

JERSEY COURT EXAMINES DIRECTORS' DUTIES AND RELIEF FROM LIABILITY

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The Royal Court has recently examined directors' duties in Jersey law in the case of *Vilsmeier v AI Airports International Limited and PI Power International Limited* [2014] JRC 257.

The judgment in *Vilsmeier* makes fascinating reading, not only for legal issues it discusses, but also for its Hollywood fact pattern involving Kazakh "specialists" allegedly dispatched by an Austrian bank to the plaintiff's home in Switzerland to deal with "the Vilsmeier problem", perceived kidnap attempts on the plaintiff's 11-year-old daughter, and spies on the companies' boards (apparently). As a result, the plaintiff, the former chairman of the two defendant companies, incurred hundreds of thousands of euros of security costs to hire bodyguards, upgrade his house and rent an armoured Audi A6, at the expense of the companies.

This article however focuses on the two legal topics considered: (i) directors' fiduciary duties under Article 74 of the Companies (Jersey) Law 1991 (**Companies Law**); and (ii) the Court's discretion to grant relief from liability for breach of duty under Article 212 of the Companies Law.

THE LAW

Article 74(1) of the Companies Law sets out the general duties of directors, being to:

- (a) act honestly and in good faith with a view to the best interests of the company; and
- (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

While Article 74(1) broadly mirrors the common law position, it does not codify it. Therefore, common

law considerations remain relevant when considering potential breaches of directors' duties.

Article 212 of the Companies Law provides that the Court may grant relief to a director from liability for breach of duty in connection with the office of director if it appears to the Court that the director acted honestly and that having regard to all the circumstances of the case the director ought fairly to be excused for such breach.

BACKGROUND TO THE LITIGATION

Vilsmeier concerned what the Court called the "Group 2 issues"; a reference to proceedings having previously been brought against the companies by another director, Bjorn Pirrwitz (*AI Airports International Limited and PI Power International Limited v Pirrwitz* [2013] JCA 177). The defendant companies in both *Vilsmeier* and *Pirrwitz* were public companies incorporated in Jersey as investment funds. Investors subsequently lost confidence in the companies' shares and their share prices fell making them attractive to certain hedge funds. Those hedge funds began purchasing stock with a view to replacing the directors with their own nominees and cutting ties with the other group entities.

It was against this backdrop that Mr Pirrwitz and Mr Vilsmeier were appointed to the boards of the companies. The appointments proved to be difficult; relations with both employees and the hedge fund investors became increasingly strained until both directors resigned. The *Pirrwitz* claim was brought in respect of unpaid exit payments.

Pirrwitz itself provided an illuminating judgment which in brief made the following findings:

- In relation to directors' remuneration the general rule is that a director is not entitled to remuneration out of the company's funds save as authorised by the articles of association of the company or by the company in general meeting.

“... the test to be applied to a Jersey director does not include the objective element of reasonableness applied to an English director.”

- The general duty of directors to “act honestly and in good faith with a view to the best interests of the company” is a subjective duty; it is for the directors to decide what is in the best interests of the company (acting honestly), not the court. However, the directors must act in the best interests of the company *for a proper purpose*. This on the other hand is an objective standard, not built on the honesty of the directors.

THE VILSMEIER JUDGMENT

The *Vilsmeier* claim was brought for unpaid overtime fees and security costs incurred by the plaintiff personally; the companies denied liability and brought a counterclaim for security costs paid by them. The main feature of the companies’ argument was that Mr Vilsmeier had incurred the security costs at their expense in breach of his duty to act in the best interests of each company. The claim was partially successful, and the counterclaim failed. In reaching its conclusions, the Court formed the view that Mr Vilsmeier was not in breach of his duties for most of the period in which he incurred the security costs (although he was in breach for some of the period). In the course of its judgment, the Court reiterated the findings in *Pirrwitz* regarding the duties of directors, and re-visited the meaning of ‘proper purpose’.

The Court went on to examine whether, had it been necessary, it would have granted relief to Mr Vilsmeier under Article 212 of the Companies Law. In its examination of Article 212 the Court noted that it is modelled on Section 727 of the UK Companies Act 1985 save that whereas Article 212 only requires that the director act “honestly”, Section 727 requires that

the director act “honestly *and reasonably*”. The Court therefore drew a distinction between the Jersey and English law positions, concluding that the exclusion of “reasonably” from Article 212 must indicate the intention of the Jersey legislature to depart from the English position and require honesty only. In other words, the test to be applied to a Jersey director does not include the objective element of reasonableness applied to an English director.

In carrying out its examination of Article 212 the Court also examined the nature of ‘honesty’, quoting heavily from the English case of *Royal Brunei Airlines v Philip Tan Kok Ming* [1995] 2 AC 378. To paraphrase, honesty has a connotation of subjectivity which describes the type of conduct assessed in the light of what a person actually knew at the time, as distinct from what a reasonable person would have known or appreciated, and honesty is mostly concerned with advertent conduct, not inadvertent. However, despite its subjective characteristics honesty maintains an objective standard because individuals are not free to set their own standards of honesty; a finding of dishonesty for misappropriating property cannot be avoided on the basis that an individual sees nothing wrong with such behaviour.

While Mr Vilsmeier was successful with the Article 212 argument this did not allow him to claim back the security costs paid by him in the period in which he was in breach of his fiduciary duties. The Court stated: “It is one thing to relieve him of liability for breach of duty under Article 212 but it is a step too far to accept his claim for reimbursement despite that breach of duty.” In other words, Article 212 is a shield and not a sword.

CONCLUSION

Vilsmeier, like *Pirrwitz*, increases our understanding of Jersey law on directors’ duties and Article 212 relief, and is informative to advisors and directors alike. On the other hand, these cases also emphasise the value of the shareholder authorisation procedure set out in Article 74(2) of the Companies Law.



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