclair: Australia rejects

- ***Grimaldi v Chameleon Mining*** [2012] Full Court of Fed Court of Australia
  - Inconsistent with Australian authority e.g. ***Hospital Products***
  - Reduced deterrent effect when needed most
  - Australia adopts a discretionary approach to CT
  - Australia's rejection of ***Lister*** consistent with other jurisdictions including Singapore

Sinclair:Singapore

- ***Sumitomo Bank Ltd v Kartika Ratna Thahir*** [1993] 1 SLR 735:

- ***Lister v Stubbs*** is:
  - (i) wrong;
  - (ii) would lead to "undesirable and unjust consequences";
  - (iii) inconsistent with the case law which preceded it;
  - (iv) Court of Appeal in ***Metropolitan Bank v Heiron*** took a wrong turning.

Sinclair:Singapore

– (v) inconsistent with the law relating to honest fiduciary liability to account for profit e.g. ***Boardman v Phipps;***
– (vi)does not reflect the mores and sense of justice of the Singapore community;
– (vii) not constrained by precedent and so free to reject it

Conclusions (1)

- Unsettled 15 years of common understanding
- Introduced complex fact-inquiries in relation to the source of assets.
- Undermining deterrent effect
- Poor analysis of principle/policy arguments although clearly influenced by insolvency

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Conclusions (2)

- Academic literature too readily ignored
- ***FHR European Ventures*** – glimmer of hope of re-assessment
- Otherwise:
  - ability to raise proprietary remedies significantly limited
  - (Unwelcome) Divergence between UK and other common law jurisdictions.

Paul McGrath QC, *Essex Court Chambers*

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A JOINT CONFERENCE OF THE SINGAPORE ACADEMY OF LAW AND THE CHANCERY BAR OF ENGLAND AND WALES

25 & 26 April 2013
Supreme Court
Singapore

PROPRIETARY REMEDIES AFTER *SINCLAIR V VERSAILLES*

PAUL McGRATH Q.C.

Essex Court Chambers

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Cross-Border Proprietary Remedies

Professor YEO Tiong Min SC
Singapore Management University

Common Law

- Preliminary questions:
  - Does the *lex fori* apply to all claims invoking the equitable jurisdiction?
  - If not, are equitable proprietary remedies matters of substance or procedure?
  - If substantive, what is the choice of law?

Common Law: Choice of Law

- Choice of law rule
  - Characterisation (what is the issue?)
  - Connecting factor (which legal system to apply?)
  - Applicable law (content of the law to be applied)
  - Any overriding forum law? (mandatory rules and fundamental public poliy)

TM Yeo, *SMU*

Deconstructing the Constructive Trust

- *Grupo Torras SA v Al-Sabah* [2001] CLC 221 (CA):
  - … determination of the applicable law depends not on the cause of action but on the particular issue in dispute (at para 121)
  - … "constructive trust' and 'constructive trustee' are terms which are often imprecisely used, or misused. The basis of liability in a case of knowing receipt is quite different from that in a case of dishonest assistance. One is a receipt-based liability which may on examination prove to be either a <u>vindication of persistent property rights</u> or a <u>personal restitutionary claim based on unjust enrichment</u> by subtraction; the other is a <u>fault-based liability</u> as an accessory to a breach of fiduciary duty. (At para 122, emphasis added)

TM Yeo, *SMU*

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Types of "constructive trust" liabilities

- Equitable accounting (personal remedy): (restoration/compensation)
- Obligation to transfer property v. beneficial interest in property
  - "… equity has proved that from the materials of obligation you can counterfeit the phenomena of property": SFC Milsom, *Historical Foundations of the Common Law* (2nd edn, 1981) at p 6.

TM Yeo, *SMU*

Tripole Trading Ltd v Prosperfield Ventures Ltd (2006) 9 HKCFAR 1

- Claim by company against third party purchaser of company assets (shares in PRC company) sold by directors allegedly in breach of fiduciary duty – PRC company subsequently restructured by provincial government
- Claimant "alleging alleging a constructive trust imposed upon the property on account of the circumstances in which it was obtained"
- Characterised as raising ***property*** issue:
  - governed by *lex situs* of the property at time of receipt (place where the company was registered and share register kept) – defendant obtained good title under that law

TM Yeo, *SMU*

First Laser Ltd v Fujian Enterprises (Holdings) Co Ltd [2012] HKCFA 52

- Claim by purchaser of shares (in PRC company) against vendor <u>for the shares</u> when sale agreement turned out to be void under its proper law (PRC) after purchase price was paid
- Characterised as raising <u>restitutionary *obligation*</u> issue
  - governed by proper law of the restitutionary obligation (ie, proper law of the underlying contract)
  - "constructive trust" may be imposed where obligation under foreign law is analogous to fiduciary obligation

TM Yeo, *SMU*

Thahir v Pertamina [1994] 3 SLR(R) 312

- Bribe received by employee in Singapore and placed in wife's bank account
- Interpleader proceedings: Employer, estate of employee and wife of employee
- Trial on employer's claim against wife of employee
- Court accepted that employer needed to show *proprietary* entitlement to money
- Issue characterised as <u>restitutionary *obligation*</u> (place of receipt - Singapore)

TM Yeo, *SMU*

Conclusion on common law

- No single choice of law rule
- Need to characterise the <u>issue in dispute</u>
- "Constructive trust" claims may raise:
  - Property issues (title, priorities)
  - Obligation issues
    - Equitable accounting
    - Obligation to transfer property (contract, wrong, unjust enrichment, other personal equities)

TM Yeo, *SMU*

Other Fora

- Australia – possibly no choice of law for equitable remedies
- UK: additional considerations -
  - Rome I Regulation (contractual obligations)
  - Rome II Regulation (non-contractual obligations)
  - Hague Trusts Convention (as extended to trusts declared by judicial decisions)
- HK SAR: additional consideration -
  - Hague Trusts Convention (as extended to trusts declared by judicial decisions)

TM Yeo, *SMU*

Rome I & II

- Rome I (contractual obligations)
  - Does not apply to the constitution of trusts or the relationship between settlors, trustees and beneficiaries
- Rome II (non-contractual obligations)
  - Does not apply to voluntary trusts or the relationship between settlors, trustees and beneficiaries
  - Unjust enrichment
  - wrongs

TM Yeo, *SMU*

Hague Trusts Convention

- Prevails over Rome I and Rome II in the UK
- Extended (UK and HK) to trusts arising from judicial decisions
- Not applicable to the creation of trusts
- Applies to content of duty of constructive trustee

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Finance, Property and Business Litigation in a Changing World

Concurrent Session 2A: Trust Litigation

Chairperson

Mr David Halpern QC, *4 New Square*

Speakers

Mr Francis Xavier SC, *Rajah & Tann LLP*

Mr Andre Maniam SC, *Wong Partnership LLP*

Ms Penelope Reed QC, *5 Stone Buildings*

Mr Christopher Tidmarsh QC, *5 Stone Buildings*

Archibald and Boris are trustees of a trust fund comprising shares in companies in the BVI held on discretionary trusts. They are the original trustees and are resident in Singapore. They have power to add beneficiaries. The trust deed says nothing about conflicts of interest. Archibald and Boris appoint Archibald as a beneficiary and appoint funds to Archibald absolutely. Archibald has spent the money on gambling and has minimal assets.

Patricia one of the beneficiaries threatens proceedings alleging that the appointment of and to Archibald should not have been made. Archibald has retired as a trustee and the new trustees are Boris and Catherine. Patricia intimates that she intends to sue Archibald, Boris and Catherine. Boris and Catherine apply to the court for directions whether they should defend the action and that they be permitted to defend it out of the trust fund. They join Patricia (but no other beneficiaries) as a defendant. Archibald applies for similar relief.

1. What are the chances of success in the action for breach of trust of:
   a. Archibald
   b. Boris
   c. Catherine?

2. What order or orders is the Court likely to make in the directions application?

Chancery Bar Association Singapore Conference: trustees' duties

1. The aim of this paper is to suggest some aspects of the duties of trustees that may be relevant to the breach of duty aspects of problem 1 of the trusts workshop.

2. First, the "no conflict rule". It is a fundamental rule of equity that trustees are not permitted to act if their personal interests conflict with their duties as trustees. (See for example *Lewin on Trusts* chapter 20.)

3. This is not an absolute rule however and can be excluded by an appropriate provision in the trust deed. It is less clear whether the rule can be excluded impliedly. This can be important where an original trustee has a personal interest in the exercise of a power. Has his original appointment impliedly authorized him to exercise the power despite his conflict? It is widely thought that there would be implied authority. **Sergeant v National Westminster Bank** (1990) 61 P&CR 518 (CA) is often quoted as support for this proposition. But some have argued that on analysis it may not be authority for such a wide proposition and in Scotland a contrary conclusion was reached: **Johnston v Macfarlane's Trustees** 1986 SC 298.

5. Secondly, the validity and scope of a power. It is settled that a power (or a trust) is valid if it is possible to say with certainty that a person is or is not a member of the class. This is subject to the power being administratively workable (**McPhail v Doulton** [1970] 2 All ER 228). A power (sometimes called "an intermediate power") permitting trustees to appoint anyone as a beneficiary except for a specified class has been held to be valid (see **Re Manisty** [1974] Ch 17): the trustees were permitted to exercise and could exercise the power in favour of anyone (other than the specified excepted class) but could be prevented from doing so "capriciously". These rules do

not assist in deciding the scope of a power. That will be determined by construction.

6. Thirdly, the remedies for breach of the conflict rule. Is the remedy merely to set the transaction aside or is equitable compensation available? In England compare: **Tito v Wadell** (No. 2) [1977] Ch. 106 at p. 2496 (the rule imposes a disability only) and **Gwembe Valley Development Co. Ltd. v Koshy** (No.3) [2004] 1 BCLC 131, para 104-108 (it is the duty of a trustee to obey the rule).

7. Fourthly, the duties of an incoming trustee. A new trustee is expected to investigate the trust provisions and dispositions made under them.

Christopher Tidmarsh QC
2 April 2013
5, Stone Buildings, Lincoln’s Inn, London WC2A 3XT.

<u>CHANCERY BAR ASSOCIATION SINGAPORE CONFERENCE: BEDDOE APPLICATIONS</u>

1. This paper is designed to provide some general background to problem 1 for the trusts workshop and deals with one issue raised by that scenario: namely in what circumstances trustees can seek Beddoe relief from the Court.

2. A Beddoe application is just a type of application for directions by trustees. Trustees and executors can always seek the directions of the Court in the event of doubt as to a particular course of action, or where they cannot agree or where they want the protection of the Court in respect of a decision which might be open to attack from the beneficiaries[1].

3. When seeking Beddoe relief, trustees seek the directions of the Court as to whether they should bring or defend

[1] See for example *Public Trustee v Cooper* [2001] WTLR 901

proceedings. The failure to apply for such an order, although perhaps unwise has been held not to be a breach of trust[2].

4. It is important that Beddoe applications are used in the right circumstances and they should never be made in the litigation itself. Consideration should always be given as to whether it is necessary to go to Court at all. If all the beneficiaries are adult and capable, then the trustee/personal representative should first of all consult them and see if they are prepared to offer an indemnity. Or in an appropriate case it might be preferable for the adult beneficiaries themselves to pursue or defend any litigation[3].

5. The best exposition of this jurisdiction can be found in the judgment of Lightman J in ***Alsop Wilkinson v Neary***[4] where he set out the categories of litigation in which trustees/personal representatives might be involved:-

> *(1) The first (which I shall call "a trust dispute") is a dispute as to the trusts on which they hold the subject matter of the*

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2 *Bonham v Blake Lapthorn Linnell* [2006] EWHC 2513 (Ch

3 *Re Evans* [1986] 1 WLR 101

4 [1996] 1 WLR 1220 at p. 1223

settlement. This may be "friendly" litigation involving e.g. the true construction of the trust instrument or some other question arising in the course of the administration of the trust; or "hostile" litigation e.g. a challenge in whole or in part to the validity of the settlement by the settlor on grounds of undue influence or by a trustee in bankruptcy or a defrauded creditor of the settlor, in which case the claim is that the trustees hold the trust funds as trustees for the settlor, the trustee in bankruptcy or creditor in place of or in addition to the beneficiaries specified in the settlement. The line between friendly and hostile litigation, which is relevant as to the incidence of costs, is not always easy to draw: see <u>In re Buckton; Buckton v. Buckton</u> *[1907] 2 Ch. 406.*

(2) The second (which I shall call "a beneficiaries dispute") is a dispute with one or more of the beneficiaries as to the propriety of any action which the trustees have taken or omitted to take or may or may not take in the future. This may take the form of proceedings by a beneficiary alleging breach of trust by the trustees and seeking removal of the trustees and /or damages for breach of trust.

(3) The third (which I shall call "a third party dispute") is a dispute with persons, otherwise than in the capacity of beneficiaries, in respect of rights and liabilities e.g. in contract

or tort assumed by the trustees as such in the course of administration of the trust.

6. It is in respect of this latter type of dispute that the trustees/personal representatives will apply to the court under this jurisdiction. Trustees are of course entitled to an indemnity from the fund for their costs but the objective in obtaining Beddoe relief is to ensure that no beneficiary can complain that their costs were incurred unnecessarily. The application should always be brought in separate proceedings.

7. However, while this represents the traditional limits of Beddoe relief there is some sign at least outside England and Wales of its extension. In *Macedonian Orthodox Community Church St Petka Incorporated v His Eminence Petar The Diocesan Bishop of The Macedonian Orthodox Diocese of Australia and New Zealand*[5] the High Court of Australia considered that the legislation providing for applications akin to Beddoe applications did not prevent trustees against whom breaches of trust were alleged and removal sought seeking the direction of the Court and indeed allowed them to take their costs from the fund. However, the case turned very much on the fact that the true dispute was as to the terms of the trust

[5] [2008] HCA 42

and it was in the interests of the trust that was resolved, the trust was charitable and not private and that the Judge hearing the application had a discretion with which the Court of Appeal ought not to have interfered.

8. One of the oddities about Beddoe applications is that the Court is presented with privileged information including usually the Opinion of Counsel obtained by the Trustees as to the merits of the main claim. If the litigation involves one of the beneficiaries then the claim form can be expressed in general terms and any privileged material should be exhibited to the statement of the claimants and not served on him. The beneficiary can be excluded from all or any part of the hearing.

9. However, a word of considerable warning. A Beddoe application ought to be a relatively cheap way of obtaining the directions of the Court. In the recent case in England of *Howell v Lees--Millais*[6] which involved an unsuccessful appeal by trustees from a costs order which followed a Beddoe application there were strong words from the Master of the Rolls:-

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[6] **[2011] EWCA Civ 786**

“In Re Beddoe, Downes v Cottam [1893] 1 Ch 547, a trustee was refused permission to take his costs out of the trust in relation to certain proceedings in which he had taken part on behalf of the trust and had been unsuccessful. In justifying that refusal, Lindley LJ referred at [1893] 1 Ch 547, 558 to "the ease and comparatively small expense with which trustees can obtain the opinion of a Judge of the Chancery Division on the question of whether an action should be brought or defended at the expense of the trust estate". To the same effect, Bowen LJ mentioned at [1893] 1 Ch 547, 562 the "inexpensive method" available to a trustee who "is doubtful as to the wisdom of pursuing or defending a lawsuit".

The possibility that an application of that type would involve well over twelve days of court time, would require more than 3,000 pages of evidence, would take some five years (or more than eighteen months if one ignores the costs issue) to resolve, and would incur the parties in costs exceeding the equivalent of £1m in present day value, would have seemed inconceivable to those two experienced judges. This should never happen again. In expressing this view, I am not seeking to suggest any particular person is to blame. The Judge may have thought that the trustees carried a large proportion of the blame, but it would be unfair and inappropriate for us to express any view on the point.”

6 April, 2013

Penelope Reed QC, 5 Stone Buildings, Lincoln's Inn

SAL/ChBA Conference 2013

Panel Session 2A – Trust Litigation

The Singapore experience with Remedial Constructive Trusts and Resulting Trusts: no longer dependent on the length of the Chancellor's foot?

Equity and Discretion

In his 1689 publication, *Table-Talk* at 46, John Selden criticised the discretionary nature of equity in this famous passage:

> "Equity is a Roguish thing: for Law we have a measure, know what to trust to, Equity is according to Conscience of him that is Chancellor, and as that is larger or narrower, so is Equity. 'Tis all one as if they should make the Standard for the measure, we call a Chancellors foot; what an uncertain measure would this be? One Chancellor has a long Foot, another a short Foot, a third an indifferent Foot: 'Tis the same thing in a Chancellors Conscience."

Some 272 years later, however, Harman LJ expressed confidence that a body of well-known principles had been developed, for the exercise of equitable jurisdiction (*Campbell Discount Co. Ltd. v Bridge* [1961] 1 Q.B. 445 at 459):

> "Equitable principles are, I think, perhaps rather too often bandied about in common law courts as though the Chancellor still had only the length of his own foot to measure when coming to a conclusion. Since the time of Lord Eldon the system of equity for good or evil has been a very precise one, and equitable jurisdiction is exercised only on well-known principles."

Bagnall J's remarks in *Cowcher v Cowcher* [1972] 1 W.L.R. 425 at 430, some nine years later, were in similar vein:

> "I am convinced that in determining rights, particularly property rights, the only justice that can be attained by mortals, who are fallible and are not omniscient, is justice according to law; the justice which flows from the application of sure and settled principles to proved or admitted facts. So in the field of equity the length of the Chancellor's foot has been measured or is capable or measurement."

