Dishonest Assistance – Understanding the Risks: Guidance Note

This Guidance Note is about dishonest assistance and will explore the legal position of those in the Island's professional trust and fiduciary services businesses who have carried out client instructions without first considering or investigating the legitimacy of their client's activities. It will use practical examples to illustrate what can go wrong, particularly centering on the recent decision of Jersey's Royal Court in Nolan v Minerva Trust & Others, and will suggest how businesses should act to avoid the risk of being held to have dishonestly assisted a client in a breach of trust or fiduciary duty.

Dishonest assistance is a category of secondary liability that can attach to a person who assists in a breach of trust or a breach of fiduciary duty. The breach of trust itself (the primary liability) need not be dishonest, although it often will be. Rather it is the assistance in that breach of trust by a third party, such as a service provider, which has to be dishonest. While in common parlance, dishonesty is usually equated with conscious wrongdoing, dishonesty in the context of dishonest assistance has a broader meaning with the potential to bring the unwary within its scope.

Nolan v Minerva Trust & Others [2014] JRC078A

This case concerned a fraudster, Gerard Walsh. Walsh was an apparently successful Irish businessman and ultimate beneficial owner of the Buchanan group of companies, all of which were incorporated in Jersey. The Royal Court concluded “that by 2005, at the latest, Mr Walsh had become a fraudster”. Walsh’s business empire collapsed by 2009.

The defrauded investors were the Nolans, a large Irish family who had made their money through road haulage. Joan Nolan, aged 29, was charged by the Nolan family with investing the family’s savings. Joan Nolan and her family, despite their business success, were not financially sophisticated people and were impressed by the facade Gerard Walsh presented when he approached them to invest their money in his companies.

The dishonest assistant was Professional Trust Company Ltd (“PTCL”). PTCL provided directors to the Buchanan companies and undertook general administration and bookkeeping for them. Minerva Trust Company Limited (“Minerva”) merged with PTCL in 2007, and was named as the defendant in the proceedings because, under the terms of its merger with PTCL, it had inherited all PTCL’s liabilities.

Gerard Walsh claimed to offer a variety of investment opportunities in companies he owned and ran. These investments were discussed only between Joan Nolan and Gerard Walsh. There was no contact between PTCL and the Nolans. In total the Nolans made eight investments equalling £5.3 million, plus a further €8.4 million. Funds were advanced to the Buchanan companies to make these investments; however the money was not used to purchase investments for the Nolans but was used instead to fund Gerard Walsh’s lifestyle and pay his overdrafts. These payments were effected by PTCL, on Gerard Walsh’s instructions, and any shares that were purchased with the Nolan’s money were worthless.

When the fraud was uncovered, efforts to pursue Walsh directly were ineffective. As well as having acquired liabilities for the actions of PTCL as part of its merger, Minerva made itself a target by continuing to argue Gerard Walsh’s case thereby supporting his defence. Minerva disclosed its documentation to the Nolans under a disclosure order, revealing its state of knowledge and degree of assistance in Walsh’s fraud.

Dishonest Assistance

Dishonest assistance gives a victim of a breach of trust a cause of action against a person who has assisted a primary wrongdoer (i.e. the trustee or other fiduciary) in that breach. As a secondary head of liability an action for dishonest assistance can be pursued independently of the original breach of trust claim. It is irrelevant that the assistant does not have (and may never have had) the assets that have been misapplied in breach of trust. Where dishonest assistance is proven, it gives rise to a personal liability to compensate the victim of the breach of trust from the assistant’s personal assets, as if the assistant were the primary wrongdoer. As is often the case in fraud claims, the primary wrongdoer will be insolvent or in such financial distress that it is impractical to obtain recovery from their personal assets. Where, as in Minerva, a large institution is identified as the assistant, an action for dishonest assistance can provide the victim of a
breach of trust with a solvent defendant against whom it can recover what the victim is unable to recover from the primary wrongdoer.

There are four basic elements that must be proven in order to ground a claim for dishonest assistance:

- The existence of a trust in favour of the plaintiff to the action;
- A breach of this trust;
- That a third party has assisted in the breach of that trust; and
- That in giving that assistance, the assistant acted dishonestly.

