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New Law Journal: Overview of fraud in the Channel islands

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In the second of a three-part series on Jersey and Guernsey law in the New Law Journal, Partner Michael Adkins, and Of Counsel James Tee along with Group Partner Simon Hurry, and Senior Associate Karen Stachura provide an overview of fraud in the Channel Islands, and the options available to victims of civil fraud in an insolvency context.

The first article in the series - insolvency in the Channel Islands - can be viewed here, and the final, third article - restructuring in the Channel Islands - can be viewed here.

Jersey

As a leading international finance centre, Jersey has sophisticated and robust measures to prevent, identify and remedy fraud. The Jersey Court has consistently and repeatedly sent a clear message that it will actively assist victims of fraud.

This short article focuses on civil fraud in an insolvency context but, in general terms, the weapons against fraud that are available in the major onshore jurisdictions will also be available in Jersey, although perhaps with a different (and often French) name.

The starting point is that no substantive cause of action is required to apply for orders which concern the identification and preservation of assets that are the subject of a fraud. This 'free standing' relief in support of foreign proceedings, coupled with the Jersey Court's willingness to assist, can be a considerable advantage.

In summary, the main weapons against civil fraud include the following:

- freezing and disclosure orders, including those against third parties;
- search and seizure orders;
- *arrêts (arrests) over property in the fraudster's hands;*
- *arrêt entre mains (arrests) over property in the hands of a third party,* being similar to an English third party debt or garnishee order but with increased flexibility as it can attach to any intangible movable property or chose in action;
- constructive trusts over assets which are the subject of a fraud, including those in the hands of an innocent party;
- knowing receipt and dishonest assistance claims against third parties; and

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- claims brought under Jersey's insolvency regime.

This article briefly explores the last category.

Customary Law

If the plaintiff can show that assets were transferred with the substantial intention to defeat the plaintiff's claim, they may be entitled to revoke the transfer under the customary law remedy known as a pauline action. This claim is brought outside of an insolvency process and has broad similarities to a claim under section 423 of the UK's Insolvency Act 1986, although in Jersey evidencing the debtor's balance sheet solvency at the relevant time(s) is an absolute defence to the claim.

Statute

The Bankruptcy (Désastre) (Jersey) Law 1990 and Companies (Jersey) Law 1991 equip an insolvency officer holder with special claims to recover assets for the benefit of a debtor's creditors. These include the unwinding of preferences (a debtor preferring one creditor over another), defeating transactions at an undervalue and claims for wrongful trading.

Particularly relevant to this article is the fraudulent trading regime, which states that any person engages in fraudulent trading if any business of a company is carried on:

- with the intention of defrauding the company's creditors or creditors of another person; or
- for a fraudulent purpose.

If it appears that fraudulent trading has occurred, the Jersey Court may order that any person who was knowingly involved in fraudulent trading make any contribution to the company's assets the Jersey Court thinks proper. The level of the contribution is therefore, in principle, unlimited.

Guernsey

Legal practitioners will find Guernsey's law largely familiar in respect of fraud and asset recovery, but there are some unique differences. The remedies and actions for civil fraud are for the most part drawn from Guernsey's customary law, and modern day actions for civil fraud in Guernsey reflects the common law position in England and Wales.

As an offshore centre the Royal Court of Guernsey will deal with claims brought for breach of trust/fiduciary duties and by insolvency practitioners (both of local and foreign companies).

There are various orders that the Court can make to assist in tracing assets which originated from the English courts, including disclosure orders such Norwich Pharmacal and Bankers Trust as well as Mareva-type freezing orders to prevent a defendant dissipating assets.

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A Guernsey customary law procedure also provides a remedy to freeze assets known as an *arrêt conservatoire*, which was traditionally used to seize property to prevent its dissipation. The *arrêt conservatoire* retains some practical usefulness in that, unlike a freezing injunction, it takes effect in rem rather than in personam.

The Pauline action has been recognised as a remedy in Guernsey law. A Pauline action enables a creditor to set aside an agreement between its debtor and a third-party recipient, which was made to defeat the interests of that debtor's creditors. It is a restitutionary remedy, so does not result in the plaintiff being awarded damages.

The Pauline action is important for creditors as the Companies (Guernsey) Law, 2008 (Companies Law), does not currently contain an equivalent to section 423 of the UK Insolvency Act, 1986.

The Companies Law does provide a statutory remedy where the business of the company was carried on with the intent to defraud its creditors. This remedy is available to a liquidator, creditor or member of the company against any person knowingly involved in the conduct. The limitation with this remedy is that the Royal Court can only order that the person contribute to the company's assets.

Section 432 of the Companies Law provides a remedy if any business of a company is carried on with intent to defraud creditors, or for any fraudulent purpose, every person who is knowingly a party to such business is guilty of an offence.

During the course of a winding up of a company it may become apparent that the business of the company has been carried on with intent to defraud creditors, the liquidator, creditor or member may apply to a court for an order that forces the director(s) to contribute to the company's assets.

The phrases "with intent to defraud creditors" and "for any fraudulent purpose" require a finding of actual dishonesty. If a company continues to carry on business and to incur debts at a time when there is, to the knowledge of the directors, no reasonable prospect of the creditors ever receiving payment on those debts.

Guernsey has many tools available to victims of fraud to protect the assets within the jurisdiction before judgment is obtained and to enforce against those assets post judgment. The Royal Court will not allow the jurisdiction to be safe haven for fraudsters and will seek to work with and enforce foreign courts orders to maintain this position.

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This article was first published in the New Law Journal and an online version of the publication can be viewed here.

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