By Mr Andre Maniam
Wong Partnership LLP

Is Equity now a settled body of law, rather than a free exercise of discretion?

In *Lau Siew Kim v Yeo Guan Chye Terence* [2008] 2 SLR(R) 108 ("*Lau Siew Kim*") at [32], the Court of Appeal endorsed four primary perspectives which should guide the court in the development of equitable principles: (a) precedent; (b) principle; (c) policy; and (d) pragmatism. "Principled pragmatism," the Court stated (at [33]), "should be the key to the court's approach in the application of equitable principles."

An analysis of Singapore jurisprudence in the areas of remedial constructive trusts ("RCTs"), and resulting trusts, suggests that the development of principles (in these areas at least) is still underway.

Remedial Constructive Trusts

In *Carl-Zeiss Stiftung v Herbert Smith (No. 2)* [1969] 2 Ch. 276 at 300, Edmund Davies LJ said:

> "English law provides no clear and all-embracing definition of a constructive trust. Its boundaries have been left perhaps deliberately vague, so as not to restrict the court by technicalities in deciding what the justice of a particular case may demand."

Fitting chronologically between the views expressed by Harman LJ and Bagnall J (as quoted above), this sets the stage for the debate that has continued to date, as to the basis (or bases) on which a constructive trust might be imposed.

In the House of Lords' decision in *Westdeutsche Landesbank Girozentrale v Islington LBC* [1996] A.C. 669 ("*Westdeutsche*") at 714−715, Lord Brown-Wilkinson drew the following distinction between an institutional constructive trust and an RCT:

> "Under an **institutional constructive trust** the trust arises by <u>operation of law</u> as from the date of the circumstances which give rise to it: the function of the court is merely to declare that such trust has arisen in the past. The consequences that flow from such trust having arisen (including the possibly unfair consequences to third parties who in the interim have received the trust property) are also determined by rules of law, not under a discretion. A **remedial constructive trust**, as I understand it, is different. It is a judicial remedy giving rise to an enforceable equitable obligation: the extent to which it operates retrospectively to the prejudice of third parties lies in <u>the discretion of the court</u>."
>
> [emphasis added]

The prospects of adopting the RCT as part of English law were, however, dimmed (if not extinguished altogether) by *Re Polly Peck International Plc (in administration) (No 2)* [1998] 3 All ER 812 ("*Polly Peck*"), and the cases which have followed it. In *Polly Peck* at 827, Mummery LJ said this in response to counsel's submission that "the law moves":

> "That is true. But it cannot be legitimately moved by judicial decision down a road signed "No Entry" by Parliament. The insolvency road is blocked off to remedial constructive trusts, at least when judge-driven in a vehicle of discretion."

To Nourse LJ, even if Polly Peck were solvent, the imposition of an RCT would not be seriously arguable (*Polly Peck* at 831):

> "…where, as here, there would be not simply a variation of proprietary rights but a variation of the manner in which the administrators are directed to deal with PPI's assets by the Insolvency Act 1986 it is not seriously arguable, even at the highest level, that a remedial constructive trust would be imposed. For myself, I would go further and hold that it would not be seriously arguable even if PPI was solvent. It is not that you need an Act of Parliament to prohibit a variation of proprietary rights. You need one to permit it; see the Variation of Trusts Act 1958 and the Matrimonial Causes Act 1973."

In Singapore, the seeds of RCTs have fallen on more fertile ground.

The various uses of the term "constructive trust" were reviewed in the High Court decision in *Panweld Trading Pte Ltd v Yong Kheng Leong and ors (Loh Yong Lim, third party)* [2012] 2 SLR 672 ("*Panweld*") (affirmed on appeal in *Yong Kheng Leong and anor v Panweld Trading Ptd Ltd and anor* [2013] 1 SLR 173), where the plaintiff company sued its director for breach of fiduciary duty, claiming that he had placed his wife on payroll and had paid her salaries over 17 years even though she was never an employee of the company. It was found that the wrongful payments had indeed been made, and the key legal issue was whether the claims against the director and his wife were time-barred. The provision under consideration was section 22(1) of the Limitation Act, which provided that no limitation period applied to an action by a beneficiary under a "trust" in certain situations.

In considering what "trust" in section 22(1) encompassed, the High Court distinguished between two classes of constructive trusts. "Class 1" included trusts that arose before the occurrence of the impeached transaction (*e.g.*, where a director, as trustee of the company's assets, misappropriates the assets), whereas "Class 2" included trusts which arose by reason of that transaction (*e.g.*, liability for dishonest assistance and knowing receipt). The High Court observed that these two classes of constructive trusts were distinct from a third type of constructive trust, the "RCT", observing as follows (*Panweld* at [74]):

> "Class 2 "constructive trusts" are not, in fact, "trusts" in the true sense of the word. It is nothing more than a formula for equitable relief; a court applying equitable principles finds that the defendant ought to be made liable in equity, and thus, imposes a constructive trust for this purpose … In the words of Millett LJ in *Paragon Finance* at 409 (which were echoed in *Dubai Aluminium* ([61] supra) at [141]-[142] and *Cradock* at 1575):
>
> > In the first class of case, however, the constructive trustee really is a trustee ... The second class of case is different ... In such a case *[the defendant] is traditionally though I think unfortunately described as a constructive trustee and said to be 'liable to account as constructive trustee.' Such a person is not in fact a trustee at all, even though he may be liable to account as if he were ... They were not in reality trusts at all, but merely a remedial mechanism by which equity gave relief for fraud*. [emphasis in original]
>
> This use of "remedial" in relation to Class 2 "constructive trusts", which restricts the plaintiff to a *personal* remedy must, of course, be distinguished from "remedial" in the sense which is used in the United States and Canada, where a "remedial constructive trust" may be imposed as a *discretionary proprietary remedy*. Under English law, constructive trusts arise based on legal rules, and the court's role in this connection is purely declaratory."
>
> [underlining added for emphasis]

Yong Pung How CJ first noted the possibility of developing the RCT doctrine in Singapore in *Public Prosecutor v Intra Group (Holdings) Co Inc* [1999] 1 SLR(R) 154, although it was found that no such trust arose on the facts (at [26], [46]). The Court of Appeal in *Ching Mun Fong v Liu Cho Chit* [2001] 1 SLR(R) 856 was likewise open to the possibility of imposing an RCT, but decided that that was not warranted in the instant case. The Court stated at [36]:

> "A remedial constructive trust is a restitutionary remedy which the court, in appropriate circumstances, gives by way of equitable relief. In order for a remedial constructive trust to arise, the payee's conscience must have been affected, while the moneys in question still remain with him. If, as was the situation in the *Westdeutsche* case ([35] *supra*), the payee learns of the mistake only after the moneys have got mixed with other funds or dissipated, no constructive trust in respect of these moneys can arise. This is because there would no longer be an identifiable fund for the trust to bite."

The lack of an identifiable fund likewise stood in the way of finding an RCT in the High Court case of *Wee Chiaw Sek Anna v Ng Li-Ann Genevieve* [2012] SGHC 197. The plaintiff ex-wife sued the estate of her deceased ex-husband claiming that he had deceived her into thinking that he was a man of no means. She claimed that, as a result of the misrepresentations, she did not apply for a division of matrimonial assets during their divorce proceedings and had entered into a separation agreement agreeing to support and maintain herself. While the Court accepted that an RCT could arise, it held that the lack of an identifiable fund on which the RCT could be imposed was fatal to the plaintiff's claim.

In *Koh Cheong Heng v Ho Yee Fong* [2011] 3 SLR 125, however, the High Court adopted the RCT as the best explanation for the power to revoke a donation mortis causa where legal title had been vested in the donee. The plaintiff was the sole owner of a property subject to the Singapore Housing and Development Act. When his health deteriorated in 2006, he transferred his interest in the property to himself and his wife as joint tenants. The transfer was made as a gift, with the intention for his wife to be provided for in case the plaintiff predeceased her. The plaintiff's wife subsequently sustained head injuries and was found to lack testamentary capacity. The plaintiff feared that should he predecease his wife, she would become the sole owner of the property, and on her death, the Property would be distributed in accordance with the Intestate Succession Act. The plaintiff thus sought to revoke the gift by obtaining a re-transfer of the property. The court allowed the gift to be revoked, endorsing (at [43]–[44]) the description of an RCT by Lord Denning MR in *Hussey v Palmer* [1972] 3 All ER 744 at 747:

> "[An RCT] is a trust imposed by law whenever justice and good conscience require it. It is a liberal process, founded on large principles of equity, to be applied in cases where the defendant cannot conscientiously keep the property for himself alone, but ought to allow another to have the property or a share in it. The trust may arise at the outset when the property is acquired, or later on, as the circumstances may require. It is an equitable remedy by which the court can enable an aggrieved party to obtain restitution.

> … Under the RCT approach, the court enjoys the discretion to determine whether or not a proprietary remedy should be awarded (Pearce, Stevens & Barr at p 315). If the court exercises its discretion to award a constructive trust, the resulting beneficial entitlement can be said to have been "imposed" by the court, which does not merely recognise a pre-existing proprietary interest (*Pearce, Stevens & Barr* at p 315).

> Therefore, the donor's equitable proprietary interest may not have to arise from the facts per se, but rather, from the exercise of the court's discretion to award such a remedy (*Pearce, Stevens & Barr* at p 315)."

The court concluded that the concerns expressed in English cases, should not stand in the way of embracing the RCT in the instant context (at [46]):

> "…it would not be overly extending the law or generating uncertainty in proprietary rights to utilise the RCT analysis as the theoretical basis for the power of revocation in a *donatio mortis causa* situation. The conditions required for a valid *donatio mortis causa* are stringent, and there is no fear that adopting RCT analysis to explain part of the doctrine would result in the widespread uncertainty feared by English judges."

Resulting Trusts

Another set of trusts, another jurisprudential debate.

In Re Vandervell's Trusts (No. 2) [1974] Ch. 269 at 289, Megarry VC identified two categories of resulting trusts: presumed resulting trusts, arising because of the transferor's presumed intention; and automatic resulting trusts, arising regardless of the transferor's intention.

In *Westdeutsche,* however, Lord Browne-Wilkinson disagreed with a division based on intention. To him, all resulting trusts were based on presumed intention; indeed, on a <u>common intention</u> between the transferor and the recipient (*Westdeutsche* at 708).

In the Privy Council decision in *Air Jamaica Ltd v Charlton* [1999] 1 W.L.R. 1399 ("*Air Jamaica*") Lord Millet then had this to say (at 1412):

> "Like a constructive trust, a resulting trust arises by operation of law, though unlike a constructive trust it gives effect to intention. But it arises whether or not the transferor intended to retain a beneficial interest − he almost always does not − since it responds to the <u>absence of any intention on his part to pass a beneficial interest</u> to the recipient."
>
> [emphasis added]

On the other hand, Professor William Swadling was of the view that resulting trusts are instead founded on a <u>positive intention</u> by the transferor to create a trust in his own favour ("A New Role for Resulting Trusts?" (1996) 16 LS 110 ("*Swadling*") at 116−117, endorsed in *Westdeutsche* at 708. See also William Swadling, "Explaining Resulting Trusts" (2008) 124 LQR 72 at 79):

> "The presumption of resulting trust which arises in the case of a transfer of property without consideration is not one of non-beneficial transfer. It is instead a presumption of transfer on trust for the transferor. And for that reason, evidence of a positive donative intent is not the only thing capable of rebutting the presumption. Any evidence which is inconsistent with the implication of an intended trust will do ... "
>
> [emphasis added]

The Singapore authorities have inclined towards intention-based resulting trusts, but the question remains, what intention: (a) the absence of intention on the part of the transferor to pass beneficial interest to the recipient (*Air Jamaica* at 1412) ("negative-intent theory"); (b) a common intention between the transferor and recipient for such trust to arise (see *Westdeutsche* at 708) ("common intention theory"); or (c) a positive intention to create a trust (*Swadling* at 116−117) ("positive-intention theory")?

While these may not be mutually exclusive, some cases may only fall within one category, *e.g.*, where, unknown to the recipient, the transferor transfers property with no intention of making a gift.

Singapore courts have yet to delve into these distinctions. In two recent decisions, *viz*, *Wong Meng Cheong v Ling Ai Wah* [2012] 1 SLR 549 (where no resulting trust was found to arise) and *Tee Yok Kiat v Pang Min Seng* [2013] SGCA 9 ("*Tee Yok Kiat*") (where a resulting trust was found have arisen on the facts), the courts made the findings on the resulting trust issue based on the intention to make a gift (or, in the case of *Tee Yok Kiat*, the lack of such intention).

Even where there has been some discussion on the jurisprudential basis of resulting trusts, it is not altogether clear which particular analysis has found favour. For example, the Court of Appeal in *Lau Siew Kim* confirmed (at [36]) that resulting trusts are intent-based, but did not clarify the specific content of this "intention" as both the negative-intent and common intention theories were endorsed ([34]-[35]) as follows:

> "Resulting trusts are presumed to arise in two sets of circumstances ... Both types of resulting trust are traditionally regarded as examples of trusts giving effect to the common intention of the parties. A resulting trust is not imposed by law against the intentions of the trustee (as is a constructive trust) but gives effect to his presumed intention.
>
> ...
>
> There is an important distinction between the presumption of resulting trust and the resulting trust itself. The presumption is an inference of a fact drawn from the existence of other facts, whereas the resulting trust

is the equitable response to those facts, proved or presumed: see Robert Chambers, Resulting Trusts (Clarendon Press, Oxford, 1997) at p 32. The difference between them is explained in Resulting Trusts (ibid) as follows:

> The facts which give rise to the presumption of resulting trust are (i) a transfer of property to another, (ii) for which the recipient does not provide the whole of the consideration. The facts which give rise to the resulting trust itself are (i) a transfer of property to another, (ii) in circumstances in which the provider does not intend to benefit the recipient.
>
> Robert Chambers has quite appropriately highlighted two essential points: first, that the lack of consideration required for the presumption is not a requirement for the resulting trust; and second, that the lack of intention to benefit the recipient required for the resulting trust is precisely the fact being inferred when the presumption is applied. It is thus apparent that a resulting trust may arise independently of the presumption so long as it can be shown that the transfer was not intended to benefit the recipient; and, in a similar vein, a resulting trust may not necessarily arise even if there was no consideration, if it can be shown that the transfer was indeed intended to benefit the recipient."

[emphasis added]

The High Court in *Yong Ching See v Lee Kah Choo Karen* [2008] 3 SLR(R) 957 at [36]−[39] similarly discussed both the negative-intent and common intention theories interchangeably and may have conflated them. Indeed, all three theories appeared to have been conflated in *Cheong Yoke Kuen v Cheong Kwok Kiong* [1999] 1 SLR(R) 1126, where the court observed as follows (at [12]−[17]):

> "The position in equity as to the ownership of a property by a person who has contributed any money towards purchase thereof is well settled. Where a person has paid the purchase price of a property ("the purchaser") and the property is conveyed or transferred to him jointly with others, or to one or more persons other than the purchaser, a resulting trust arises in favour of the purchaser, and he is the beneficial owner of the property: *Dyer v Dyer* (1788) 2 Cox 92. If there are more than one purchaser and they paid the purchase money in unequal

shares, the beneficial interest acquired by each of them will be in proportion to their respective contributions. Such a resulting trust is based on the presumed intention of the parties and such presumption is rebuttable by evidence of an intention on the part of the purchaser to make a gift or by the presumption of advancement which arises when a voluntary conveyance or transfer is made to a person to whom the purchaser stands in loco parentis.

...

The nature of a constructive trust is such that it could not be said to be "created" by the parties. It is a trust which is imposed by equity in respect of an interest in a property in a variety of circumstances which would render it inequitable for the owner of the property or any interest therein to hold it for his benefit. It arises independently of the intention of the parties. A resulting trust, however, is different. It arises from a certain transaction carried out intentionally by the parties concerned and the court infers an intention to create a trust in favour of a party.

[emphasis added]

It remains to be seen how Singapore courts will analyse resulting trusts, when the distinction between the various types of intention is material (*e.g.*, where the transferee can have no common intention with the transferor), or where there is really no relevant intention to speak of (*e.g.*, where an express trust fails in whole or in part, as in *Vandervell v IRC* [1966] Ch. 261).

1 April 2013

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Finance, Property and Business Litigation in a Changing World

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25 April 2013

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ANALYSIS OF QUESTION 3

Housing and Development Act (“HDA”), Singapore (Cap. 129)

(Since 2010)

- 51-(8): *No trust in respect of any protected property shall be created by the owner thereof without the prior written approval of the Board.*

- 51-(9): *Every trust which purports to be created in respect of any protected property without the prior written approval of the Board shall be null and void.*

- 51-(10): *No person shall become entitled to any protected property (or any interest in such property) under any resulting trust or constructive trust whensoever created or arising.*

- Despite the express wording of Section 51(10) of the HDA, a series of Singapore cases have held that a resulting/constructive trust can arise if the relevant beneficiary was eligible to hold the HDB property.

  - *Chong Sze Pak v. Chong Ser Yoong* [2011] SGHC 42 (Woo Bih Li J)
  - *Koh Cheong Heng v. Ho Yee Fong* [2011] SGHC 48 (Prakash J)
  - *Tan Chui Lian v. Neo Liew Eng* [2006] SGHC 203 (Sundaresh Menon JC)
  - *Cheong Yoke Kuen v. Cheong Kwok Kiong* [1999] SGCA 27

- The intent of the HDA was to “prevent a situation where a person who is ineligible to own an HDB to become entitled to one.” (*Chong Sze Pak* at [57]-[60])

- Interpreting the sections purposively, the Courts have held that resulting / constructive trust claims will not be barred if the beneficiaries were eligible for ownership

- But note that express trusts are still prohibited

Conclusion

➢ The analysis for Question 3 in the hypothetical would therefore not differ from that of Question 1 and 2 in respect of the resulting / constructive trusts.