**Existence of a Trust**

For the purposes of a dishonest assistance claim, a trust can arise in a myriad ways. Strictly speaking the foundation of a dishonest assistance claim is based upon there being a fiduciary duty. There is no need for a formal document or express trust, although this will suffice. A trust may arise informally on the basis of a particular set of facts. Such a trust is known as a “constructive trust”. A constructive trust is a legal artifice that will arise by operation of law where the law considers it would be unconscionable for a person (A) who holds an asset, to deny the beneficial interest of another person in the asset. Instead A must hold it on trust for the true beneficial owner. The Court will order the return of property or its proceeds, and/or compensation and disgorgement of profits made by the constructive trustee. A fiduciary duty, in the nature of a trust, will also come within the meaning of ‘trust’ for these purposes. Therefore the duties owed to a company by its directors are a trust in this regard. A breach of those duties (such as a misappropriation of the company’s property by the director) may give rise to a constructive trust in favour of the company.

In Minerva, there was no express trust but the court considered that, on the facts, two species of constructive trusts had arisen; a Halley Trust (so named from the English case of *Halley v Law Society* [2003] EWCA Civ 97) and a Quistclose Trust (so named from the English case of *Barclays Bank Ltd v Quistclose Investments Ltd* [1968] UKHL 4).

**The essence of a “Halley” Trust** is as follows: Money is paid by A to B under a contract. B knows the contract is impossible to perform, or has no intention of performing it. The contract was therefore a charade or scam to get hold of A’s money. The trust exists from the moment the contract for which the money is paid is impossible to perform i.e. the creation of the trust and its breach are in effect simultaneous. On the facts in Minerva, a Halley Trust arose over the money paid by the Nolans to Walsh for him to invest because the investments he told them he would make were a charade in that Walsh never intended to invest their money at all.”

**The essence of a “Quistclose” trust is as follows:** A pays B money, both agreeing it is to be used by B for a specific purpose only. This money does not form part of B’s general property to use as he wishes. The Trust exists from the time the money was received, and is breached as soon as it used for another purpose.

**Breach of Trust**

It is usually straightforward to establish that a breach of trust has occurred once a constructive trust arises; the existence of the trust and the breach often occur simultaneously. Often the breach involves the misapplication of the property subject to the trust. In the Halley trust, the breach is when the fraudster obtains funds. In the Quistclose trust, the breach is when money is applied to a purpose other than that agreed.

**Assistance**

What amounts to assistance in each case is highly fact specific. The requirement is that whatever assistance is provided, it must in fact assist in the breach of trust. Assistance need not be the sole cause of the breach, it may simply enable it. It isn’t necessary to prove that the breach could not have happened without the assistance, nor will it necessarily be a defence to say that the breach would have happened anyway without the assistance. The assistance will normally precede the breach or be contemporaneous with it. Once the breach of trust has been fully implemented, subsequent acts or omissions of the assistant will not assist its commission because the breach of trust has already been committed. However, in those cases where the breach of trust consists of misappropriation of assets, the breach
will be a continuing one and will not end when the assets have initially been removed from the trust fund but only when
they have been hidden away from the reach of the beneficiaries. The assistance will normally take the form of
channelling, investing or otherwise using the money representing the trust property while it is in the course of being
laundered, even though it occurs after the initial misappropriation.

In Minerva, PTCL made the payments which plainly assisted Walsh in his breach of trust. Other examples of assistance
could be (but are not limited to) acting as trustee or director of a company used as part of a fraudulent scheme. Because
the assistance does not have to be the sole cause of the breach, more tangential assistance may suffice, such as
providing a correspondence address, the provision of bookkeeping services and/or incorporating companies –
provided it actually assists in the breach of trust.

**Dishonesty: Civil v Criminal Cases**

The dishonesty element in a claim for dishonest assistance is more complex than first appears. The test applied in
criminal cases is not applicable. There are two aspects of the criminal dishonesty test. Firstly there is an objective test:
was what the defendant did dishonest in accordance with the ordinary standards of a reasonable and honest person? If
the answer is ‘yes’ then it is necessary to proceed to a second, subjective test: did the defendant himself realise that was
he did was dishonest by those standards?

This subjective element is not used for the purposes of establishing whether a person was dishonest for the purposes of
dishonest assistance.

The dishonesty standard in civil cases is objective: "Not acting as an honest person would act in the circumstance." The
Defendant’s own standards of honesty are irrelevant as is his belief (however genuine) that he was acting honestly. See
37.

