Guernsey, INSOL Channel Islands: The future of crime, taxation and auditors offshore

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Ogier partners **Mathew Newman** in Guernsey and **Bruce MacNeil** in Jersey report from an INSOL seminar in Guernsey in June, which examined the future challenges for offshore insolvencies, particularly as regards taxation, auditors and when criminal investigations and insolvency clash.

INSOL's Channel Islands 2019 seminar took place in Guernsey on 20 June. The theme of the conference was "The future" with a series of forward-looking panels designed to get delegates talking about how our profession is going to be adapting to new types of asset classes and their interaction with various areas of law. The conference was ably chaired by **Karen Le Cras** from Carey Olsen in Guernsey and **Ed Drummond** from Bedell Cristin in Jersey.

Before the main programme began, **Justice Paul Heath**, formerly of the New Zealand High Court and on his first visit to Guernsey, talked to delegates about INSOL's mediation programme, which had been designed to provide an alternative dispute resolution service on cross-border restructuring and insolvency matters. Due to the service being under-used, it was dis-established, but the message was that INSOL is still very interested in providing mediation services in the insolvency sector and delegates were encouraged to get involved.

Crime v insolvency

The first session, entitled "When crime and insolvency collide" was chaired by **Alan Roberts** from Grant Thornton in Jersey, with speakers **Patrick Crothers** from the UK National Crime Agency, **Laura Hatfield** from Bedell Cristin in the Cayman Islands and **David Standish** from KPMG in London. The session was divided into three parts, all examining the conflict between criminal investigations/confiscations, and the civil recovery for creditors that a formal insolvency process results in.

Standish, an experienced insolvency practitioner specialising in contentious fraud cases, provided insights into two current cases, one of which is a current Jersey case. He looked at the primacy of criminal confiscation orders over an insolvency process, often depriving an insolvent estate of any assets at all, and talked about issues of privilege and Insolvency Act 1986 powers that are hampered as a result of those criminal investigations.

Hatfield, following a similar line, discussed the recent Cayman cases of Caledonian Bank and Abraaj, both of which involved criminal investigations by US criminal agencies that interfered with, and restricted the ability of, the Cayman insolvency practitioners appointed over those entities to bring about a return to creditors. In particular, a freeze put on Caledonian Bank by the SEC had caused a run on the Bank, which led directly to its insolvency – a process criticised by the US judge in that case.

The other side of the coin was put forward by Crothers, a current officer at the NCA with substantial experience in economic crime in Northern Ireland in particular. He focussed on the need for police intervention in the recovery of proceeds of crime, with far wider powers than any insolvency practitioner would have; the expansion of non-conviction based asset recovery; and unexplained wealth orders, which also do not necessarily lead to a conviction.

Crothers made it clear that the objective was to repatriate the proceeds of crime with the victims of those crimes and his conclusion appeared to be that civil recovery in an insolvency, and criminal investigations leading to a confiscation order or similar, actually end up with the same result – victims or creditors gaining a recovery of the sums that they had lost to the fraudster.

Taxation offshore

The next session, entitled "What is making waves offshore" was presented by **Jo Huxtable** from Deloitte in Guernsey, **James Quarmby** from Stephenson Harwood in London and **Matthew Gilbert** from Maples Group's British Virgin Islands team in London. The speakers discussed a range of international tax and transparency initiatives impacting the offshore world including the US's Foreign Account Tax Compliance Act (FATCA), which requires foreign financial institutions to report the assets of anyone who was born or ever lived in the US to the Department of the Treasury. They also discussed the OECD's common reporting standard (CRS) introduced in 2014 for global banks and tax authorities to combat tax evasion; base erosion and profit shifting (BEPs) strategies used by multinationals to shift profits from jurisdictions with high tax to low tax regions; beneficial ownership registers; black lists of tax havens; and substance requirements that require companies present in certain low tax jurisdictions to show they have genuine local substance there.

This was a topical session as on 19 June, the governments of Jersey, Guernsey and the Isle of Man jointly announced a series of steps regarding each jurisdiction's central register of beneficial

ownership of companies and how each will move towards developing international standards of transparency over the next few years. This is consistent with the EU's approach to transparency of beneficial ownership of companies under the EU's Fifth Money Laundering Directive.

Quarmby argued that, while there is strong political pressure from certain Members of Parliament and various groups in the UK to move towards greater transparency, there is a tension between transparency on the one hand and privacy, which is a human right, on the other. He argued strongly in favour of the right to privacy and against having public registers of beneficial ownership, noting that the Channel Islands and the Isle of Man already have registers of beneficial ownership which are accessible by law enforcement and tax authorities. He also noted that there is likely to be a divergence between the EU standards and the international standards on transparency over time and that the UK will need to consider its position in light of Brexit developments in future.

Huxtable discussed the substance legislation that was brought into force earlier this year in the Channel Islands, the BVI and the Cayman Islands in response to findings of the EU Code of Conduct Group for business taxation. The legislation imposes requirements relating to how relevant companies are directed and managed, ensuring that adequate activity is conducted in the jurisdiction of tax residence and ensuring that the relevant Core Income Generating Activities (CIGAs) are conducted in the jurisdiction of tax residence. Gilbert compared and contrasted the introduction of substance legislation in the Channel Islands and the BVI and noted the importance of adhering to developing international standards in this area.