➢ However, the analysis of Question 3 in the hypothetical would differ in respect of the express trust.

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ANALYSIS OF QUESTION 4

Residential Property Act, Singapore (Cap. 274)

3. —(1) Except as provided in this Act —

(*c*) no foreign person shall purchase or acquire any residential property or any estate or interest therein except by way of a mortgage, charge or reconveyance.

(2) Any —

(*c*) purchase or acquisition of any residential property or of any estate or interest therein by any foreign person, except by way of a mortgage, charge or reconveyance, made in contravention of subsection (1)(*c*),

shall be null and void.

Residential Property Act, Singapore

23. (2) Any trust created in whatever manner or form pursuant to subsection (1) shall be null and void and there shall be no resulting trust in favour of the foreign person; and any contract or covenant between such citizen or approved purchaser and the foreign person in respect of such residential property or any estate or interest therein shall be null and void.

Short Answer

- Andy held the flat absolutely when he purchased it in 2005.

- Sam has no recourse to any proprietary remedies:
  1. No express trust
  2. No 'institutional' constructive trust
  3. No reliance on the doctrine of knowing receipt

- The RPA provisions are not impregnable.

- Two exceptions have been carved out:

  1. If the circumstances are such that the law will impose a constructive trust (even as against the parties wishes) – *Public Prosecutor v. Intra Group* (Holdings) Co Inc [1999] SGHC 11

  2. Where circumstances allow a claim in restitution to a party who has entered into an illegal transaction as a result of a mistake as to the facts constituting illegality – *Aqua Art Pte Ltd v. Goodman Development (S) Pte Ltd* [2011] SGCA 7

- A third route may lie under the doctrine of repentance or timely repudiation (rubric of restitution):

  A person who has transferred property for an illegal purpose can nevertheless recover it provided that he withdraws from the transaction before the illegal purpose has been wholly or partly performed.

  - *Tribe v Tribe* [1996] Ch 107

  - *Aqua Art* [2011] SGCA 7

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Finance, Property and Business Litigation in a Changing World

Concurrent Session 2B: Fiduciary and Partnership Duties

Speakers

Ms Lesley Anderson QC, *Kings Chambers*

Mr Robert Pearce QC, *Radcliffe Chambers*

Mr Kenneth Tan Wee Kheng SC, *Kenneth Tan Partnership*

Associate Professor Wan Wai Yee, *School of Law, Singapore Management University*

FINANCE, PROPERTY AND BUSINESS LITIGATION IN A CHANGING WORLD

A Joint Conference of the Singapore Academy of Law and the Chancery Bar of England and Wales

Concurrent Session 2B: FIDUCIARY AND PARTNERSHIP DUTIES
Thursday 25 April 2013

Lesley Anderson QC
Hardwicke and Kings Chambers

1. <u>The meaning and scope of fiduciary duties</u>

1.1. A fiduciary is someone who owes fiduciary duties and a fiduciary relationship is one where one person, the fiduciary, owes fiduciary duties to the other. As observed by one leading text, Finn on *Fiduciary Obligations* (1977), it is because he is subject to fiduciary obligations that he is a fiduciary.

1.2. The question is an important one because the existence of a fiduciary relationship defines the circumstances in which a stricter set of obligations may be owed by one party to another.

1.3. Traditional thinking looked to the nature of the relationship and certain settled categories of fiduciary relationship were recognised as deserving the special protection underpinned by the equitable doctrine. Thus, classically, the relationships of trustee and beneficiary; agent and principal; director and company; solicitor and client; partners; guardian and ward; receiver and mortgagee all gave rise to a rebuttable presumption that a fiduciary relationship existed.

1.4. However, it has long been accepted that the class of fiduciary relationships is never closed – *English v Dedham Vale Properties Limited* [1978] 1 WLR 93 at 110 per Slade J. The particular advantage conferred by the finding of a fiduciary relationship encourages a creative, albeit largely fact-specific, approach.

1.5. The Courts have been prepared to find that a fiduciary relationship existed, on the facts, between:

1.5.1. Director and shareholder – *Peskin v Anderson* [2000] EWCA Civ 326 at [31-36];

1.5.2. Employer and employee - *Nottingham University v Fishel* [2000] IRLR 471 and *Cobbetts LLP v Hodge* [2009] EWHC 786 (Ch) at [89-98];

1.5.3. Bank and customer – *Commonwealth Bank of Australia v Smith* (1991) 102 ALR 453 at 476;

1.5.4. Manager and musician client – *O'Sullivan v Management Agency & Music Limited* [1985] 1 QB 428.

1.6. Further, even if a court finds that a fiduciary relationship exists, it does not follow that the fiduciary will be subject to all fiduciary duties. As Lord Browne-Wilkinson pointed out in *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145 at 206:

"*The phrase "fiduciary duties" is a dangerous one, giving rise to the mistaken assumption that all fiduciaries owe the same duty in all circumstances. That is not the case"*.

1.7. The imposition of fiduciary duties may be appropriate in relation to part only of the relationship – see *Nottingham University v Fishel* supra.

1.8. As these few examples make clear, a review of the relevant authorities suggests that the courts have adopted a great degree of flexibility to deciding whether or not particular circumstances gave rise to a fiduciary relationship. It was clearly not sufficient to suggest that the mere existence of a commercial relationship (usually rooted in the express terms of a contract) precluded a finding that one party was in a fiduciary relationship with the other. On the other hand, underlying the classic fiduciary relationships lay the notion that one party (the fiduciary) was under an obligation to subordinate his interests to the other. As the author of another of the leading texts *Snell's Equity* notes at [7-005], it is normally inappropriate to expect a commercial party to do so.

1.9. What has not always been clear is whether there is any coherent principle or principles which unite these cases.

2. The *Ross River* decision

2.1. Recent case-law favours a flexible approach to the question of when a fiduciary relationship will arise.

2.2. In *(1) Ross River Limited (2) Blue River Ltd Partnership v (1) Waveley Commercial Ltd (2) Peter Barnett (3) Paul Harney (4) Westbury Properties Limited* [2012] EWHC 81 at [235] – [255], the Court considered the circumstances in which it would be appropriate to find a fiduciary relationship (thus imposing fiduciary obligations on one party to the relationship in favour of the other party) outside of the accepted classes of fiduciary relationships and the class of fiduciary relationships and the circumstances in which such a relationship would be imposed/found.

2.3. At [235] the Court stated (based on its review of the relevant authorities) that in recent times the Courts had adopted a great degree of flexibility when deciding whether or not particular circumstances give rise to a fiduciary relationship and in doing so had accepted 2 propositions, namely: -

2.3.1. A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances that give rise to a relationship of trust and confidence.

2.3.2. The concept encapsulates a situation where one person is in a relationship with another which gives rise to a legitimate expectation, which equity will recognise, that the fiduciary will not use his or her position in a way which is adverse to the interests of his/her principal.

2.4. The following further points were made:

2.4.1. *"Fiduciary duties are obligations imposed by law as a reaction to particular circumstances of responsibility assumed by one person in respect of the conduct of the affairs of another".*

2.4.2. In relation to the assumption of responsibility the Court stressed that it would have to be a voluntary assumption of responsibility.

2.4.3. Whilst the issue as to whether or not to impose a fiduciary relationship would depend on all the facts and circumstances of the relevant case, it would be exceptional to impose such a relationship in the context of a commercial relationship where ordinarily one party would not expect/and would not be expected to subordinate their interests to those of the other party.

2.4.4. Further, it would be a difficult (but not impossible) task to impose a fiduciary relationship in a situation where the relationship between the parties had been negotiated and agreed in a contract. Absent exceptional circumstances the parties would be treated as having determined the rights and obligations of their relationship in the contract.

2.5. The test is an objective not a subjective one. It is tentatively suggested that one is generally looking for:

2.5.1. A <u>relationship</u> which contains some or all of the identifying features or hallmarks of one of the classic or traditional relationships. So, in *Murad v Al-Saraj* [2004] EWHC 1235 (Ch), a case involving a joint venture, the court found a fiduciary relationship to exist because the arrangement before it was akin to one of partnership because it involved a relationship of mutual trust and confidence.

2.5.2. The <u>special feature</u> that one person has voluntarily assumed responsibility in circumstances which gives rise to a legitimate expectation that he will not abuse his position. Usually, this will be because the party assuming responsibility is in some superior position compared with the other (for example, in possession of superior knowledge or access to information).

2.6. The joint venture context is illustrative. Examination of the facts of each particular case may reveal one or more of the following features:

2.6.1. A relationship of quasi-partnership and was therefore founded on a relationship of mutual trust and confidence. As the term quasi-partnership connotes, the parties are akin to partners in a partnership which has at its essence mutual obligations of good faith. Whilst that of itself is not sufficient to justify the imposition of a fiduciary relationship may be the starting point for consideration of the other factors set out below.

2.6.2. One party may, as a matter of practicality, have been excluded from any involvement in the day-to-day management and affairs of the relevant joint venture vehicle and become reliant on the other for information such that there is no "equality of arms".

2.6.3. The other party knows that the other will be relying on him for the provision of financial and other information and is able to influence the information that is provided to the other.

2.6.4. There is no conflict between the fiduciary's own position and the imposition of the duty to the other party.

2.7. So, in *Ross River* itself, Waveley had undertaken the development of a property pursuant to a joint venture agreement with Ross River. The agreement provided that, upon a sale of the development site, Ross River was to receive a share of the net profits (which it could elect to take either as a fixed sum or as a percentage share) and there was a side agreement which gave it a priority share. Ross River elected to take a percentage share based on information provided to it by Waveley. Waveley then sold the site to Westbury, a company which had been incorporated by Mr Barnett (who was at all times a director of Waveley). This led to Ross River being suspicious and bringing the present claim.

2.8. The Judge held that Waveley was under an implied obligation to act in good faith in its conduct of the joint venture and it was obliged not to do anything in connection with its handling of the joint venture revenues which favoured itself to Ross River's disadvantage (including in relation to the side agreement). He also found that Mr Barnett owed similar fiduciary duties to Ross River (see further below).

3. <u>In what circumstances does a fiduciary owe a duty to disclose misconduct?</u>

3.1. Recent cases have also considered the somewhat difficult question whether, and if so in what circumstances, a fiduciary may be obliged to disclose his or her own misconduct or that of others. So, in the classic type of breach of duty case, if a fiduciary is obliged to disgorge a profit made in breach of duty to his principal, is he also under a (logically, antecedent) obligation to disclose that the profit has been made? The most recent observations have been in the context of directors/employees who leave to join rivals and consider the extent to which, consistently with their duties, they may make preparations to do so. The cases are not entirely consistent but again it is possible to suggest the following tentative conclusions.

3.2. In *Horcal Ltd v Gatland* [1984] BCLC 549 at 554 it was suggested, *obiter*, that fiduciaries owed a duty to reveal a breach of duty giving rise to a duty to account.

3.3. In *Sybron Corporation v Rochem Ltd* [1984] Ch 112 there was said to be no general duty on an employee to report his fellow employee's breach of duty but that one might arise on the proper construction of the relevant contract of employment.

3.4. However, in *Item Software (UK) Ltd v Fassihi* [2004] EWCA Civ 1244, the Court of Appeal held that a company director was liable for a failure to disclose his own misconduct but not because he had been under a free-standing fiduciary obligation to do so. Instead, the court favoured the view that the director was liable for breach of his duty (not necessarily fiduciary) as a director to act in good faith in what he believed to be the best interests of the company.

3.5. *Item Software* was followed in the recent decision of *GHLM Trading Ltd v (1) Anil Kumar Maroo (2) Nita Anilkumari Maroo (3) Brocade International Ltd (4) Jose Paulo de Oliveiro Loureiro* [2012] EWHC 61 (Ch). So, a failure to disclose misconduct or any other information would amount to a breach of the duty of good faith if the fiduciary subjectively concluded that it would be in the interests of the principal to know of the same or he would have so concluded if he had been acting in good faith (see GHLM at [194]).

3.6. The relationship of employer/employee does not as a general rule incorporate an obligation on the employee to disclose the wrongdoing or conduct which is contrary to the employer's best interests of fellow employees and even an express obligation "to use best endeavours to promote the general interests and welfare of the company" does not incorporate such a duty – *Lonmar Global Risks Ltd (formerly SBJ Global Risks Ltd v (1) Barrie West (2) Laurence Niel Mee (3) Stephen Karpus (4) Tyser & Co Ltd* [2010] EWHC 2878 (QB) per Hickinbottom J.

3.7. As the Court of Appeal cautioned in the recent decision of *Jeremy Michael Ranson v Customer Systems Plc* [2012] EWCA Civ 841 it is dangerous to reason from cases about company directors to cases about employees and, in the latter case, it is necessary to ask the anterior question: does the employee owe fiduciary (as opposed to contractual) duties at all? The content of any contractual duty of fidelity and the existence and content of any fiduciary duty (which the court stressed are different) are to be determined, in the first instance, by the terms of the relevant contract of employment. The Court upheld the finding in *Fishel* that there was no general obligation on an employee to report his own misconduct. In doing so, the Court re-affirmed that *Fassihi* was a case founded on the duty of loyalty and not a free-standing duty.

3.8. It would accordingly be unsafe to reason from these recent cases any support for any wider principle that fiduciaries are by reason simply of that position, under an obligation to disclose their own wrongdoing or that of others.

4. <u>In what circumstances does a fiduciary owe fiduciary duties to a third party?</u>

4.1. As noted above, the *Ross River* decision is also of interest on the question of whether, and if so in what circumstances, a fiduciary may owe duties to a third party. Having concluded that Waveley did owe certain fiduciary duties to Ross River, the Judge went on to consider whether Mr Barnett also did so.

4.2. He expressly rejected the submission made by Ross River's counsel that it was "absolutely obvious" that he did so.

4.3. The Judge stated:

"I do not regard the answer to this question as at all obvious. The cases stress that any question of recognising the existence of a fiduciary relationship outside the classic cases is very sensitive to the facts of the particular case. Further, normally it will not be right to hold that a director of a company which is dealing with a third party owes personal fiduciary obligations to that third party, even in a case where the company owes fiduciary obligations to the third party. The distinction which is normally to be made between the company and the director is a fundamental one in company law. Nonetheless, the cases show that it is possible in special circumstances to find that a director has taken on such a fiduciary obligation. Are the circumstances here special enough or are they no more than what is normally the case where a company deals with a third party?"

4.4. He went on to find that, on the facts the arrangements between the parties served to emphasise the personal contribution being made by Mr Barnett and Mr Harney in carrying out the joint venture and that Mr Barnett did owe a fiduciary obligation of good faith to Ross River from the entry into the joint venture in December 2004 and also a fiduciary obligation not to do anything in relation to the handling of the joint venture revenues which favoured himself to the disadvantage of Ross River.

LESLEY ANDERSON QC

1 April 2013

FINANCE, PROPERTY AND BUSINESS LITIGATION IN A CHANGING WORLD

A Joint Conference of the Singapore Academy of Law
and the Chancery Bar of England and Wales

Concurrent Session 2B: FIDUCIARY AND PARTNERSHIP DUTIES
Thursday 25 April 2013

Robert Pearce QC
Radcliffe Chambers

Fiduciary duties in partnership and limited partnerships - a background paper

Fiduciary duties

1. Fiduciary duties originate in the jurisprudence of the courts of equity, which supplemented the jurisdiction of the courts of common law, and which sought to give effect to the requirements of conscience. A breach of fiduciary duty may lead to the grant of remedies not available for breach of other duties.

2. In Millett LJ's classic formulation of the basic principles[1]:

> **"A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal. This is not intended to be an exhaustive list, but it is sufficient to indicate the nature of fiduciary obligations. They are the defining characteristics of the fiduciary."**

[1] Bristol & West Building Society v Mothew [1998] 1 Ch 1 at 18A.

3. As Lesley Anderson QC's paper shows, the authorities stress that not all fiduciaries owe the same fiduciary duties, and that not every duty owed by a fiduciary is a fiduciary duty.

4. As Lesley Anderson QC also shows, fiduciary duties which arise in a commercial setting must be moulded to conform to the contractual and business context[2]. The process is explained thus by Sales J in In F & C Alternative Investments (Holdings) Ltd v Barthelemy (No 2)[3]:

> **"[222] In some contexts, for instance in the paradigm cases described by Lord Browne-Wilkinson[4], the content of the fiduciary obligations which arise will be reasonably standard and well known, having been worked out in the cases over decades if not centuries. Where a person agrees to be appointed as a company director in ordinary circumstances, for example, the fiduciary obligations which are attached to that role are known, at least in general terms. However, there has always been scope for fiduciary duties to be found to arise in a range of other contexts which have important similarities to the paradigm cases, but also significant differences. In those contexts, it is necessary to examine with some care what is the precise content of the particular fiduciary obligations arising in the specific circumstances of the individual case.**
>
> **[223] Fiduciary obligations may arise in a wide range of business relationships, where a substantial degree of control over the property or affairs of one person is given to another person. Very often, of course, a contract may lie at the heart of such a business relationship, and then a question arises about the way in which fiduciary obligations may be imposed alongside the obligations spelled out in the contract. In making their contract, the parties will have bargained for a distribution of risk and for the main standards of conduct to be applied between them. In commercial contexts, care has to be taken in identifying any fiduciary obligations which may arise that the court does not distort the bargain made by the parties … The touchstone is to ask what obligations of a fiduciary character may reasonably be expected to apply in the particular context, where the contract between the parties will usually provide the major part of the contextual framework in which that question arises."**

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2 See further The Rt. Hon Sir Peter Millett, "Equity's Place in the Law of Commerce" (1998) 114 LQR 214.

