Neutral Citation Number: [2019] EWHC 1375 (Comm)

Case No: LM-2018-000057

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
LONDON CIRCUIT COMMERCIAL COURT (QBD)

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: 04/06/2019

Before :

Andrew Henshaw QC
(sitting as a Judge of the High Court)

- -

Between :

GLOBAL CURRENCY EXCHANGE NETWORK LIMITED	**Claimant**
- and –	
OSAGE 1 LIMITED	**Defendant**

- -
- -

George Hilton (instructed by **Howard Kennedy LLP**) for the **Claimant**
David Warner (instructed by **Meaby & Co Solicitors LLP**) for the **Defendant**

Hearing date: 8 March 2019
Draft judgment circulated 6 May 2019

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Approved Judgment

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ANDREW HENSHAW QC

Mr Andrew Henshaw QC :

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(A) INTRODUCTION

1. The Claimant ("***GCEN***") is an FCA-registered payment institution which provides foreign exchange and payments services to clients. It holds sums of £101,926.81 and €89.50 ("***the Funds***") in accounts referable to the Defendant, one of GCEN's clients. The Defendant ("***Osage***") used GCEN's services to receive, convert to US dollars and transfer funds intended for investment, via Osage, in an oil drilling venture in Osage County, Oklahoma.

2. Some of GCEN's bank accounts were frozen in 2015, and in September 2016 GCEN obtained from Osage's solicitors a copy of what appears to have been an intended application by the Metropolitan Police under section 295 of the Proceeds of Crime Act 2002 ("***POCA***") for the continued detention of £50,000 cash stated to have been seized from GCEN, naming Osage and others as persons likely to be affected by detention of those funds ("***the CDA document***").

3. These events led GCEN to perform its own analysis of Osage's accounts with GCEN. In the light of this analysis and the contents of the CDA document, GCEN says it considers there to be a real foundation for an expectation of claims from investors to the Funds, on the basis that Osage may have procured the Funds from investors by deceit and/or misrepresentation and/or unlawful mis-selling practices, and that Osage may be operating a Ponzi scheme (i.e. a scheme whereby later investments are used to

pay purported returns on earlier investments in order to create an illusion of genuine investment returns).

4. In March 2018 GCEN issued the present CPR Part 8 claim in the form of an interpleader application pursuant to CPR Part 86. CPR Part 86 allows a stakeholder to apply to the court for a direction as to where it should pay a debt or money where competing claims are made or expected to be made against the stakeholder in respect of that debt or money by two or more persons.

5. GCEN accepts that the Funds do not belong to it, and says it is content to pay the Funds to whichever party or parties the court may direct. It anticipates competing claims because:

   i) Osage claims the Funds and has previously threatened an injunction and proceedings to recover them, and

   ii) if investors were made aware of the details of Osage's investment scheme, GCEN expects that they too would make claims against it for the return of the Funds.

   GCEN at this stage seeks directions for the service of its application and evidence on various investors to allow them the opportunity to make legal claims to the Funds.

6. Osage's position is that the proceedings should be dismissed. It points out that GCEN has received no indication of any potential investor claim to the Funds in the 3½ years since Osage's accounts with GCEN were frozen. Osage says GCEN has simply decided unilaterally to withhold payment of monies it holds on Osage's behalf, based on the contents of the CDA document: which is unsigned and was never issued. Osage also submits that there is no plausible legal basis on which an investor could have a relevant claim to the Funds (as opposed to a claim against Osage which the Funds might be used to satisfy) even if he/she had a legal claim of the kind GCEN envisages might be made. GCEN is, on Osage's case, seeking via its Part 86 application an indemnity to which it is not entitled, and should instead simply hand over Osage's money.

7. This case came before HHJ Klein (sitting as a Judge of the High Court) on 25 January 2019. The Judge required GCEN to set out in writing the legal basis for the existing or potential competing claims which it contends might be brought in respect of the Funds, and a succinct factual summary based on the evidence before the court and relevant to those claims. Osage was then to respond in writing. The Judge directed that the present hearing be listed, with a time estimate of half a day in order to:

   > "(a) Determine whether the stakeholder claim ought to be dismissed on grounds that there exist no competing or potential competing claims to the balance standing in the Claimant's account relating to the Defendant or on the ground that any such competing claims or potential claims are not expected to be made.
   >
   > (b) In the event that the stakeholder claim is not dismissed, for the court to give such directions as it deems fit, to include:

(i) Who, if anyone, should be notified of and/or joined as Defendant to the claim in accordance with CPR Part 19 or other power of the Court;

(ii) If anyone is to be joined as a Defendant or notified, the method of service and/or notification that should be ordered.

(iii) Fixing a date for a further hearing for directions."

(B) BACKGROUND FACTS AND EVIDENCE

8. GCEN states that it provides foreign exchange and payments services to clients including companies, private individuals and investments funds. It is registered with the FCA as a payment institution under the Payment Services Regulations 2009 and with HMRC under the Money Laundering Regulations 2007.

9. Osage states that it was formed in 2014 to acquire and develop the rights to drill for oil in Osage County, Oklahoma, under the terms of a drilling lease known as the Oklahoma HC-5A lease; and has raised approximately £4.43 million through the sale of non-voting shares to enable it to exploit those rights.