Auditors under the spotlight

The pre-lunchtime session was chaired by **Andrea Harris** of KRyS Global in Guernsey and focussed on the responsibility of auditors in the event of a high profile or large-scale corporate collapse. **Maurice Moses** from EY in London offered an auditor's perspective whilst **Simon Salzedo QC** of Brick Court Chambers, who has written a book on auditor professional negligence, provided great insight into the test for auditor negligence and how the case law has developed since the seminal case of *Caparo v Dickman* in 1990, which established a three-part test for a duty of care to arise in negligence.

Salzedo QC made it very clear that the standard expected of an auditor is now of "professional scepticism". Moses put forward the interesting theory that auditors should no longer think of their clients as clients, because you owe a duty to your client and want to please them, which conflicts with the expected sceptic's role of the auditor nowadays. There was also a discussion about the Big 4 accountancy firms in particular splitting off their audit teams from the rest of the consultancy to avoid perceptions of conflict.

Finally, mention was made of the current Guernsey case of *Providence Investment Fund PCC Limited v PricewaterhouseCoopers*, where an insolvent fund is suing its auditor for negligence in

the sum of around £14 million (US$17.4 million) because of the auditor's failure to spot that the fund's investors were being defrauded.

The keynote speech was given by **Sandra Särav** from the Government Chief Information Officer's Office of Estonia, who presented on agility in governments and the adoption of digital technologies in Estonia. She stated that 99% of public services in Estonia are offered digitally, with only a few exceptions where physical presence is required. Särav explained that since gaining independence from the Soviet Union in 1991, Estonia has taken a digital approach to modernising its economy and has been at the forefront of adopting digital technologies in the public sector, including artificial intelligence, data embassies and e-Residency. Estonia has become a digital society and now has more tech unicorns – private companies valued at more than US$1 billion – per capita than any other small country in the world.

The next session was presented by **William Callewaert** of BDO in Guernsey, **Ben Jones** from the London office of Bryan Cave Leighton Paisner, **David Jones** of Carey Olsen in Guernsey and **William Scott-Gall** of Duff & Phelps in London. The panel discussed case studies covering recent corporate failures and enforcement actions in the UK relating to digital assets, which are a new asset class which can present legal and practical challenges in an enforcement scenario.

David Jones contrasted the security interests laws in Jersey and Guernsey and discussed the 2019 case of *Solutus Advisors v Aurium Real Estate* in which the Royal Court of Jersey showed a willingness to provide certainty and protection to a security trustee that was looking to enforce a Jersey law security interest. While the Royal Court was not willing to provide the requested order under Article 52 of the Security Interests (Jersey) Law 2012, the Court was willing to approve a proposed enforcement sale under Article 51 of the Trusts (Jersey) Law 1984. The Court found that the security trustee was deemed to be in compliance with its statutory duty to take all commercially reasonable steps to obtain fair market value for the collateral – this decision provided welcome certainty to the security trustee.

Finally, the panel discussed proposed restructuring reforms in the UK and the Channel Islands, introducing the principle of a "debtor in possession", a restructuring moratorium and a court-approved restructuring plan – these are all concepts that will be familiar to US bankruptcy lawyers and are likely to be adopted in the UK in future.

The final session was entitled "Let Battle Commence – Big Case Roundup", and was chaired by Mathew Newman of Ogier in Guernsey. The session comprised four panels with four speakers talking about particular offshore insolvency cases of interest over the past 12 months.

Abel Lyall from Mourant in Guernsey talked about *Carlyle Capital Corporation v Conway*, going into some detail as to why the liquidators of the fund decided to pursue the directors, and why the claim failed at trial – essentially because the judge found that the claim was hindsight-driven. The issues were narrower on appeal, and focussed on the duties of the directors, but again the case was lost. It was confirmed that the liquidators are seeking leave to appeal to the

Privy Council.

Andrew Shaw, a barrister from South Square, talked about the Saad Investments case that he had been involved in. While the facts are too long to go into in this article, it is safe to say the Saad case – which resulted in a 1,300-word judgment in May 2018 – has given rise to more court time than any other Cayman or offshore case in recent times. There were no new points of law as such, but the sheer size of both the US$9.2 billion fraud that the judge found had been perpetrated, and therefore of the case, demonstrates that offshore courts are more than capable of dealing with complex high value cases.

David Wilson, from Oben Law in Jersey, talked about the *Z Trusts case*, which deals with the concept of an "insolvent trust". He concentrated on the first instance judgment (the Court of Appeal judgment not having been released until after the seminar had taken place on 28 June) and the finding by the Court that, in essence, a corporate-style insolvency waterfall should apply to the order of priority of creditors in the trusts, which also interacts with the question of the trustee's own remuneration and whether the trustee personally or the trust fund is liable to creditors, following the Privy Council decision in the Guernsey case of *Investec v Glenalla*.

Finally, **Kirsten Kitt** from Simmons & Simmons in London talked about her experience acting for Grant Thornton in the Tchenguiz litigation. Grant Thornton partners were appointed liquidators of 16 Guernsey trusts controlled by UK property mogul Robert Tchenguiz and four related BVI companies. The role of Kitt's firm was diverse to say the least, dealing with proceedings involving the Serious Fraud office, trust proceedings in Guernsey, judicial review proceedings and both criminal and regulatory investigations. The skills of an insolvency and restructuring lawyer need to be extremely varied, given the types of issues that arise.

Overall INSOL'S Channel Islands 2019 seminar brought together numerous active participants in the offshore restructuring and insolvency world, with sessions covering various areas that are likely to impact that world in coming years, including: crime and insolvency, digital assets, transparency initiatives, substance requirements, the future of audit, new methods of security enforcement and case law developments over the past 12 months.

Given the current economic environment, there is likely to be an increase in offshore restructuring and insolvency work over the next few years and we are certainly living in interesting times.

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