In the case of Royal Brunei, the following conclusion was drawn concerning the limits of subjectivity as a defence:

“Carelessness is not dishonesty. Thus for the most part dishonesty is to be equated with conscious impropriety.
However these subjective characteristics of honesty do not mean that individuals are free to set their own standards
of honesty in particular circumstances. Honesty is not an optional scale, with higher or lower values according to the
moral standards of each individual.”

In the case of Barlow Clowes, this idea is developed:

“If by ordinary standards a defendant’s state of mind would be characterised as dishonest, it is irrelevant that the
defendant judges by different standards. X had an exaggerated notion of dutiful service to clients, which produced a
warped moral approach that it was not improper to treat carrying out clients’ instructions as being all-important…. X
may well have thought this to be an honest attitude, but if so, he was wrong.”

It is not necessary for the assistant to know there is a trust, what a trust is, nor to know the details of the trustee’s (i.e. the
primary wrongdoer’s) conduct: Someone can know, and can certainly suspect, that he is assisting in a misappropriation
of money without knowing that the money is held on trust or what a trust means.

An honest person is deemed to be taken to make inquiries as soon as he/she is suspicious. Taking a risk that the
primary wrongdoer has prejudiced the interests of other people can mean the person taking that risk is dishonest. The
underlying principle is that an honest person should have little difficulty in knowing whether a proposed transaction, or his
participation in it, would offend the normally accepted standards of honest conduct.

A court will look at all the circumstances known to the third party at the time of the assistance. The court will also have
regard to personal attributes of the assistant, such as his experience and intelligence, and the reason why he acted as
he did.

This taking into account of ‘all the circumstances’ was important in the Minerva case, where the Royal Court took
account of the statutory and regulatory environment that PTCL worked in:
“The environmental and regulatory background essentially required PTCL/Minerva to be honest, adequately protect funds it controlled which were not its own, [and] know and understand the transactions it was undertaking, into which it should make active inquiry.”

**Regulatory Requirements for PTCL**

PTCL was subject to the following regulatory laws which will be well known to those working in Jersey’s finance industry:

- Financial Services (Jersey) Law 1998,
- Financial Services (Trust Company Business (Assets – Customer money)) (Jersey) Order 2000,

As far as PTCL’s “state of mind” was concerned, conscious knowledge of impropriety was not needed; suspicion on its part concerning Walsh’s activities was enough. PTCL’s knowledge of the circumstances was shown to have accumulated over time. It was contained in the records and in the minds of its staff. Knowledge that an honest officer of PTCL would have acquired on one occasion was held to have informed PTCL’s state of mind in a subsequent transaction. This was described by the court as “cumulative knowledge”.

No individual PTCL directors were pursued at trial, as no one individual had sufficient knowledge when combined with the requirement of having rendered assistance to Walsh. Three officers gave evidence before the Royal Court and were extensively cross-examined. Two were found to have given unsatisfactory evidence, and to have acted in ways that were dishonest.

PTCL (and thereby Minerva) was found to be dishonest because it:

- Always followed Gerard Walsh’s instructions without challenge;
- Knew that money coming in from the Nolans and payments going out were for Gerard Walsh’s personal benefit;
- Followed Gerard Walsh’s instructions not to contact the Nolans;
- Agreed to Gerard Walsh’s instructions to lie to others;
- Accepted Gerard Walsh’s explanations which looked objectively were implausible.

**The Columba Deal**

An example of this was with regard to a company called Columba. Gerard Walsh purchased Columba, the business of which he described to the Nolans as being “management solutions for information retrieval” in 2005 for €6, plus an earn-out consideration, all of which PTCL knew. Columba never made any profit and so no earn-out consideration was ever paid. Gerard Walsh told Joan Nolan a few months after buying Columba that he had bought Columba for €7 million, and he would let the Nolans buy 25% at cost price. The Nolans therefore paid €1.75 million to acquire 25% of Columba which in fact was only worth €1.50.

PTCL held no documents recording the origin of the €1.75 million payment into Buchanan, but knew it was from the Nolans for Columba shares. PTCL knew the funds were not invested in Columba at all but were all used for Gerard Walsh’s benefit: cars for his children, a deposit on a flat in Eaton Square and legal bills. PTCL did not query any of these payments; they just made them at Walsh’s instruction.

