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UPDATE

Royal Court considers the nature of tripartite relationship between trustee, manager and unitholder in a unit trust context

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The Royal Court of Guernsey in *Tranquility Holdings Limited v. Invista Real Estate Investment Management (CI) Limited* (unreported judgment 38/2015) recently considered for the first time the nature and extent of the duties owed to unitholders by the manager of a Guernsey domiciled unit trust.

Background

Invista Real Estate Investment Management (CI) Limited (**Invista**) is the manager of the Invista Property Portfolio Fund (the **Fund**), an open-ended unit trust authorised as a Class B collective scheme by the Guernsey Financial Services Commission. The Fund invested in the United Kingdom commercial property market through a fund of funds approach and performed well until late 2007 when the market for commercial property suffered a downturn. The level of redemption requests in late 2007 exceeded the Fund's liquid resources and on 24 December 2007 Invista took the decision to suspend dealings in the Fund. The Fund was later placed into liquidation.

Tranquility Holdings Limited (**Tranquility**) is a unitholder in the Fund. In short, Tranquility's primary case was that Invista breached the duty of care and/or fiduciary duties it owed to Tranquility (and other unitholders in the Fund) by accepting and processing unitholders' redemption requests, notwithstanding the failure of those redeeming unitholders to provide the minimum notice required by the Fund's constitutional documents for redemption requests. Tranquility's case was that Invista thereby preferred some unitholders over others with the result that the consequent level of redemptions ultimately led to the otherwise avoidable suspension of the Fund.

Invista applied for summary judgment on and/or strike out of Tranquility's claim in its entirety (the **Application**). By Judgment dated 3 August 2015 (the **Judgment**) the Royal Court (per Bailiff Collas) granted the Application, both summarily dismissing and striking out Tranquility's claim. Mourant Ozannes acted for Invista.

The Application and the Judgment

The Application was brought on a number of grounds, including that:

1. as a matter of law, Invista does not owe Tranquility the duties alleged to have been breached. Rather, Invista's duties are limited to those set out in the Trust Instrument constituting the Fund (the **Trust Deed**);
2. in any event, Invista has not acted in breach of any duty owed;
3. even if Invista has acted in breach of duty, a unitholder such as Tranquility does not have standing to bring a claim against Invista in respect of the Fund; and that
4. Tranquility's case fails as a matter of causation.

Both the second and fourth grounds were successful.

Invista's primary submission with respect to the second ground was that in formulating its case Tranquility had treated the notice periods for redemptions as if they were mandatory. However, for each notice period

there was an element of discretion. (For example, the Trust Deed provided that redemption requests needed to be received no less than 'x' number of business days prior to the relevant Dealing Day (depending on the value of the redemption) 'or such earlier or later day as the Manager shall from time to time determine').

The Bailiff agreed that these provisions provided Invista with 'considerable discretion and latitude as to the handling of redemption requests' which had not been acknowledged by Tranquility. He thus found that Tranquility's claim was based on a false assumption that the notice periods were fixed. This meant that, in order to succeed with its claim, the Plaintiff would have to prove not that the Defendant failed to observe the fixed time periods, but that in deciding whether or not to abbreviate or lengthen those periods, it was acting in breach of its powers. That case would require expert evidence which had not been produced. The Bailiff indicated that had this been the only ground for granting summary judgment or strike out, he would probably still have refused leave to amend the claim given that the Plaintiff already had every opportunity to amend (and had in fact already amended its claim) and the amendment would be a radical alteration to its case.

In relation to the fourth ground, Tranquility's claim was, in effect, that but for Invista's failure to enforce compliance with the notice periods the Fund would have survived. It was clear however that the liquidity issues faced by the Fund were not caused solely by the level of redemption requests, but by the significant decline in the value of subscriptions for new units in the Fund, such that redemptions could no longer be paid from subscription monies (which had been the case until the downturn in the commercial property market). The Bailiff considered that it was reasonable to assume on the basis of the evidence adduced by Invista that further redemption requests would have been received and that the drop in the level of subscriptions would have continued. He thus concluded that there was no realistic prospect of Tranquility showing that the suspension of the Fund could have been avoided long enough for Tranquility to make (and have honoured) its own redemption request. Moreover, this defect in the claim was not something which could be remedied by amendment to the pleadings.