3 [2012] Ch 613 at [222] – [223].

4 In White v Jones [1995] 2 AC 207 at 271.

5. In an influential article[5], Professor James Edelman has argued that the correct approach to the identification of the existence and scope of fiduciary relations is not to focus on which relationships are fiduciary, based on notions of status, but to treat fiduciary duties as terms which are expressed or implied in voluntary undertakings. His suggested approach results in convergence of the approach to the identification of fiduciary duties and the approach to the implication of contractual terms[6].

Unlimited partnerships

6. The English law of unlimited partnerships is partially codified by the Partnership Act 1890 ("PA 1890")[7]. The nature of a partnership is described by sections 1 to 4. Partnership is defined as "the relation which subsists between persons carrying on a business in common with a view of profit"[8]. The definition is qualified to exclude the relationship between members of registered companies or other incorporated bodies[9] and is elaborated by "rules" (perhaps more aptly described as further elements of the definition) for determining the existence of a partnership[10]. Persons who have entered into a partnership with one another are collectively called a "firm"[11], but a partnership has no legal identity separate from that of its members.

7. Sections 5 to 18 establish the framework for relations between partners and persons dealing with them. By section 5, every partner is an agent of the firm and the other partners for the purpose of the business of the partnership, and by that and the following sections each partner is, in general, made jointly, or jointly and severally, liable for the consequences of acts carried out in the course of the firm's business.

8. Sections 19 to 31 establish a framework for relations between partners, which, however, may be varied by agreement between them. By sections 28 to 30, a partner

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5 "When do Fiduciary Duties Arise" (2010) 126 LQR 302. The article is based on papers presented at the Obligations IV conference at the National University of Singapore and at the Faculty of Law of Singapore Management University.

6 Attorney General of Belize v Belize Telecom [2009] 1 WLR 1988. See F & C Alternative Investments (Holdings) Ltd v Barthelemy (No 2) [2012] Ch 613 at [225].

7 Applied in Singapore by the Application of English Law Act 1993.

8 Section 1 (1).

9 Section 1 (2).

10 Section 2.

11 Section 4 (1).

is bound to render true accounts and full information of all things affecting the partnership to the others, must account to the firm for any benefit derived by him without the consent of the other partners from any transaction concerning the partnership or from any use by him of the partnership property, name or business connection, and must account to the firm for profits made by him without the consent of the other partners in any business of the same nature as and competing with that of the firm.

9. Sections 32 to 44 provide for a partnership to be dissolved either in circumstances agreed by the partners, or automatically, or by the court in its discretion when specified grounds are made out, and they prescribe how the affairs of a dissolved partnership are to be wound up.

10. Although a partnership arises by agreement, once formed, it is not governed solely by the law of contract:

> **"By entering into the relationship of partnership, the parties submit themselves to the jurisdiction of the court of equity and the general principles developed by that court in the exercise of its equitable jurisdiction in respect of partnerships."**[12]

11. It is not settled whether acceptance by one partner of a repudiatory breach by another, without more, dissolves a partnership[13]. Even if it does, the partner accepting the breach is not thereby discharged from liability to contribute to the firm's existing or future liabilities: these continue, as with all other modes of dissolution, to be dealt with by the statutory scheme for winding up the affairs of the firm[14].

12. Partnership is commonly said to give rise to mutual obligations of good faith. The precise source of this obligation, and whether it is to be regarded as a contractual or a fiduciary obligation, is not always clear[15]. A partnership agreement will often contain

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12 Hurst v Bryk [2002] 1 AC 185 at 195 (Lord Millett).

13 Hurst v Bryk [2002] 1 AC 185; Mullins v Laughton [2003] Ch. 250.

14 Hurst v Bryk [2002] 1 AC 185.

15 It is variously said to be an implied term of the partnership agreement (Blackett-Ord, Partnership Law, 4th ed. para 11.1), the result of a presumption of law that partnerships are based on the mutual trust and confidence of each partner in the integrity of the others (Halsbury, Laws of England, 5th ed. Vol. 79 para 106) and an obligation which the law imposes on a partner (Lindley & Banks on Partnership 19th ed. para 6.01).

a term to the effect that the partners will act in good faith on relation to the partnership, or be just and faithful in their mutual dealings. Where this is the case, the relevant obligation arises by express agreement. If the partners have not agreed to the contrary, their mutual dealings will be governed by, amongst other things, PA 1890 sections 28 to 30 (summarised above). These impose mutual obligations of candour and fair dealing, but they do not (nor does any other provision of the Act) use the term "good faith". In such a case, to say that partners owe mutual obligations of good faith is perhaps best understood as a paraphrase or summary of the obligations applied to their agreement by statute.

13. The relation between partners is commonly said to be an established category of fiduciary relationship[16]. The basis for this is that (applying Millett LJ's formulation) each partner has undertaken to act for or on behalf of the other in relation to the affairs of the firm in circumstances which give rise to a relationship of trust and confidence. However, the fiduciary obligation between partners is unlike many other established categories of fiduciary relationship, in that it will usually arise out of a bargain made at arm's length.

14. It appears that, in principle, a partnership agreement can negate the existence of any obligation of good faith or fiduciary relationship between the partners, provided always that the relationship between them remains one between "persons carrying on a business in common with a view of profit" and which satisfies the other elements of the definition of "partnership" in section 1 of PA 1890.

15. One facet of the fiduciary obligation of loyalty is that a fiduciary must not make an unauthorised profit from his fiduciary position. This principle may apply even if it was impossible for the person to whom the fiduciary duty is owed to have made the profit himself, and even if such person would have chosen not to do so[17].

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16 Snell's Equity, 32nd ed. para 7-004; see also for example Helmore v Smith (1886) 35 Ch D 436 at 444: "If fiduciary relation means anything I cannot conceive a stronger case of fiduciary relation than that which exists between partners. Their mutual confidence is the life blood of the concern. It is because they trust one another that they are partners in the first instance; it is because they continue to trust one another that the business goes on".

17 Regal (Hastings) Ltd v Gulliver [1967] 2 AC 134; Boardman v Phipps [1967] 2 AC 46.

16. This principle applies to partnerships in what may be considered to be an attenuated form. In Aas v Benham[18] a partner in a firm of shipbrokers assisted in forming a company whose object was shipbuilding, using information obtained as a member of the firm, and he received remuneration for assisting in the formation of that company and for acting as a director of it. It was held that he was not accountable to the firm for that remuneration, on the ground that shipbuilding was not within the scope of the partnership's business. Lindley LJ said[19]:

"As regards the use by a partner of information obtained by him in the course of the transaction of partnership business, or by reason of his connection with the firm, the principle is that if he avails himself of it for any purpose which is within the scope of the partnership business, or of any competing business, the profits of which belong to the firm, he must account to the firm for any benefits which he may have derived from such information, but there is no principle or authority which entitles a firm to benefits derived by a partner from the use of information for purposes which are wholly without the scope of the firm's business … . It is not the source of the information, but the use to which it is applied, which is important in such matters."

17. In Boardman v Phipps[20] the House of Lords, by a majority, held that self-appointed agents of a trust were accountable to the trust for profits made by then using information acquired as such agents. Two of the majority (Lords Hodson and Guest) distinguished Aas v Benham[21]. Lord Guest said[22]:

"That, however, was a case of partnership where the scope of the partners' power to bind the partnership can be closely defined in relation to the partnership deed. In the present case the knowledge and information obtained by Boardman was obtained in the course of the fiduciary position in which he had placed himself. The only defence available to a person in such a fiduciary position is that he made the profits with the knowledge and assent of the trustees".

18 [1891] 2 Ch 244.
19 At 255.
20 [1967] 2 AC 46.
21 [1891] 2 Ch 244.
22 At 117F.

18. In O'Donnell v Shanahan[23] the Court of Appeal rejected an attempt to limit the accountability of company directors for unauthorised profits by reference to Aas v Benham[24]. Rimer LJ said[25]:

> **"To those familiar with the wider obligations of accountability to which trustees and directors are subject, the decision in Aas v Benham may at first sight appear to reflect a surprisingly narrow approach. But the explanation is that a trustee's and director's fiduciary duties are not similarly circumscribed by the terms of a contract."**

19. There is an obvious tension between the decisions in Aas v Benham[26] and cases such as Boardman v Phipps[27]. Precedent apart, it is surely arguable that a partner who obtains a profit not authorised by his partners from an opportunity which he obtains as a partner should be accountable to the firm for the profit, even if the opportunity was unrelated to the firm's business, and conversely that a company director who obtains a profit not authorised by the company from an opportunity which he obtains as a director and which is unrelated to the company's business should be treated in the same way as a partner in the equivalent situation.

Limited liability partnerships

20. In English law, a limited liability partnership is a form of legal entity authorised by the Limited Liability Partnership Act 2000 ("LLPA 2000")[28]. It is a body corporate with a legal personality separate from that of its members, and it has unlimited capacity[29]. Except where otherwise provided by LLPA 2000 or any other enactment, partnership law does not apply to it[30]. It may be incorporated pursuant to an application for registration made by two or more persons associated for carrying on a lawful business with a view to profit[31].

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23 [2009] EWCA (Civ) 751.
24 [1891] 2 Ch 244.
25 At [68].
26 [1891] 2 Ch 244.
27 [1967] 2 AC 46.
28 Compare the Singapore Limited Liability Partnerships Act 2005.
29 Section 1.
30 Section 1 (5).
31 Section 2 (1).

21. The mutual rights and obligations of the members, and of the LLP and the members, are governed by agreement between them, and, in default of agreement, by provisions made by statutory regulations (the default provisions being loosely modelled on PA 1890 sections 24 - 30)[32]. Whereas unlimited partners "submit themselves to the jurisdiction of the court of equity and the general principles developed by that court in the exercise of its equitable jurisdiction in respect of partnerships" (see paragraph 10 above), there is no equivalent submission in the case of LLPs, the internal workings of the LLP being, in general, governed solely by the LLP agreement.

22. Every member of a LLP is the agent of the LLP[33], but a LLP is not bound by anything done by a member in dealing with a member if the member in fact has no authority to act for the LLP in doing that thing, and the person knows he has no authority or does not know or believe him to be a member of the LLP[34]. Where a member of the LLP is liable to any person (other than another member of the LLP) as a result of a wrongful act or omission of his in the course of the business of the LLP or with its authority, the LLP is liable to the same extent as the member[35]. Provisions of the companies and insolvency legislation are applied, with modifications, to regulate the accounts and auditing of LLPs, their insolvency and winding up, and other matters[36].

23. Since a LLP has a legal capacity separate from its members it offers (unlike an unlimited partnership) a means of carrying on business without necessarily exposing its members to liabilities incurred in doing so.

24. LLPA 2000 section 5 (1) envisages that the rights of the LLP and the members as between themselves will be governed by agreement. Such agreements may take a wide variety of forms, and in consequence it is unhelpful to generalise about the circumstances in which they will give rise to fiduciary obligations. The first English

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32 Section 5 (1); Limited Liability Partnership Regulations 2001, reg. 7.
33 Section 6 (1).
34 Section 6 (2).
35 Section 6 (4).
36 Limited Liability Partnership Regulations 2001, Limited Liability Partnerships (Account and Audit) (Application of Companies Act 2006) Regulations 2008, Limited Liability Partnerships (Application of Companies Act 2006) Regulations 2009.

case to consider the matter in detail, F & C Alternative Investments (Holdings) Ltd v Barthelemy (No 2)[37] is, nevertheless, instructive.

25. In that case, a LLP had been formed to carry on the business of conducting the management of fund of hedge fund vehicles, marketing them, and associated and other activities. The members of the LLP were a company ("Holdings"), which was itself comprised in a group ("F & C") which carried on a range of businesses in the field of asset management, and two individuals, B and C, with expertise in managing fund of hedge funds products. The basic concept was that F & C would provide the working capital, clients, and administrative and technical support, and that B and C would provide specialist expertise.

26. The provisions of the agreement constituting the LLP ("the agreement") included provisions:

    26.1. Requiring each member other than Holdings to devote his full time and attention to the business of the LLP (clause 13.1).

    26.2. That each member shall at all times show the utmost good faith to the LLP (clause 13.6).

    26.3. For there to be a management committee consisting of B, C and such other persons as were determined by the board of the LLP from time to time, (clause 17).

    26.4. For there to be a board consisting of B, C and up to three persons appointed by Holdings "as its board representatives" (clause 18).

    26.5. For there to be a compensation (or remuneration) committee consisting of B, C and two named representatives of F & C (clause 20).

    26.6. For there to be meetings of members (clause 22).

27. Sales J held that:

    27.1. Holdings' "representatives" on the board of the LLP were not, when acting in that capacity, agents of Holdings, but were its representatives in a looser sense (judgment paragraphs 204 – 6). The reasons which led to this conclusion

37 [2012] Ch 613.

included that clear language would be needed to subject such individuals to fiduciary duties both to the LLP and to the person that appointed him. Sales J accepted that such individuals owed fiduciary duties to the LLP (see further below), but he considered that the agreement did not show that they were also intended to owe fiduciary duties to Holdings.

27.2. It was nevertheless possible to attribute the acts of those representatives to Holdings and its parent company for the purpose of awarding relief against those companies under the Companies Act 2006 section 994 (unfair prejudice), as applied to LLPs (judgment paragraphs (1094 – 1107).

27.3. The members of the LLP, as such, did not owe a general fiduciary duty of good faith to the LLP, in addition to the contractual duty in clause 13.6 of the agreement (judgment paragraphs 217 – 220). The reasons which led to this conclusion included that Holdings (as distinct from the persons appointed by it as its representatives on the board of the LLP) did not undertake active duties in the management of the LLP.

27.4. The members of the LLP did not (unlike partners in an unlimited partnership) owe fiduciary duties to each other (judgment paragraphs 207 – 216). The reasons which led to this conclusion included the following:

27.4.1. LLPA 2000 section 1 (5) provides that, save as specifically provided, the law relating to partnership does not apply to a LLP.

27.4.2. As a result of pre-legislative consultation, it had been decided not to enact a duty of good faith owed between members.

27.4.3. LLPA 2000 envisages that the mutual rights and obligations of members will be governed by agreement between them.

27.4.4. In those circumstances, it was necessary to resort to basic equitable principles to determine what fiduciary obligations arose in the context of a LLP.

27.4.5. Applying those principles, a fiduciary obligation arose when one person assumes responsibility for the management of another's property or affairs.

27.4.6. Under the agreement, Holdings did not assume responsibility to act as agent for the LLP, for its individual members, or for the management of the LLP's affairs.

27.4.7. There was an analogy between the position of members under the agreement and the position of company shareholders, who do not owe fiduciary obligations to each other.

27.5. The members of the board, management committee and compensation committee owed, as such, fiduciary duties to the LLP (judgment paragraphs 221 – 54). The existence and content of these duties had to be ascertained from the contractual and business context (see the extract from the judgment cited at paragraph 4 above). The prominent features of that context included (judgment paragraph 226):

27.5.1. The primary commercial objective of the LLP was to marry B and C's expertise with F & C's reputation and client base.

27.5.2. Some tension between the interests of F & C and those of B and C was inherent in the structure of the LLP created by the agreement.

27.5.3. It was envisaged that F & C's representatives and B and C would be involved in making decisions for the LLP, notwithstanding that B and C's and F & C's own financial interests might be affected by the decisions.

27.6. Applying that approach (judgment paragraphs 227 – 259):

27.6.1. There was informed consent to the relaxation of the principle that a fiduciary may not put himself in a position of conflict of interest.

27.6.2. There was informed consent to the relaxation of the principle that a fiduciary may not profit from his position, to the extent of consenting to the making of commercial profits envisaged by the agreement.

27.6.3. The principles that a fiduciary must act in the best interests of his beneficiary (i.e. the LLP) and in good faith were qualified to allow the F & C representatives to have regard to the interests of F & C as well as to those of the LLP, and to allow B and C to have regard to their personal interests as well as to those of the LLP.

28. Sales J's view of the extent to which, as mentioned above, the fiduciary obligations to the LLP of those serving on its committees were qualified is illustrated by the following passages in the judgment:

"[236] In the case of the LLP, it was known and intended that F&C should have its "representatives" on the Board and other governance organs of the LLP to balance out the Defendants' [i.e. B and C's] membership of those organs, and that the Defendants and those representatives should not be disabled from acting by the fact that there might at times be an actual conflict of interest nor disabled from having regard to some degree to their own interests and F&C's interests respectively. Given the interests which the LLP was intended to serve and the way in which the parties intended those interests to be balanced within the governance structures of the LLP, there was no ready set of alternative Board members whose judgment of what the LLP should do would be uncontaminated by consideration of either self-interest or the interests of F&C …

[237] On the formulation set out in the paragraph above, the difficulty lies in identifying the degree to which it was legitimate for the LLP Board members to have regard either to their own self-interest (in the case of the Defendants) or F&C's interests (in the case of the F&C representatives). This is highly dependent on the particular factual circumstances in which the question what to do might arise. Whilst not being able to specify precisely in advance what they could or could not do is somewhat frustrating, that is simply a function of the blurring of roles which the parties intended should occur within the LLP and the usual flexibility of equitable standards of conscionable behaviour once one moves away from the clear paradigm fiduciary relationships, especially where those standards fall to be applied in relation to the management of a business in a relationship which was intended to continue over a substantial period of time and which would have to adapt to meeting a wide range of often unforeseen business situations.