PTCL then sent Joan Nolan a nominee declaration regarding 25% of the Columba shares but PTCL, on Gerard Walsh’s instructions, still recorded and declared the Buchanan company as sole holder of all Columba shares and voting rights. The court declared that “it is clear to us that PTCL simply never took the Nolans seriously as shareholders in... Columba.”

In relation to Columba, the court concluded that on the facts a Quistclose trust had arisen – money was invested by the Nolans purely to buy Columba shares, not to fund the Buchanan Group generally. When the money was not used to invest in Columba this gave rise to a breach of trust. PTCL’s payments to fund Walsh’s lifestyle amounted to assistance in that breach, and PTCL was dishonest – their lack of surprise at the vastly inflated purchase price was described as being “wholly astonishing”.

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The publicly available judgment contains quoted passages from the transcripts of the evidence of the Minerva officer under cross examination that make for uncomfortable reading:

**Q:** Do you know of anything that changed between May 2005, when you purchased this company, and September 2005 when you sold a quarter of it the Nolans to make this company suddenly become worth more than a million times what you paid for it?

**A:** No. […]

**Q:** And you made no enquiries at all as to why such a large sum would be paid for such a worthless company?

**A:** It wasn’t understood that the company was worthless at all. As I said, I wasn’t surprised at the time. It was no doubt discussed with Mr Walsh…

The Court stated that:

“An honest trust officer in the position of [X] would at the very least have queried whether… the transaction was “bona fide and honest or otherwise”. The fact that both [X] and [Y] did not share the view that Mr Walsh’s deal with the Nolans was extraordinary only goes to show… that neither of them in fact gave the deal any thought or any independent consideration all.”

In brief, PTCL should have asked the Nolans what they thought they were getting for their €1.75 million.

The Conclusion of the Royal Court in respect of the Columba investment was:

“For the reasons we have set out above, we conclude that the conduct of [X] (and through him of PTCL) in relation to the Columba investment was commercially unacceptable and that he, and through PTCL, were guilty of dishonestly assisting BHL’s breach of the Quistclose trust in [the Nolans’ investment vehicle]’s favour.”

**Lessons from Nolan v Minerva?**

Quite simply, do not be a puppet for your client; instead you should be alert and sceptical. It is important to understand and be clear as to the relationships between the legal and natural persons to whom you provide services. Are they the settlor, the beneficiaries, an investor? Do not rely on the fact that your client has no criminal convictions and remember that a request to redact or amend documents, or to record something in an inaccurate or non-standard way, should trigger alarm bells.

Anything giving cause for concern should be recorded prominently on the file, and reported to the service team. All those working on a client’s affairs should be aware of the client’s history, so that they can put any developments into context.

If the client refuses to provide explanations, persist in asking until (s)he gives one with which you are comfortable. If you receive an explanation, subject that explanation to rigorous scrutiny. Do not just accept anything that you are told. If you are given an explanation that is inconsistent with an earlier explanation, or with documents or other facts known to you, then that is unacceptable.

Once you know your client has lied, even if not to you, always require independent verification of what (s)he says. This may require seeking direct confirmation from those whose money is at risk. If you are discouraged by your client from talking to those people, that is a cause for serious concern. Once you have a concern that anything improper might be happening, any payments must be embargoed while it is investigated.

**Warning signs of fraud include:**

- Wide disparities in prices (e.g. Columba);
- Investments offering very high guaranteed returns and no loss to capital;
- Funds not used in a way consistent with the ‘pitch’ to investors;
- Secrecy;

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• The use of euphemisms such as “commissions” that may be sent offshore for no obvious or legitimate reason.

Limitation

The limitation period on claims for dishonest assistance is three years after the dishonest assistance occurs but it is important to note that time only begins to run from the date when the Plaintiff has sufficient evidence to plead dishonesty – this can only happen when there is reasonably credible evidence of fraud. The concealment of facts, as will be common in fraud cases, means that time may not begin to run until sometime after the dishonest assistance has occurred.

The defences available on a claim of dishonest assistance are limited. Besides limitation the only other defences generally available are concurrence by the beneficiary of the trust that is said to have been breached in the dishonest assistance, or release. As with concurrence, for a beneficiary to give a release, they must be an adult and have capacity to give a release and must have all proper information available to him to give the release freely.

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