As to the first and third grounds, Invista principally relied on clause 19.1 of the Trust Deed to limit any rights of a unitholder to those expressly provided for in the Trust Deed. To subscribe for units in the Fund, unitholders were required to confirm in writing that they had read the Trust Deed and irrevocably agreed to abide by and be bound by its terms. Invista argued further that any duties it owed were to the trustee and/or the Fund only, and not to individual unitholders such as Tranquility.

As noted above, Tranquility's position was that Invista owed it and other unitholders a duty of care and/or a fiduciary duty. It relied on the Jersey case of *Barclays Wealth Trustees (Jersey) Limited (in its capacity as trustee of the R2 Bulgaria Property Fund) v Equity Trust (Jersey) Limited* [2014] JRC 102 D[1] in which Commissioner Herbert, in dismissing a strike out application, found that it was arguable that the manager of a unit trust owed fiduciary duties to unitholders and/or could be held by a court to be a trustee of the trust. Invista sought to distinguish the Barclays case inter alia on the basis of differences of wording between the trust instruments in each case and the fact that, in this case, the trustee had reviewed and affirmed Invista's actions in the Fund's annual report for the year ended 31 January 2008.

Ultimately, the Bailiff adopted the same approach as Commissioner Herbert and decided that it would be inappropriate in the context of a strike out application for him to make a legal ruling on a novel point of law which could have 'serious implications for unit trusts, for those who invest in them and for those who manage them or act as trustees'. (The Bailiff agreed that the legal position was at best arguable). He did, though, give some judicial insight (at [86] to [92]):

> 'I am persuaded that the following propositions are at least arguable. The relationship between the Plaintiff [Tranquility], the Defendant [Invista] as Manager, and the Trustee is a tripartite arrangement or a triangular relationship … it is both contractual and triangular. The Application Form executed by the Plaintiff [Tranquility] [for subscription of units in the Fund] envisaged acceptance by both the Trustee and the Manager …

[1] See our earlier update: 'R2R: The mysterious case of the unit trust'.

> The wording of the Application Form has all the features of a contract and in my judgment there is no doubt that upon acceptance of the Plaintiff's [Tranquility's] application, a contract was completed by the three parties.
>
> The Trust Instrument is very different in its terms from those of a typical private trust. It has many features of a contractual document but there is no doubt that a Trust exists, as defined in section 1 of The Trusts (Guernsey) Law, 2007. The powers and duties of the Trustee are more limited than are normally seen in a private trust because many of those duties and powers are entrusted to the Manager …
>
> In the case of the Unit Trust with which I am concerned, if it were the case that the Manager owed no duties to a Unitholder enforceable by the Unitholder, a Unitholder who sought to claim a remedy for a breach by the Manager of any of its obligations would have to take action against the Trustee for failing to take reasonable care to ensure that the Trust had been properly managed by the Manager in accordance with [The Collective Investment Scheme Class B Rules 1990] …
>
> If that were the only remedy available, it would have serious limitations …'

Comment

This decision is noteworthy because:

- it considers the legal relationship between trustees, managers and unitholders in a unit trust context. Whilst the Bailiff did not reach any firm conclusions, his thoughts (which track the Jersey Royal Court) are likely to be of interest to many in the funds industry, both locally and abroad;
- the Court was cognisant of the turmoil created by the global financial crisis and was unwilling to find Invista liable without a proper analysis of causation and loss; and
- it demonstrates that investors who have lost money (whether as a consequence of 2008 or at all) will face an uphill task without real evidence of wrongdoing.

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