…

[239] … In my view, following on from the discussion above, the F&C representatives on those bodies were entitled to take the interests of F&C into account alongside those of the LLP as a distinct entity, but not so as wholly to subordinate the interests of the LLP to those of F&C. In practical terms this means that they were obliged to strive to maintain a fair balance between the distinct interests of the Defendants and F&C bundled up collectively in the LLP.

They were also entitled to give weight to the interests of the LLP in being linked to the F&C Group, such that the LLP could be expected to benefit from being closely allied to a strong F&C. In light of that, the view could legitimately be taken that sometimes a degree of restraint by the LLP in pursuing its interests, so as to assist F&C in the pursuit of its wider interests, might overall be in the interests of the LLP.

[240] Of course, the fact that this departure from the ordinary requirement that a fiduciary avoid all conflicts of interest was intended to create a business vehicle within which the tensions associated with such conflicts would in practice be mediated and regulated through the governance structures within the LLP made it important that those structures should be carefully adhered to, if the whole set of relationships established by the Agreement was to work properly …".

29. In dealing with that issue, Sales J considered the observations of Millett LJ in Bristol and West Building Society v Mothew[38] concerning the position of a fiduciary who acts for two principals. Sales J's discussion of that point assists in clarifying an area of the law which often causes difficulty[39]. Millett LJ said that:

29.1. A fiduciary who acts for two principals with potentially conflicting interests without the informed consent of both is in breach of his obligation of undivided loyalty.

29.2. Even if a fiduciary is properly acting for two principals with potentially conflicting interests he must act in good faith in the interests of each and must not act with the intention of furthering the interests of one principal to the prejudice of the other. He must not allow the performance of his obligation to one principal to be influenced by his relationship with the other. He must serve each as if he were his only principal. Conduct which is in breach of this duty need not be dishonest but it must be intentional.

29.3. If a fiduciary finds himself in a position where there is an actual conflict of duty, so that he cannot fulfil his duty to one without failing in his obligations to another, he may have no alternative but to cease to act for one and preferably both.

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38 [1998] Ch 1 at 18 – 19.

39 See further Matthew Conaglen, "Fiduciary Regulation of Conflicts Between Duties" (2009) 125 LQR 111.

30. Sales J said of this last point[40]:

"That statement is readily understandable in the context with which Millett LJ was dealing in that case, namely a solicitor acting for two clients. The solicitor/client relationship involves a particularly strong degree of confidence and trust, and the content of the fiduciary duties associated with it is well established and demanding. It is also relevant that there is a ready supply of alternative solicitors who are able to act and can readily be substituted if an actual conflict of interest is perceived to arise. But in my view, read on its own, Millett LJ's statement does not take full account of the wide and varied range of circumstances in which fiduciary obligations of different types and of greater or lesser force may arise. The paradigm cases of fiduciary relationships, such as those between solicitors and their clients, are at the centre of a family of such relationships sharing some but not necessarily all characteristics, where the force of the obligations to be identified as inhering in those relationships (what is reasonably to be expected of the person who has taken on the task of acting for another in those relationships) may vary and become weaker the further one moves from the those central cases."

31. The decision in F & C Alternative Investments (Holdings) Ltd v Barthelemy (No 2)[41] is a valuable illustration of the modern approach to the identification of fiduciary obligations in commercial settings, emphasising, as it does, the importance of a careful analysis of the contractual and business context in which the obligations are alleged to arise.

Robert Pearce QC

5 April 2013

[40] At [228].

[41] [2012] Ch 613.

FINANCE, PROPERTY AND BUSINESS LITIGATION IN A CHANGING WORLD

A JOINT CONFERENCE OF THE SINGAPORE ACADEMY OF LAW AND THE CHANCERY BAR OF ENGLAND AND WALES

25 & 26 April 2013
Supreme Court
Singapore

Fiduciary Duties of Financial Advisory Firms in Takeovers and Restructurings

WAI YEE WAN

Singapore Management University

CHANCERY BAR | SINGAPORE ACADEMY OF LAW | Celebrating 25 Years 1988-2013

PROBLEMS

- Financial advisory firms which are conglomerate operations offer many services (and not only financial advisory services) – giving rise to potential conflicts of interests
- Examples:
  - Lending / syndication for competing bidders and advising target in hostile bid (conflict between clients) [*In re Toys R Us*; *Re Del Monte Shareholders' Litigation]*
  - Engage in proprietary trading in competition with client's interests [*ASIC v Citigroup*]
  - Has interest in in target or in potential bidder [*In Re El Pasco Shareholders Litigation*]

PROBLEMS

- Boutique financial advisory firms are not necessarily free from conflicts:
  - When advising a company which is in financial distress for rehabilitation purposes, are there any duties owed to creditors of the company? [NB: discussion confined to financial advisers are acting as financial advisers and not acting as liquidator or judicial manager]
  - Discussion of *Re TT International* (SGCA)

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ISSUES

- Do financial advisers owe fiduciary duties to their clients in advising them in takeover transactions?
  - If so, what is the scope and content of obligation to avoid conflicts of interests?
  - Can such duties be excluded or limited by contract?
- Do financial advisers owe fiduciary duties to creditors in advising companies in financial distress that are pursuing a scheme of arrangement?
  - If so, what is the scope and content of obligation to avoid conflicts of interests?

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TAKEOVERS

- When does a professional adviser owe fiduciary duties to his client?
  - Look at undertaking of the adviser: *Bristol & West Building Society v Mothew* etc
  - Status-based approach: Analogy to cases involving banking relationships, corporate advisers and clients
- England: *United Pan-Europe Communications v Deutsche Bank*
- Australia: *ASIC v Citigroup*
- Singapore: *Deutsche Bank v Chang Tse Wen*

TAKEOVERS

- Content of the fiduciary obligation
  - Double employment rule
  - Duty of good faith
  - No inhibition rule
  - Actual conflict rule
- NB: Confidentiality and obligation of advice

TAKEOVERS

- Can conflicts of interests be managed by contract? Terms of retainer
  - *Kelly v Cooper*
- Use contract to exclude fiduciary relationship
  - *ASIC v Citigroup*

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ASIC V CITIGROUP

- "The Company acknowledges that Citigroup has been retained hereunder solely as an adviser to the Company, and not as an adviser to or agent of any other person, and that the Company's engagement of Citigroup is as **an independent contractor and not in any other capacity including as a fiduciary.** Citigroup may, to the extent it deems appropriate, render the services hereunder through one or more of its related bodies corporate..."

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ASIC V CITIGROUP

- "The Company should be aware that Citigroup and/or its related bodies corporate may be providing or may in the future provide financial or other services to other parties with conflicting interests. However, consistent with **our long-standing policy to hold in confidence the affairs of our customers, we will not use confidential information obtained from the Company except in connection with our services to, and our relationship with, the Company,** nor will we use on the Company's behalf any confidential information obtained from any other customer."

TAKEOVERS

- Use contract and informed consent to manage fiduciary relationship
  - Use contract to limit fiduciary relationship
  - Post-contract, use consent but question of scope of consent (Discuss *ASIC v Citigroup*)
- Use Chinese wall and contract to manage conflict of interest

TAKEOVERS – APPLYING PRINCIPLES

- Acting for multiple parties in the same takeover transaction
  - Double employment rule applies
  - Exclude / limit the fiduciary relationship and use Chinese wall
- Singapore Code on Takeovers and Mergers, note 2 to rule 7.3

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TAKEOVERS – APPLYING PRINCIPLES

- Acting for client whose interests are against existing client in unrelated matters
- More relevant to solicitors but possibly arise for FAs e.g. FA is advising client A on a material acquisition / internal reorganisation and same firm (different team) is engaged to advise client B which is considering making a bid for client A
- Case law here mostly for solicitors (*Marks and Spencer v Freshfields*)

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TAKEOVERS – APPLYING PRINCIPLES

- Acting for proposed client whose interests are against former client
- Issues of confidentiality and not fiduciary
- *Mannesmann v Goldman Sachs*
- Singapore Code on Takeovers and Mergers, note 2 to rule 7.3

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RESTRUCTURINGS

- Scheme of arrangement under section 210 of the Companies Act is popular to rehabilitate the company
- Financial adviser is engaged by the financially distressed company to work out a scheme of arrangement if unlikely that all debtors consent to restructuring
- Problem: Role of the scheme manager not statutorily defined (he is not an approved insolvency practitioner); he is the target's financial adviser and is subsequently appointed by the company to administer the scheme

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RESTRUCTURINGS

- Yet, the scheme manager plays important role, particularly in adjudicating proof of debts for the purposes of voting
- Scheme manager faces potential conflicts of interests:
  - Structure of remuneration: *Re TT International* [based not only on time-costs for work done but also on success of scheme and debt written off]
  - Past relationships with certain creditors of the scheme company (e.g. advisory etc)
  - Past relationships with management of scheme company: *Re TT International*

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RESTRUCTURINGS

- Are scheme managers fiduciaries of creditors before and after the approval of the court?
- *TT International*: CA says pre-effectiveness, scheme manager has a quasi-judicial role and owes a duty, in adjudicating the proof of debts for the purposes of voting at the scheme, to be objective, independent, fair and impartial [quasi-fiduciary?]
- Post-effectiveness, CA says that scheme manager owes fiduciary duties to the company and creditors in administering the scheme.

Wai Yee Wan, *Singapore Management University*

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RESTRUCTURINGS

- On facts, success-based fee was invalidated as scheme manager was conflicted
- Problem with holding that scheme manager has obligation to avoid conflict of interest between his interests and creditors' interests:
  - Possible? He is appointed by the *company*
  - Remunerated on the basis of success of scheme (even without an onerous success-based fee)
  - Whose consent to the fee arrangement is required? Consent of majority representing 75% in value? Consent of each creditor?

Wai Yee Wan, *Singapore Management University*

CONCLUSIONS

- Not settled case law as to whether fiduciary duties will arise for financial advisory firms advising in takeovers – will the contractual techniques to exclude or modify fiduciary obligations work? If there are fiduciary duties, what is the scope of consent required?
- For restructurings, questions remain unanswered:
  - Previous relationship between the scheme manager and the company/directors? E.g. provision of advisory services
  - Previous relationship between the scheme manager and certain of the creditors?

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A JOINT CONFERENCE OF THE SINGAPORE ACADEMY OF LAW AND THE CHANCERY BAR OF ENGLAND AND WALES

25 & 26 April 2013
Supreme Court
Singapore

Fiduciary Duties of Financial Advisory Firms in Takeovers and Restructurings

WAI YEE WAN

Singapore Management University

CHANCERY BAR

SINGAPORE ACADEMY OF LAW

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FINANCE, PROPERTY AND BUSINESS LITIGATION IN A CHANGING WORLD

A Joint Conference of the Singapore Academy of Law and the Chancery Bar of England and Wales

Concurrent Session 2B: FIDUCIARY AND PARTNERSHIP DUTIES
Thursday 25 April 2013

Kenneth Tan SC
Kenneth Tan Partnership

Fiduciary duties of parties to a joint venture : cases from Singapore and Malaysia

Introduction

1. The classic definition of a "fiduciary" formulated by Millet LJ in Bristol & West Building Society v Mothew[1] was cited with approval by the Court of Appeal in Ng Eng Ghee v Mamato Kapildev Dave[2], and recently adopted by Philip Pillay J in Deutsche Bank AG v Chang Tse Wen[3].

"*A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence*. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position where his duty and his interest conflict; he may not act for his own benefit or the benefit of a third person

[1] [1998] Ch 1 at [18]
[2] [2009] 3 SLR(R) 109 at [135]
[3] [2013] 1 SLR 1310 at [104]

without the informed consent of his principal. [emphasis as added by Phillip Pillay J][4]".

2. In addition to the established categories of relationships which give rise to fiduciary relationship eg. partners, principal and agent, director and company, master-agent and solicitor-client, a fiduciary relationship may exist in the context of a commercial relationship : " the real question is whether or not the nature of the relationship between the parties satisfied the criteria of a fiduciary relationship[5]".

3. For example, the Court of Appeal in Smile Inc Dental Surgeons Pte Ltd v Lui Andrew Stewart addressed the circumstances where fiduciary duties could arise in an employment contract[6] :

"…(fiduciary duties) … result from the fact that within a particular contractual relationship there are specific contractual obligations which the employee has undertaken which have placed him in a situation where equity imposes these rigorous duties in addition to the contractual obligations. Where this occurs, the scope of the fiduciary obligations both arises out of, and is circumscribed by, the contractual terms; it is circumscribed because equity cannot alter the terms of the contract validly undertaken…"

4. Several Singapore and Malaysian cases which address the extent to which parties to a joint venture agreement may owe fiduciary duties in the context of a joint venture agreement illustrate the difficulties of addressing whether the nature of the relationship between the parties gives rise to any fiduciary duties.

[4] Robert Pearce QC adopts the same classic formulation at [2] of his paper.
[5] Deutsch Bank AG v Chang Tse Wen at [105] and [109]
[6] [2012] 4 SLR 308 at [52] quoting Elias J in Nottingham University v Fishel [2000] IRLR 471 at [91]

Singapore and Malaysian cases

5. One approach has been to analyse the extent to which a partnership structure has been adopted in a joint venture, as under Singapore law, as in English law, partnership is a recognized category of fiduciary relationships[7].

6. Selvam J in Canadian Pacific (Bermuda) Ltd v Nederkoorn Pte Ltd[8] adopted this approach in finding that on the facts before him, there was a joint venture without a partnership. There the plaintiff and the defendant had entered into a joint venture to operate a shipping business on the terms contained in a MOU. Pursuant to the MOU, companies were incorporated in Singapore and Bermuda with the intention that the joint venture business should be carried out by the Bermuda company with the Singapore company acting as its agent and manager. After the end of the joint venture, the plaintiff sued the defendant claiming reimbursements of advances made to and expenses incurred for the joint venture business. Selvam J found that the parties were not partners and there was no obligation to account personally for the profits and losses of the joint venture business. He construed the MOU as providing that there would be a joint venture company which would carry on the joint venture business and held that a partnership business was not contemplated by or mentioned in the MOU. As a result, the joint venture parties have only claims as shareholders in the joint venture companies, and contracting partiues to the MOU: they did not owe each other ficuciary duties.

7. When Canadian Pacific (Bermuda) Ltd v Nederkoorn Pte Ltd, went on appeal before the Court of Appeal, the Court of Appeal affirmed Selvam J's ruling that there was no partnership between the parties. It was however raised that conceivably, short of a partnership, there could be super added to the parties relationship as shareholders in the joint venture companies an agreement to share profits and losses, and that the relationship inherent in that agreement imported a fiduciary duty on the parties to account as joint venturers[9].

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[7] As suggested in Hewitt on Joint Ventures (5th ed)(2011) at 11-21
[8] [1998] 1 SLR(R) 559
[9] [1999] 1 SLR(R) 628 at 22(b)

8. Prakash J in Rabian Bee bte Mohamed Ibrahim v Salim Ibrahim[10] adopted a similar approach to Selvam J but found in that case that the plaintiff and the defendant siblings who by oral agreement jointly entered the property market through the purchase and refurbishment of residential properties for letting or sale via various holding joint venture companies were acting in partnership. She found that the siblings had agreed to go into business together for an indefinite period with the joint venture companies being only shells.

9. In approaching the issue of whether a joint venture was a partnership, the Court of Appeal in Canadian Pacific (Bermuda) Ltd v Nederkoorn Pte Ltd[11] had made clear that the use of any labels by the parties to describe their relationship as a "partnership" or otherwise, "do not provide much assistance … as pointed out by Cozens-Hardy MR in Weiner v Harris [1910] 1KB 285, 260:

> "It is quite plain that by a mere use of a well-known legal phrase you cannot constitute a transaction that which you attempt to describe by that phrase. Perhaps the commonest instance of all, which has come before the courts in many phases, is this: Two parties enter into a transaction and say 'it is hereby declared there is no partnership between us'. The Court pays no regard to that. The Court looks at the transaction and says 'is this, in point of law, really a partnership?' It is not in the least conclusive that the parties have used a term or language intended to indicate that the transaction is not that which in law it is."

10. As an illustration, Chan Seng Onn J in Econ Piling Pte Ltd v NCC International AB[12] found on the facts before him that, although the joint venture agreement between the parties made clear that the Joint Venture Agreement did not constitute a partnership, the parties were partners.

11. In Newacres Sdn Bhd v Sri Alam Sdn Bhd [13], the Malaysian Supreme Court in dealing with a joint venture agreement which stated that the relationship was not one of a

[10] [2007] 2 SLR(R) 655
[11] at [23]
[12] [2008] SGHC 26
[13] [2009] 9 MLJ 661 at [15]

partnership approached the issue of whether there was a fiduciary relatiosnhip between the joint ventureres in the following way:

"…

In the High Court of Australia case of Jenyns v Pacific Curator (Q) Dixon CJ, McTiernan and Kitto JJ have this to say at p 133:

We are not here dealing with any of the traditional relations of influence or confidence – solicior and client, physician and patient, priest and peninitent, guardian and ward, trustee and cestui que trust. It is a special relatioship set up by the actual reposing of confidence. It is therefore necessary to see the extent and nature of the confidence reposed and whether it involved any ascendancy over the will of the person supposedly dependent on the confidence.

The judges were talking about fiduciary duties bewteen the parties. In the case of James Bittchnell & Anor v The Equity Trustees, Executors and Agency Co Ltd and Anor Dixon CJ at p 407 explains the fiduciary relationship between partners and how the relationship is to be determined. This is what he says:

The relationship between partners is, of course, fiduciary. Indeed, it has been said that a stronger case of fiduciary relationship cannot be conceived than that which exists between partners. "Their mutual confidence is the lifeblood of the concern. It is because they continue to trust one another that they are partners in the first instance; it is because they continue to trust on another that the business goes on" (per Bacon VC in Helmore v Smith (1890) 15 App Cas 223 at 225; (1886) 35 Ch D 436 at p 444). The relation is based, in some degree, upon a mutual confidence that the partners will engage in some particular activity or transcation for the joint advantage only. In some degree it arises from the very fact that they are associated for such a common end and are agents for one another in its accomplishment. Lord Blackburn found in this consideration alone sufficient reason for the fiduciary character of the partnership relation (Cassels v Stewart (1881) 6 App Cas at p 79). *The subject matter over which the fiduciary obligations extend is determined by the character of the venture of* *undertaking for which the partnership exists, and this is to be ascertained, not merely from the express agreement of the parties, whether embodied in written instruments or not, but also from the course of dealing pursued by the firm.* Once the subject matter of the mutual confidence is so determined, it ought not be difficult to apply the clear and inflexible doctrines which determine the accountability of fiduciaries for gains obtained in dealing with third parties. (Emphasis added)

This passage was approved by Lord Wilberforce in the case of New Zealand Netherlands Society Oranje Incorporated v Kuys & Anor. At p 1226 Lord Wilberforce says, after quoting the relevant passage of Dixon J's judgment:

That was said in the context of a partnership but the principle must be of general application.

We would with respect, accept this proposition."

12. Several cases in Malaysia accordingly adopted the approach of determining wherther on the facts there was mutual trust and confidence between joint ventureres for the proper working of their relationship to the extent that the parties to the joint venture owed fiduciary duties to each other.

13. In Hartela Contractors Ltd v Hartecon JV Sdn Bhd & Anor[14], Hartela, a Finnish company with considerable experience in the manufacture of pre-cast concrete panels used in the construction of prefabricated houses entered into a joint venture with Ferrostaal. The joint venture agreement had contemplated that contracts be obtained first for the construction of houses and finacing arranged before a factory was set up. However, the parties proceeded to set up the factory at the outset.

14. The Malaysian Court of Appeal agreed with the finding of an arbitrator that Ferrostaal had relied on the skill and expertise of Hartela in the enterprise, and Hartela "had a

[14] [1999] 2 MLJ 481

duty to use its best endeavours to ensure the success of the venture…The joint venture agreement…expressly stipulates such an obligation in the form of the ‘ best endeavours clause’ That meant that Hartela was under a duty to use its best endeavours to promote the interests of (the joint venture company). (The decision to set up a factory before obtaining contracts or financing) was not in the best interests of (the joint venture company). Hartela knew that. It was the expert. It should have warned Ferrostaal of the danger. That was the extent of the fiduciary duty. But it failed to warn Ferrostaal. That…amounts to a breach of fiduciary duty in the circumastances of the present cae.”

15. In Kuan Chit & Ors v Daro (M) Sdn Bhd[15], the plaintiff, a registered proprietor of a piece of land entered into a joint venture with the defendant, a developer, who undertook to develop the land into a housing scheme. Under the building plans, a portion of the land was reserved for the construction of a road and a mosque. The defendant, pursuant to a power of attorney granted by the plaintiff, surrendered the reserved portion of the land to the government. However, knowing that the reserved land was not so requried, the defendant had the land alienated to it, and developed the land for itself.

16. The joint venture agreement made clear that as between the plaintiff and the defendant "…this Agreement shall not create any form of partnership whatsoever between them.." but also provided that "the parties declare that it is their intention that this Agreement shall operate between them with fairmess and without detriment to any of them…"

17. Heliliah J found that there was a fiduciary relationship between the joint venture parties and gave the plaintiff declarations that it was entitled to a portion of the market value of the land alienated to the developer.

[15] [2009] 9 MLJ 661

18. In Ezzen Heights Sdn Bhd v Ikhlas Abadi Sdn Bhd[16] the plaintiff and the defendant entered into a joint venture agreement to jointly develop the plaintiff's land. The plaintiff was entitled to 4 lots and the defendant 8 lots. The plaintiff terminated the joint venture agreement after completeion of the development project and sold the defendant's lots to a third party. The Court of Appeal, as one of the grounds for finding the plaintiff liable to the defendant in the defendant's counterclaim for the deivery of the defendant's lots by the plaintiff found[17] that the plaintiff, being a party to the joint venture agreement owed the defendant fiduciary duties, including the duty of utmost good faith, and that the plantiff had breached its fiduciary duties to the defendant.

19. The Singapore and Malaysian cases illustrate the evolution to adopting a more flexible approach of deciding whether or not on specific facts the parties to a joint venture agreement could be found to owe any fiduciary duties to another. The recent English case of Ross River Limited, Blue River Limited Partnership v Waveley Commercial Ltd, Peter Barnett & Others[18] highlighted in Lesley Anderson QC's paper proceeded on the pleading that the joint venture agreement gave rise to a relationship of trust and confidence to the parties to the agreement and is consistent with the evolving flexible approach.

20. The Malaysian cases illustrate that fiduciary duties may be more likely to be found in the context of a joint venture where the joint venturer has assumed responsibility, or at least a large degree of control, over the other joint venturer's affairs, especially if the other has little experience or expertise in the matter[19].

21. However there is an important distinction in starting from the premise that there is a partnership, and the premise that there is only a joint venture. Unlike partnerships that are inherently fiduciary, joint ventures are not. Indeed joint ventures are usually

[16] [2011] 4 MLJ 173
[17] at [25] and [26]
[18] [2012] EWHC 81
[19] The pointers in the English cases in the joint venture context in Lesley Anderson's paper [2.6] are equally appropriate in the local context

detailed contractual agreements which are likely to set out the bargain for the distribution of risk and reward, and the main standards of conduct to be applied between joint venturers. Accordingly, any undertaking by any joint venturer of a relationship of trust and confidence to the other joint venturers has to arise out of and be circumscribed by the contractual terms[20]. It is not likely to be easy in such a context for fiduciary duties to be found to arise.

Kenneth Tan SC

[20] See as recent examples in England of Ross River Limited and F&C Alterative Investments

Finance, Property and Business Litigation in a Changing World

Concurrent Session 2C: Trust Formation and Administration

Speakers

Mr Michael Gibbon QC, *Maitland Chambers*

Associate Professor Kelvin Low, *School of Law, Singapore Management University*

FINANCE, PROPERTY AND BUSINESS LITIGATION IN A CHANGING WORLD

CONCURRENT SESSION 2C: TRUST FORMATION AND ADMINISTRATION

Speakers:
Mr Michael Gibbon Q.C.
Maitland Chambers

Associate Professor Kelvin Low
Singapore Management University

<u>REFERENCE MATERIALS</u>

<u>What is a trust? Requirements for formation of a valid express trust/Control by the Court</u>

Armitage v Nurse [1998] Ch 241
Re Beloved Wilkes's Charity (1851) 3 Mac. & G. 440
Breakspear v Ackland [2008] EWHC 220 (Ch); [2009] Ch 32
Convention on the Law Applicable to Trusts and on Their Recognition, Art 2
Knight v Knight (1840) 3 Beav. 148
Morice v Bishop of Durham (1805) 10 Ves. Jr. 522
McPhail v Doulton [1971] AC 424
Re Manisty's Settlement [1974] Ch 17
Recognition of Trusts Act 1987
Schmidt v Rosewood Trust [2003] UKPC 26; [2003] 2 AC 709
Whishaw v Stephens (Re Gulbenkian) [1970] AC 508
Re Wood [1949] Ch 498

<u>Trusts which are "shams" by formation; relevance of administration to identification of "sham"</u>

A v A [2007] EWHC 99 (Fam); [2007] 2 FLR 467
Re The Esteem Settlement [2004] WTLR 1
Goodright v Wells (1771) Dougl. 771
Hill v Spread Trustee [2006] EWCA Civ 542; [2007] 1 BCLC 450
Hitch v Stone [2001] EWCA Civ 63; [2001] STC 214

MacKinnon v Regent Trust Co. [2005] WTLR 1367
Midland Bank v Wyatt [1997] 1 BCLC 242
Minwalla v Minwalla [2004] EWHC 2823 (Fam); [2005] 1 FLR 771
Rahman v Chase Bank [1991] 1 JLR 103
Shalson v Russo [2003] EWHC 1637 (Ch); [2005] Ch 281
Snook v London and West Riding Investments [1967] 2 QB 786

<u>What is a trust? Rights & Obligations of Parties in the Administration of a trust</u>

Leigh & Sullivan Ltd v Aliakmon Shipping Co Ltd (The Aliakmon) [1986] AC 785
MCC Proceeds Inc v Lehman Brothers International (Europe) [1998] 4 All ER 675
Vandepitte v Preferred Accident Insurance Corp of New York [1933] AC 70
Hayim v Citibank NA [1987] AC 730
Barbados Trust Co Ltd (formerly CI Trustees (Asia Pacific) Ltd) v Bank of Zambia [2007] 2 All ER (Comm) 445
Jennings v Mather [1902] 1 KB 1
Re Johnson (1880) 15 Ch D 548
Chappell v Somers & Blake [2004] Ch 19
Malkins Nominees Ltd v Société Financière Mirelis [2004] EWHC 2631
P & A Swift Investments v Combined English Stores Group Plc [1989] 1 AC 632
City of London Corporation v Fell [1994] 1 AC 458
Boyer v Warbey [1953] 1 QB 234
Shell UK Ltd v Total UK Ltd [2011] QB 86
Cheng-Wong Mei Ling Theresa v Oei Hong Leong [2006] 2 SLR(R) 637

<u>Arbitration clauses in trusts</u>

Trust Law Committee, 'Arbitration of trust disputes' (2012) 18 *Trusts and Trustees* 296
Nicholas Le Poidevin Q.C., 'Arbitration and trusts - can it be done?' (2012) 18 *Trusts and Trustees* 307
Lawrence Cohen Q.C. and Joanna Poole, 'Trust arbitration - is it desirable and does it work?' (2012) 18 *Trusts and Trustees* 324
Re Lysaght [1966] Ch 191
Re Butlin's Settlement Trusts [1976] Ch 251
Day v Day [2013] EWCA Civ 280
Williams v Earle (1868) LR 3 QB 739
Old Grovebury Manor Farm Ltd v W Seymour Plant Sales and Hire Ltd (No 2) [1979] 1 WLR 1397
Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd [1994] 1 AC 85
Tulk v Moxhay (1848) 2 Ph. 774
Saunders v Vautier (1841) Cr. & Ph. 240
Bruno W. Boesch, 'The ICC initiative' (2012) 18 *Trusts and Trustees* 316
Vandervell v IRC [1967] 2 AC 291
Re Vandervell's Trusts (No 2) [1974] Ch 269

Verbatim Transcript of Concurrent Session 2C: Trust Formation and Administration

M: What is a trust? There is no single definition. Just for today, I will start with a "working" definition of trust, as seen on the trust. A trust has the following characteristics ((a)-(c) on slide). It strikes me that there's a conspicuous aspect and that is the issue of control.

There are many quotations on this element of control.

E.g. Lord Eldon LC in Morice v Bishop of Durham (1805) 10 Ves Jr 522, at 539: "The principle… is this. As it is a maxim, that the execution of a trust shall be under the control of the Court, it must be of such a nature, that it can be under control."

Sir William Grant in Morice: "there can be no trust, over the exercise of which this Court will not assume a control for an uncontrollable power of disposition is ownership, not a trust."

Harman J in Re Wood [1949] Ch 498, at 501: "A gift on trust must have cestui que trust."

Schmidt v Rosewood: "It is fundamental to the law of trusts that the court has jurisdiction to supervise and if appropriate intervene in the administration of a trust, including a discretionary trust."

M: We also have the 3 certainties which everyone is familiar with. My focus today is on the certainty of objects. As seen on the slide:

Fixed trust: Lord Upjohn in Re Gulbenkian

Discretionary trusts: McPhail v Doulton

Power to add beneficiaries: Re Manisty's Settlement

M: Lord Walker in Rosewood talks about "modern" discretionary trusts, which have special advantages in terms of confidentiality, wide discretions in favour of a widely-defined class of beneficiaries and the concept of the concealed settlor: "a cloak against transparency."

The essence of all these is the problem that: might certain "modern" trusts be unenforceable? One solution is the court's principled approach to "regard the right to seek disclosure of trust documents as one aspect of the court's inherent jurisdiction to supervise, and if necessary to intervene in, the administration of the trust." (Schmidt v Rosewood)

M: By moving away from the proprietary aspect to the disclosure of documents, it gives rise to enforceability because the court can always exercise its inherent jurisdiction. However, this also means that even beneficiaries of fixed trusts do not have absolute interests in such circumstances. What they have is the right to ask the court to exercise its discretion, which may or may not be in the beneficiaries' favour.

For the last point, I cite the case of Breakspear v Ackland. If trustees make an application to the court on whether they should disclose the settlor's letters of wishes, it is inevitably a self-defeating application since they have to produce the documents in the first place.

Administration of a trust

K: I'm starting with the "working" definition of a trust and I'm going to focus on a number of parts within this definition. The definition uses the word "assets" and not "property". It is important to note such differences. For example, the distinction between property rights and personal obligations are clear, but choses in action are considered properties.

Some academics define a trust as an equitable obligation. Such definition has been criticised.

For example: Let's say we have a starship and we have trustees and beneficiaries. It looks like 2 relationships interacting with the thing

But the picture is wrong. When we look at equitable property, the subject matter of the equitable interest is a right, not the thing itself. Thus, what the beneficiary has is a right against the right of the trustee.

Another example: If the starship is destroyed, who can, and should sue? Starting with the beneficiary, case law is quite established that a beneficiary cannot sue in his own name for what a stranger has done to the property (MCC Proceeds v Lehman Brothers). Regarding trustee: In Malkins Nominees v Societe Financiere Mirelis, the court stated that the loss of the shares was the loss of the trustees. Thus, the trustees could recover substantial damages.

Some of you may know that even though beneficiaries cannot sue in his own name, he can still use the principle in Vandepitte v Preferred Accident. The beneficiaries sue the trustees to force the trustees to sue the promisor. What you actually have is not a direct action by the beneficiaries, but a way to bring two actions into one proceeding, a shortcut. This ties in with the new understanding that a beneficiary's right is a right against the trustee's right.

However, you can't always take advantage of the Vandepitte procedure. Lord Templeman in Hayim v Citibank said that the beneficiaries have no action against 3rd parties except in certain circumstances, thus the Vandepitte procedure is NOT available as of right.

In Land law, the passing of covenants that touch and concern land only happen when they is a legal assignment. But if we look at a trust as creating a right to a right, this can be explained. It is quite clear the equitable owner has no right to the right of the legal owner. There is no privity of estate.

Next, we very often refer to the trust as if the trust exists, as if the trust is a legal person, e.g. the trust suffered a loss. This is not actually how trusts work. The trustee's liabilities are personal and do not amount to the trust value (in the absence of fraud). A creditor cannot execute against the trust assets. Instead, the trustee has a right of indemnity against the trust or the beneficiary. The creditor claims against the trustee who then claims from the trust of beneficiary. However, this right of indemnity can be lost.

"Sham" trust

M: There are two overlapping areas for consideration based on case law – "sham" by formation as well as the relevance of administration to the identification of "sham".

What do I mean by "sham"? The seminal case is Snook v London and West riding Investments [1967], i.e. "acts done or documents executed by the parties to the 'sham' which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations" different from what they actually are.

Rahman v Chase Bank [1991] JLR 301 states: "The settlement was a sham in the sense that it was made to appear to be what it was not… The trustee was never made master of the assets. KAR intended to and in fact retained control of the capital and income of the trust fund throughout his lifetime".

How far can Rahman be applied? It is actually set back in Re Esteem Settlement [2004] WTLR 1 at [54]: "In order to find a sham, the Court must find that both the settlor and the trustee had the intention that the trust position should be otherwise than as set out in the trust deed which they both executed." Thus, they must share an intention to mislead, which narrows the decision in Rahman. Re Esteem also stated that it is not a sham if the trustees "genuinely exercise their obligations" in good faith despite following the settlor's request.

Other cases that concern "sham" trusts:

Midland Bank v Wyatt [197] 1 BCLC 242, at 252h.

Hitch v Stone [2001] STC 214 (tax and land law case). 5 general principles concerning sham para (64)ff

Shalson v Russo [2005] Ch 281 at para [190]; but the case has been criticised regarding the settlor's "unspoken" intention.

Family law context: Minwalla v Minwalla [2005] 1 FLR 771, at [57]-[58]

A v A [2007]: If a non-shamming trustee is appointed, the trust may be valid, even if it was previously a sham, from the date of appointment of the current trustee.

Key conclusions for "sham" trusts:

Normal question is whether there was a "sham" at formation, but subsequent admin and conduct is relevant to assessing that

Shamming intention must be shared

Shamming trust could turn into non-shamming trust if new non-shamming trustees are appointed.

Arbitration

K: Conclusion of the Trust Law committee that arbitration clauses in trust documents don't work because only the courts can enforce the obligations of the trustees has been criticised. One retort is that if beneficiaries take whatever they're entitled to from the settlor by the latter's benevolence, why should they not take the conditions attached, such as arbitration clauses?

If you have non-assignment clause in lease agreements, it does not actually prevent assignments. It only ensures that there is a breach if there is assignment. But if there are non-assignment clauses in contracts, they actually do prevent assignments. Thus, we allow parties to do a lot more in contracts than in property rights. Since trust law is more a proprietary concept, it is not appropriate to argue that just because you can do something in contract means you can do the same thing in trust.

If we can analogise arbitration clauses with choice of law clauses, perhaps the court is less likely to exercise their discretion to order a stay.

How about 3-parties scenario (settlor transfer property to trustee). 2 hurdles:

Is there an agreement? Just because there is settlor and a trustee in the picture doesn't mean there is an agreement. We know that if a trustee disclaims the trust, the trust will not fail and the court can appoint a new trustee. If that is the case, perhaps the consent of agreement of the trustee is not that essential in this kind of situation. Also, in the case of rectifying documents, cases say that unless there is bargain that results in the trust being set up, the only relevant intention is that of the settlor, not the trustees.

How to bind the beneficiaries? In England, the key provision is s 82(2) of the Arbitration Act 1996. In Singapore, we don't have such a provision and may be an insurmountable problem. Even in England, some commentators have suggested that beneficiaries may or may not fall within the provision because the beneficiaries' rights do not derive from the settlor since the latter prima facie has no rights in the trust.

One other possibility if you really want to make arbitration clauses work is that suggested by Underhill and Hayton: trust of a covenant to arbitrate and make it part of the trust.

Also, there is an ICC Model Arbitration Clause for International Trust Disputes: make beneficiaries agree to be bound by the arbitration clauses. The potential problem is what you see in Vandervell v IRC. If you make agreements to arbitrate, there will always be a gap and thus a resulting trust, which will result in unpleasant tax consequences.

Finance, Property and Business Litigation in a Changing World

Concurrent Session 2D: Schemes of Arrangement

Speakers

Mr Lee Eng Beng SC, *Rajah & Tann LLP*

Ms Catherine Addy, *Maitland Chambers*

Assistant Professor Tracey Evans Chan, *Faculty of Law, National University of Singapore*

Session 2D:
Schemes of Arrangement

Lee Eng Beng SC
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CHANCERY BAR
SINGAPORE ACADEMY OF LAW

- Schemes first introduced in the UK in 1870 for companies in the course of winding up. Extended to all companies in 1907: see *Re Savoy Hotel* [1981] 1 Ch 351 at 358-359.
- In Singapore, schemes were introduced in first Companies Act in 1967. Based on English and Australian provisions.
- No substantive legislative amendment since then. For legislative history of s 210, see *Oriental Insurance* [2008] 2 SLR(R) 121 at [31]-[41].

- Since early 1990s, schemes have completely eclipsed judicial management (similar to UK administration) as a corporate rescue or debt restructuring regime in Singapore.
- Heavy usage, accumulation of ground experience and a substantial amount of local case law have created a corporate insolvency regime with Singapore characteristics.
- Significant differences between the UK and the Singapore experience.

- In essence, a scheme is a proposal between company and its creditors for compromise of the creditors' claims, approved by majority in value and 75% in value of each class of creditors present and voting at the scheme meeting, and sanctioned by the Court.
- Prevents a small minority from frustrating a debt restructuring exercise.
- Reverses the effect of creditor apathy.

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- Flexibility to accommodate commercial terms of debt restructuring, but a scheme is voted on as a package. No option to accept some terms and reject others.

- Two court applications - an initial application for the convening of creditors' meetings, and a subsequent application for court sanction after requisite majority creditor approval has been obtained.

- Creditors are required to be divided into classes, based on how their rights will be affected by the proposed scheme.

- Application may be made for limited moratorium against creditor action, once there is a proposed scheme (s 210(10)). Key difference from English provision.

- Singapore courts have adopted practical and commercially sensible approach in granting moratorium and sanction.

- Emphasis on due process and proper disclosure, and finality upon sanction - general reluctance to intervene in the commercial terms of schemes.

- Schemes are preferred by financially distressed companies because management remains in possession and can opt for its choice of financial advisor and/or scheme manager.

- Less adverse publicity than judicial management.

- Less risk of disruption to company’s normal business operations, and suspension of listing.

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- Schemes are available for foreign companies, and can be effected for corporate groups.
- Schemes are forward looking; less risk of inquiry into past transactions.

- Key legal and practical issues remain.
- Classification of creditors: imprecise test, complexity of modern financing and credit transactions, treatment of contingent claims, discounting of votes in lieu of different classification.
- Proof of debts: no legislative framework, no independent adjudication, treatment of disputed debts, transparency to all scheme creditors – judicial clarification given in *TT International Ltd* [2012] 2 SLR 213.

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- Issues relating to supervision and regulation of financial advisors and/or scheme managers. See *TT International Ltd (No 2)* [2012] 4 SLR 1182.

- No statutory protection of creditors and restrictions on company's transactions during period of moratorium.

- Nature and extent of judicial supervision over process and terms of scheme is not settled.

- Potential for scheme process to develop into unique debtor-in-possession insolvency regime for Singapore?

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A JOINT CONFERENCE OF THE SINGAPORE ACADEMY OF LAW AND THE CHANCERY BAR OF ENGLAND AND WALES

25 & 26 April 2013
Supreme Court
Singapore

Session 2D:
Schemes of Arrangement

Lee Eng Beng SC
Rajah & Tann LLP

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FINANCE, PROPERTY AND BUSINESS LITIGATION IN A CHANGING WORLD

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The Scheme of Arrangement as a Corporate Rescue Mechanism

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Outline

- Organic development of s.210 into a corporate rescue mechanism
- Continuing issues in the s.210 process
- Looking over the horizon

Organic development

- Rise of the SOA process as the preferred mechanism of choice for corporate rescue/restructuring
- Limitations of Judicial Management
  - Adverse market signalling
  - Loss of managerial control – especially in a market of many closely held public-listed companies
  - Reliance on SOA anyway to effect a restructuring

Organic development

- Limited moratorium on creditor enforcement
  - Yet continues to be read liberally
  - *Re TT International* [2010] – stay on *commencement or continuation* of all proceedings against the company.
- Purposive implementation of classification requirement
  - *Royal Bank of Scotland v TT International* [2012]
    - Broad practical and objective approach
    - Avoid impractical mushrooming of classes that could result in the creation of unjustified minority vetoes

Organic development

- Advance directions on classification
  - The English Practice Statement [2002] approach was endorsed recently in *RBS v TT International* [2012]
- SOA reach extends to
  - A wide range of creditors beyond the scope of the winding up proof of debt rules
  - Unliquidated tort claimants
    - *SAAG Oilfield v Shaik Sukol* [2012]
  - Unaccrued tort claims?
    - *B&S Distributors Pty Ltd* (1986) *Cf. Re T& N Ltd* [2006]

Organic development

- SOA reach extends to third party rights and obligations
  - As long as it is explicitly provided for: *Daewoo Singapore* [2003]
  - Similar development in England: *Re La Seda de Barcelona SA* [2010] EWHC 1364 (Ch)
- Principle of transparency
  - Disclosure of material information for informed voting
  - Extends to provenance of claims supporting proofs
  - Terms of scheme manager's remuneration agreement
    - *RBS v TT International* [2012]

Organic development

- Adaptation of insolvency norms and processes for creditor protection
  - *Pari passu* principle influential *but not* mandatory
    - *Hitachi Plant Engineering v. Eltraco* [2006]
  - Liquidator duties adapted to apply to scheme manager and chairman of the s.210 meeting
  - Proof of debt mechanisms and rights of appeal
    - *RBS v TT International* [2012]
    - *SAAG Oilfields v. Shaik Sukol* [2012] – unliquidated claims
  - Review of scheme manager's remuneration
    - *RBS v. TT International* [2012] (No.2)

Continuing issues

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Jurisdiction to sanction schemes

- *Section 210(11)*
- *Re TPC Korea* [2010]
  - Applies the substantial connection test in winding up of foreign companies
  - *Dicta* suggesting that substantial connection will be interpreted narrowly:
    - To enable an orderly distribution of Singapore located assets in favour of eligible Singapore creditors.
  - Critical to Singapore's position as a restructuring centre.
    - See English developments, e.g. *Re Rodenstock GmBh* [2011]; *Re PrimaCom Holdings* [2012]- sufficient if governing law of the restructured facilities is English law.

Vote discounting

- Thus far, vote discounting has been used only in relation to votes counting towards the majority
  - Handling of debt assignments and share-splitting
- Can this extend to opposing votes, in order to bring votes across the statutory threshold?
  - Australia – statutory amendments made to address problem: Corporations Act 2001, s.411(4)(a)(ii)
  - Provisions of s.210 and reasoning in *UDL Argos* do not seem to support going this far:
    - Jurisdiction to sanction rests on the initial voting threshold

Vote discounting

- Developing two stage approach?
  – Presumptive suspicion
    - Related party claims – shareholders and wholly owned subsidiaries: *RBS v TT International* [2012]
  – Otherwise, *prima facie* case for discounting needs to be made out:
    - *Wah Yuen Engineering v. SCM Pte Ltd* [2003]
    - Difficult scenarios:
      – Vulture funds – buy debt at a substantial discount; seeking a quick profitable exit.
      – Partially held subsidiaries; JV companies

Inter-class cram downs

- *Re Tea Corp* principle: classes with no economic interest in assets need not be consulted.
- Competing analyses of the different judgments in *Re Tea Corp*
  – Cramdown on classes "out of the money" – scheme binding on them nonetheless
  – SOA only in relation to classes that have an economic interest in the company – other classes technically not bound by the scheme
- No case yet in Singapore on this important issue:
  – Defines the bargaining space under the SOA framework
  – Can of worms?
    - Valuation problems and information asymmetry, but encourages negotiated outcomes – e.g. use of options to capture upside value.

Involuntary creditors

- Scope of SOA – "creditor" under s.210
- Treatment of such claims under the SOA
  - Onus now on company and court to make appropriate provision for unliquidated tort or other claimants
    - *SAAG Oilfields v. Shaik Sukol* [2012]
  - Effective solution?
  - Essentially a priority issue:
    - Separate classification? – see *Third Parties (Rights against Insurers) Act* – automatic transfer of rights of co. against insurers to third party claimant
    - Amendment to the Act to include schemes of arrangement?

The scope of judicial discretion

- The Singapore courts have thus far arguably taken a pro-restructuring outlook
  - A Chapter 11-type vision articulated by the former CJ:
    - "the Court of Appeal… not only ordered a re-vote on a scheme of arrangement to address the grievances of the creditors that it lacked transparency, it also imposed conditions for sanctioning the scheme after the second vote *to allow itself a continuing supervisory role in implementing the scheme*. In other words, the court interpreted s 210(4) of the Companies Act[16] broadly to enable it to allow the company to be reorganised in a manner almost resembling a Chapter 11 reorganisation.
  - S.210(4) – court may grant approval subject to such alterations or conditions it thinks just

The scope of judicial discretion

– Thus far, the courts have taken the initiative to:
  - Send a scheme back to the creditors' meeting for re-vote
  - Force scheme company and scheme managers to renegotiate remuneration terms
  - Amend the terms of the scheme as proposed to satisfy opposing creditor concerns
– What is the proper balance between party autonomy and judicial intervention?

Looking over the horizon

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Broader moratorium?

- Various calls for a broader statutory moratorium under s.210
  - Whatever the ambiguity, unlikely that "proceedings" can be given a wider meaning than in s.227B for JM.
  - Should we go further and sweep in security and quasi-security interests?
    - Certainly necessary to prevent unilateral action scuppering a viable scheme: see e.g. *Sea Assets v. Garuda Indonesia* (2001) EWHC (Ch) unreported.
    - But a broad extensive moratorium may send the wrong signal to creditors.
  - Compromise – a broad, but *discretionary* moratorium?

Governance framework of SOAs

- Tension in corporate rescue policy
  - Advantages of allowing management to continue vs. the real potential for abuse and self-serving behaviour
  - Some proposals or methods to address this:
    - Integrated or hybrid model of governance
      - Board comprising existing management and external trustee with veto powers to protect creditor interests
      - Cf. s.176(10A) Malaysian Companies Act
    - Dedicated monitoring agent for the creditors/creditors' committee
      - E.g. Monitor under s.11.7, Canadian Companies Creditors' Arrangement Act; appointments of "CROs" in some cases
    - Menu approach where selection of measures made on a case by case basis.

Schemes of Arrangement

Catherine Addy

Barrister - Maitland Chambers

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- **Arrangements with creditors of insolvent companies.**
- **Scheme of Arrangement ("SOA") v. Company Voluntary Arrangement ("CVA")**
- *"if the company is insolvent, the objective of the scheme may be more simply and economically achieved by a company voluntary arrangement"* but *"a scheme .. has the advantage that the court may approve the distribution of assets otherwise than in accordance with the creditors' strict legal rights"*;
  paragraph 20.15 of the Chancery Guide

SOA v CVA

Brief overview of SOA process:

- **Governed by Part 20, Companies Act 2006, which applies "*where a compromise or arrangement is proposed between a company and (a) its creditors, or any class of them, or (b) its members, or any class of them*"**

- **Procedure is essentially a 3 stage process:**
  - **Court hearing to summon relevant class meeting/s**
  - **Holding of the various class meetings**
  - **Court hearing to sanction the decisions of the meetings**

Breaking that 3 stage process down further:

- Company draws up proposal for scheme and identifies relevant class/es of creditors who will be affected.
- Company files application at court to summon meetings
- **Substantive court hearing: court considers whether to summon relevant class meeting/s and their composition**
- Notices summoning the meetings and Explanatory Statement are circulated
- **Separate class meetings are held and votes cast**
- *If the meeting/s approve the scheme*, **further court hearing to sanction the decisions of the meeting/s** and make any orders required to give effect to the scheme; <u>Re National Bank Limited</u> [1966] 1 WLR 819 @ 829A-C (and s900)

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The oft quoted passage from Buckley

*"In exercising its power of sanction the court will seek first that the provisions in the statute have been complied with; second that the class was fairly represented by those who attended the meeting and that the statutory majority are acting bona fide and are not coercing the minority in order to promote interests adverse to those of the class whom they purport to represent and thirdly, **that the arrangement is such as an intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve**.*
*The court does not sit merely to see that the majority are acting bona fide and thereupon to register the decision of the meeting; but at the same time the court will be slow to differ from the meeting, unless either the class has not been properly consulted, or the meeting has not considered the matter with a view to the interests of the class which it is empowered to bind, or some blot is found in the scheme." [**emphasis added**]*

What is required for 'approval'..?

- ***"a majority in number representing 75% in value of the creditors or class or creditors … present and voting either in person or by proxy at the meeting summoned"***
  (s899(1) CA 2006)

- **i.e. 2 hurdles: SOA must be approved by:**
  (i) a majority in number of those present and voting ("the numerosity threshold") <u>and</u>
  (ii) by persons representing 75% in value of those present and voting ("the value threshold").

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SOA v CVA

Brief overview of CVAs:

- **Governed by Part I of the Insolvency Act 1986 and corresponding Insolvency Rules**
- **Their purpose is to enable a company to enter into "*a composition in satisfaction of its debts or a scheme of arrangement of its affairs*", referred to as a "*voluntary arrangement*".**

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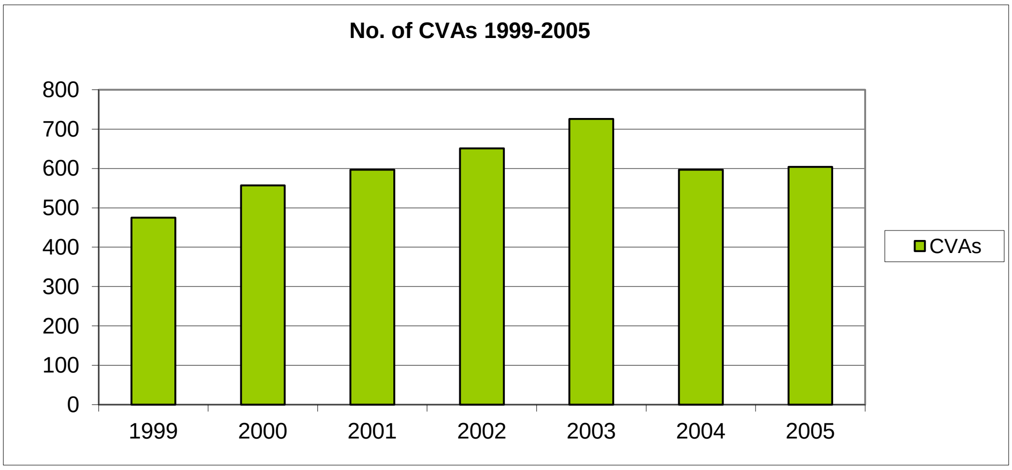
- **The reasonably widespread use of CVAs can be demonstrated by the following data extracted from the Insolvency Service's Interim Evaluation Report on the Insolvency Act 2000:**



Source: Companies House and the Department of Trade and Industry

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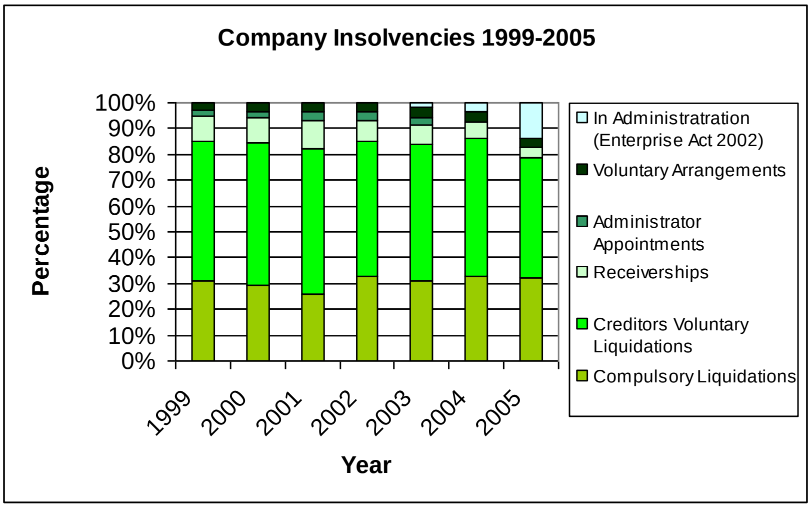
Source: Department of Trade & Industry



Company Insolvency by Type	1999	2000	2001	2002	2003	2004	2005
Compulsory Liquidations	5,209	4,925	4,675	6,230	5,234	4,584	5,233
Creditors Voluntary Liquidations	9,071	9,392	10,297	10,075	8,950	7,608	7,660
Receiverships	1,618	1,595	1,914	1,541	1,261	864	590
Administrator Appointments	440	438	698	643	497	1	4
Company Voluntary Arrangements	475	557	597	651	726	597	604
In Administration (Enterprise Act 2002)					247	457	2257

Brief overview of the CVA process:

- **Step 1: directors formulate the "Proposal" to the company and its creditors 'for a composition in satisfaction of its debts or a scheme of arrangement of its affairs'**

  The proposal is "*one which provides for some person ("the nominee") to act in relation to the voluntary arrangement either as trustee or otherwise for the purpose of supervising its implementation; and the nominee must be a person who is qualified to act as an insolvency practitioner …*"
- **Step 1A: A 'small company' may apply for moratorium**

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Brief overview of the CVA process: …

- **Step 2: proposal is submitted to the nominee together with a statement of the company's affairs**
- **Step 3: within 28 days, the nominee submits a report to the court stating that he is of the opinion that the proposed CVA has a reasonable prospect of being approved and implemented and that the meetings of the company and its creditors should be summoned to consider the proposal**
- **Step 4: meetings of the company and of 'every creditor of the company of whose claim and address the nominee is aware' are summoned by the nominee; the Proposal (and statement of affairs) is circulated with the notice of the meeting (at least 14 days in advance)**

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Brief overview of the CVA process: …

- **Step 5: meetings decide whether to approve the Proposal.** Proposal is approved when:
  (a) *"voted for by more than one half in value of the members present in person or by proxy and voting"*; and
  (b) *"a majority of three-quarters or more (in value) of those [creditors] present and voting in person or by proxy have voted in favour of it"*; IR 1.19-1.20
- **In calculating the "value threshold" –**
  - **secured creditors are left out of account, and**
  - **the creditors' resolution is invalid if those voting against it include more than half in value of the creditors, excluding persons who are not connected to the company.**

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Brief overview of the CVA process: …

- **Upon approval, CVA takes effect:**
  "*as if made by the company at the creditors' meeting*" and "*binds every person who…(i) was entitled to vote at that meeting (whether or not he was represented at it) or (ii) would have been so entitled if he had had notice of it, as if he were a party to the voluntary arrangement*"; s5 IA 1986
- (Nominee, who is now "Supervisor" of the CVA, files a report at Court confirming outcome of meetings)

SOA v CVA

- **Who can they bind?**
  …….. the meaning of "creditor"

- **Future/contingent liabilities:**
  - Re Midland Coal, Coke & Iron Company [1895] 1 CH 267 (SOA)
  - Re Cancol Ltd [1996] 1 All ER 38 (CVA)
  - Re T&N Ltd (No 3) [2006] EWHC 1447 (Ch)

SOA v CVA

- **Bondholders?**
  Consider:
  Re Dunderland Iron Ore Co Ltd [1909]1 Ch 446;
  Re Castle Holdco 4 Limited & Ors [2009] EWHC 1347 (Ch); and
  The Enfranchisement of Bondholders in the Marconi Schemes of Arrangement (2003) 11 JIBFL 421

- **Secured creditors (SOA only)**

- **By contrast, a CVA cannot adversely affect the rights of either a secured or a preferential creditor without their individual concurrence; see ss4(3)-(4) IA 1986.**

- **Re Lehman Bros International (Europe) (No 2) [2009] EWCA Civ 1161 – *an attempted step too far***

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SOA v CVA – some key distinctions:

SOA		CVA
• court procedure and associated expense	v	out of court process
• as many meetings as classes	v	one creditors meeting
• Numerosity threshold and value threshold	v	no additional numerosity threshold
• creditor approval is subject to judicial discretion	v	effective upon creditor approval (subject to unfair prejudice challenge)
• (currently) no moratorium	v	moratorium available for 'small' companies
• greater flexibility in content	v	more limited utility

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SOA v CVA

- **Brings us back to where we started:**

  *"if the company is insolvent, the objective of the scheme **may** be more simply and economically achieved by a company voluntary arrangement"* **but** *"a scheme .. has the advantage that the court may approve the distribution of assets otherwise than in accordance with the creditors' strict legal rights"* *

  *paragraph 20.15 of the Chancery Guide

Catherine Addy, ***Maitland Chambers***

Schemes of Arrangement

Catherine Addy

Barrister – Maitland Chambers

Verbatim Transcript of Concurrent Session 2D: Schemes of Arrangement

LEB

Intro to schemes of arrangement

Schemes modelled on English provision, taken on life of own in terms of practical experiences, what happens on the ground, court's perpective.

One significant mod to English provision is subclause that allows companies applying for schemes of arrangement to arrange for moratorium. 210(10) CA. provision remained unchanged since.

Since 1990s schemes overtaken JM as restructuring regime. Never took off. By 1990 schemes a lot more popular with companies. from 1990s to today heavy usage, ground experience, almost like debtor in possession insolvency regime. Courts prepared to give 6 months, even 18 months for company to do scheme. Issues moratorium. Company can get maybe 24 months protection against creditors even while it works out its plans. Significant differences between uk and sg exp.

[brief overview of CA provisions]

no option for creditors to negotiate. Package deal. Negotiations are done before company proposes deal, powerful creditors have meetings and express wishes to company.

Q: in England, composition of classes dealt with early at initial application. How in sg?

A: in SG, court of appeal said recently that it's open to ask at initial application. But in sg large numbers of creditors, so notice to all of them, submissions

Q: but how about representative creditors?

A: who would fund it? To be very cynical sg lumps everyone into the same class and hopes no one objects.

The period between initial application and scheme approval can be very long. Court has been willing to grant extensions as long as creditors support

Q: advantage: we have administration+ a scheme in uk usually. Administrators can apply to court for direction. For example, when comparing scheme scenario to insolvency position, would have to ask court what insolvency position is.

A: can do a scheme in JM, but JM's not popular. Very very few schemes done by jm

General observations. Sg courts practical and professional in granting applications, some might say 'liberal' but in recent years courts have been scrutinising reasons to give moratorium. Period of time in mid 1990s where companies abused it, tried to give creditors a raw deal. Usually a few weeks now and they get the company to get an extension.

Emphasis is on due process and proper disclosure. Reluctance to intervene in commercial terms of schemes. One exception TT International – amended terms of scheme. Amendment after creditors made submissions about why they wanted changes.

Why not JM?

People invoke it way too late, by the time the judicial manager comes in there's no much to save. Increasing complexty of business, unrealistic to think that accountants can come in, churn out statement of proposal in 90 days, 150 days, even a year, when management hasn't been available to do that. So JM not effective corp rescue mechanism.

Companies like schemes, less adversity. JM seen as precursor to liquidation. When you publicise schemes, public reaction is that no one knows what this means. Solvent companies use it too. Companies would prefer this. Less risk of suspension in case of a listed company.

Once company goes into JM, bank sets-off everything, suppliers insist on cash, employees quit, customers go elsewhere. Not for schemes.

Schemes available for foreign companies, corporate groups. Holding company does scheme for benefit of group. For JM may have to put entire group under JM. No restriction on foreign companies.

Also one more thing – no inquiry into past transactions. JM/liquidator will inquire into past transaction.

Topical issues

Still uncertainty with classification of creditors, complexity of modern credit. Many types of security, contingent claims, etc. Issue with different financing transactions and instruments. Issues with treatment of contingent claims. How to treat creditors when claims not crystallised but payments going on?

Courts can say that in lieu of different classification they can discount votes of certain groups, related companies, etc.

No legislative framework for proof of debt. Who does it, what material has to be supplied etc. What happens now is proof of debt mechanism provided in document or explanatory statement, but no binding force until scheme has been sanctioned, and you can't saction until you prove debts. Quite a lot of judicial comments in tt international where court laid guidelines on how manager should adjudicate on claims,whether creditors who think other debts shouldn't have admitted should have access to documents etc.

Issues with regulation o scheme managers. TT (no 2) what happened there was that there was a scheme manager with a success fee arrangement allowing him to be paid 5% of debts restructured. Not disclosed. Scheme manager also adjudicating debts. Argued that material information, if creditors knew, they might have voted differently. Problem was discovered after scheme was sanctioned. Normally court would have set aside sanction, but since everyone proceeded on the basis that it was sanctioned, what they did was that overall remuneration of manager to be taxed by high court. Taxed on basis of liquidators. Never really explained how they got that power.

No statutory protection of creditors, no restrictions on company's behaviour during this period. Because we allow companies to apply, started out as simple provision allowing company to be given respite, but how companies operate is that they ask for a blanket moratorium and courts grant it. But who looks out for creditor's interests? No court officer. In tt cases, COA a bit more aggressive in supervising scheme process including amending terms after sanctioning. Decided that some proofs of debts not adjudicated on correctly, and if proper, would have failed voting. But told creditors to go back to revote after the adjustments and they passed it.

Future direction for sg. Scheme successful, practical, efficient way of restructuring. Balanced carefully need for proper disclosure, creditor democracy and ability to determine terms, but some judicial supervision over possible abuse and oppressive tactics. One hope is that sg could develop into a restructuring hub for companies in region. Committee looking into insolvency reform to address some of these issues highlighted.

Tracey Evans Chan

Schemes preferred because perceptions of JM. Moratorium technically against present proceedings, but courts just order over future proceedings too. Not supportable on language but practical.

Endorsed English practice statement for pre-classification of creditors, but potential problems with creditors who didn't/couldn't make representations at first hearing.

Broad interpretation of who can be bound by scheme. Unliquidated tort claimants. But unaccrued tort claims? Australian authority to the contrary, claimant that can be put on notice and be part of meetings.

Audience: and it changed the rules for insolvency too.

There is a downside to this – if there are other ways that claimant could have gotten compensated, may not be happy to be bound by scheme.

Audience: English caselaw a bit misleading, any big restructuring is two years of work. Dissenting creditors are bought off. That information is never disclosed to the court. No doubt that if there are secret bribes to creditors, that's wrong. But seems to be allowed. No one's actually disclosed 'to get to this stage, we paid this much'.

LEB: alwaysthought that if creditors were bought out, that breaches equality expectation of creditors.

We're not getting people complaining at the sanction stage since they don't know that this is being done. At least for us, we're looking at company in negotiation period. Canadian model – statutory observer who's supposed to report to at least the creditor's committee.

Back to third party rights. Schemes can extend to directors guarantees too.

Audience: if a particular third party right is given up by virtue of being bound into a class, that would be dealt with by unfairness or irregularity. But if that class agrees to give up rights, it's okay.

Audience 2: you're talking about compromising rights of third parties. But can't interfere with obligations TO third parties.

As long as you include it expressly in the scheme it's okay. But how it can be done is include third parties as contingent debtors. So they can assert that claim as parties to the scheme themselves.

Audience 2: so where the third party is happy to participate it's possible. I've come across situations where third party rejected scheme. Put one borrower into scheme, but other creditors outside scheme.

Depends on how crucial that point is to the scheme. But if you expressly include it in the scheme, is possible.

LEB: surely company and creditor can agree not to discharge but

We've been quite aggressive in importing insolvency norms. Pari passu can be avoided but need good reasons. liquidator duties apply to scheme manager, proof of debts can be appealed to court, even payment to manager.

Jurisdiction to sanction schemes in Singapore is the same. As long as jurisdiction is there to wind up company, jurisdiction is there to scheme. One decision at high court level. Applies substantial connection test, dicta that subst connection test will be interpreted narrowly. "Assets in sg not enough. To enable orderly distribution of sg assets to sg crediors." I think that's too narrow – sometimes it's about rights and obligations, not just assets. Restructuring not distribution. Uk is more open, we could go with that route.

Audience: But that derives from an insurance case. And also in Germany schemes may be recognised as a judgment.

In this area the more sensible case is [first case] which said that jurisdiction+substantial place of business? Has to be present. No point getting scheme if it's not recognised where it matters.

Two basic points about discounting. No doubt that courts discount. Can bring it under threshold by discounting yes votes. But can you discount no votes and sanction the scheme? Opponents can sometimes assign debts to reduce numbers.

Developing a two stage approach in discounting. Presumptive suspicion by related parties and shareholders – taken out. Apart from that, I read wah yuen to say that you must show some prima facie case to show that votes should be discounted. How about vulture funds that buy up debt cheaply?

Audience 3: court has discretion not to approve.

Yes. Vulture funds – prefer to make a quick buck by liquidating assets. Is this something a court should consider in deciding?

In US bankruptcy judge can sanction scheme over objections of creditors.

Re Tea Corp – people with no economic interests in assets need not be consulted. But how does this work? Claims out of the money can be crammed down, or claims out of the money not bound by scheme? Done frequently in UK, which is that you can value company at going concern value and eliminate lowest rung creditors. Hasn't been done in SG, but could be a useful tool.

Recognising this could deal with the holdout problem in classes. But is this going to open a can of worms? Valuation is troublesome. My view is yes, but the court has to be cautious in sanctioning scheme where this re tea cramdown has been used.

Last point. I find this case much more interesting. Involuntary creditors. We've had a recent case (SAAG oilfields), employees who had potential tort claim. Definition of creditors under scheme would have covered tort claims. One didn't know, other didn't turn up to vote. So they were cut off from potential coverage from insurance over these claims. Court took wide reading of creditors, caught by scheme. But recognised potential injustice because insurance cover was lost. Solution to this is that onus is on company and court to make provisons for unliquidated tort claimants. But it assumes a bit much that companies or court will know that there are claims out there. Separate classification necessary? Third parties against insurers act transfers insurance to claimants. But doesn't apply to scheme unlike UK. Maybe this should be amended so it kicks in in schemes too. But another way is for court to amend scheme once this has been discovered.

I was going to talk about how we should improve schemes but maybe another time.

Catherine Addy

I want to limit what I'm talking about to SOAs with insolvent companies. We essentially have two schemes, schemes and company voluntary arrangements ("CVA"). Consideration's been given to CVAs in the Singapore insolvency legislation.

Practitioners reminded that in insolvency, objective sometimes more easily achieved with CVA, but scheme may rearrange rights more easily, not in accordance with strict legal rights.

In terms of identifying creditors, test is still "so dissimilar that they can't consult sensibly". Have to look at rights both outside and inside the scheme to identify. Application to court to call meetings. Substantive court hearing – court decides whether to summon meetings and composition of classes.

Unless there are good reasons for not doing so, applicant must take all reasonable steps to notify people affected by scheme, proposed classes, etc. by time of application, creditors should have all this information. Court can also appoint representative creditors.

Test for sanctioning: buckley. Procedural correctness, bona fide, "intelligent and honest man [of each class] might reasonably approve". Company has to report on how meetings have been held, issues raised, etc. creditors can complain about conduct.

SOA v CVA

Governed by part 1 of insolvency act. CVAs introduced 1986. Reasonably well used.

Step 1: Company proposes for some person to act as trustee or supervise implementation. Insolveny practitioner. If small company, get automatic moratorium.

LEB: why only to small companies?

Good question that's the legislative decision at this moment. There's been some consideration. But it's about economic impact. Impact on the larger economy not so significant for small economy, moratorium affects more creditors for large.

Step 2: proposal submitted to nominee.

Step 3: nominee reports to the court in 28 days that CVA has reasonable prospect of approval, should summon meetings.

Step 4: meetings convened

Step 5: 1/2 in value and numbers of members, 3/4 of creditors in value must support. Secured crditors taken out.

[see slides – just explaining slides]

And that's it. No court involvement in process. Only court involvement is if there's a challenge – so if complaints from credtors.

Who can they bind? Creditors. No definition of creditors. Caselaw definitions. Judiciary says that it has to be interpreted in widest sense. Re midland coal, re cancol, re t&n. contingent creditors also bound. Really taken as far as it can go, potential tort claimants.

Bondholders? Can be bound. Who is person who can exercise vote for purposes of vote? Trustee was found to be creditor, not beneficiaries of the debenture. 1909 case. Risky case, now try to use the ultimate beneficial interest as voters, but have to use some mechanism for that.

Secured or preferential debts can't be bound by CVAs but not SOAs.

Re lehman bros international (Europe) (no 2) – so hopeless that couldn't find out who the beneficial owners were. All owners would exchange property interests under scheme for claims under scheme. But court rejected – scheme can't deal with property rights. Can't extinguish property rights. Only obligations.

Difference: schemes, heavy court involvement+costs, cva out of court process. Cva only one meeting. CVAs no numerosity threshold. CVAs auto-approved. No moratorium for SOAs, but for CVAs, small companies.

Summary – much greater flexibility with schemes, CVAs more limited, but depending on the creditors involved and what you want, CVAs maybe better. No moratorium for SOAs, but for CVAs, small companies.

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