10. From about February 2015 to September 2015 Osage used GCEN's services to receive funds from new shareholders, to convert them into US dollars, and to transfer funds to Osage's operating partners in Oklahoma. GCEN's functions were:

    i) to operate an escrow account of behalf of Osage;

    ii) to receive funds paid by prospective shareholders in Osage, and carry out money laundering checks on them on Osage's behalf;

    iii) to return such funds to the prospective shareholder if the money laundering checks were not satisfactorily completed;

    iv) to transfer the funds to Osage's main account with GCEN if those checks were satisfactorily completed; and

    v) to transfer funds in US dollars to operating partners in the US on behalf of Osage when required.

11. Osage's evidence is that this arrangement gave prospective investors and Osage itself security because investors' funds were held securely while money laundering checks were carried out, pending the issue to the investors of shares in Osage. Osage itself thereby avoided the risk of non-payment for shares which it has issued.

12. GCEN appears to have notified Osage in July 2015 that its account facilities with GCEN would be withdrawn at the end of August 2015. In September 2015 Osage became aware that its accounts with GCEN, containing the Funds, had been frozen. GCEN says it was notified at this time, September 2015, that it was unable to operate various accounts it held with Royal Bank of Scotland Plc, with whom it had held accounts since January 2013. GCEN subsequently learned that several of those accounts had been frozen. GCEN's evidence (set out in a witness statement of Ms Fiona Hinds, a partner in GCEN's solicitors Howard Kennedy) is that RBS supplied it

with certain information in confidence in this regard which, due to statutory and court-ordered confidentiality restrictions, GCEN is currently unable to disclose.

13. As a result of these matters, GCEN was for a period unable to pay monies out of the accounts referable to Osage. That restriction was subsequently lifted, but GCEN has continued to retain the Funds for the reasons outlined in §§ 2-5 above.

14. In September 2016 Osage's solicitors provided GCEN with a copy of the CDA document. That document, headed "*First Application for Continued Detention of Seized Cash*", is a completed but unsigned form of application in "*Form A*" for an order to be sought from Stratford Magistrates Court under section 295(4) Proceeds of Crime Act 2002 and rules 4 and 5 of the Magistrates' Courts (Detention and Forfeiture of Cash) Rules 2002/2998. The applicant is stated to be DC Charles Teggart of the Metropolitan Police and the subject-matter to be £50,000 in cash seized on 21 January 2016 from GCEN. GCEN states that no assets have in fact been seized from it, and it has not been served with any order arising from the CDA document. Nonetheless, GCEN makes the point that the contents of the document indicate that the Metropolitan Police had a number of serious concerns, apparently based on evidence they had obtained, about Osage's conduct in raising share capital.

15. The CDA document includes a list of *"any other persons likely to be affected by an order for detention of the cash",* namely *"Glenn King, David Hyman and Martin Finch of Oakmont and Partners Limited, Monarch Asset Management ltd, Kansas B2 Project and Osage 1".* It states that there are *"reasonable grounds for suspecting that the cash is either recoverable property or is intended by any person for use in unlawful conduct".* The grounds set out include the following:

    i) *"Information was received on the 24/12/2015 that a company called Parish Eastway had cold called a Pensioner to invest in an oil well Investment called Osage oil (Martin Finch is the director). This type of investment is considered a Collective Investment Scheme under the Financial Conduct Authority guidelines, and there are strict rules which must be adhered to when selling this type of investment."*

    ii) *"Any business selling this type of business must be an appointed representative of a FCA authorised firm, which Parish Eastway are not. ... This type of investment is high risk, and should not be offered to ordinary members of the public. Mr David Hyman (Business partner of Glenn King) is accredited by the FCA ... to sell this type of investment however he is not the only person who has been selling ..."*

    iii) *"A witness informed the police that he is a retired pensioner; he was cold called by a company called Parish Eastway, asking him to invest in an oil well investment called Osage 1. He paid £5,000 for the investment and was informed that 25% of his money would pay brokerage and other costs, he believed that 75% of his money would be invested in the oil well. On reviewing his paperwork, he was not considered a person the investment was suitable for and his money was returned. A few weeks later with no apparent substantial change in circumstances, his status had changed to a person who was considered a sophisticated investor and his investment went through. This person was spoken to by police on the phone, who sounded confused and*

was not able to coherently explain what they had invested in, nor explain what fees were to be taken out of their investment, who had called them, and who was dealing with their investment. Since this initial investment the witness has been contacted by other brokerages offering similar investment, despite not giving permission for their details to be passed on to other brokerages …"

iv) *"Monies for the Oil Investments were paid into [GCEN] … Enquiries show the account the monies were paid into are owned and controlled by Oakmount and Partners Limited, where Glenn King is the director, Kansas B2 Project and Osage 1 where Martin Finch is the director. Approximately £3 million has been paid into the Osage account from investors between the 18th March 2015 to 2nd October 2015. Glenn King has been paid £394,087.44, Monarch Asset management Ltd (Director David Hyman) has been paid, £195,761.41, and Mr Martin Finch has been paid £27,724.98. This totals £617,573.83. Total monies readily identifiable as relating to oil well investments amounts to $828,887.43 when exchanged amount to £585,453.10. This is less than a quarter of the monies paid by the investors. These figures do not include payments made to brokerages selling the Oil Well investments. On the face of it, it appears that a large percentage of the investor's monies are being paid to Glenn King, David Hyman and Martin Finch and Brokerages, this would mean that approximately 19% of investors monies are actually being invested in the Oil wells. …"*

v) *"It would also appear that dividends are being paid to investors from this account, from the actual monies being invested, yet there are no deposits from the oil well companies that would reconcile these payments. …"*

vi) *"Glenn King has had all his Business and Private UK bank accounts closed by the separate banking institutes, Duncan Lawrie Private Banking, Lloyds, and NatWest and Santander and also one with First Gulf Bank in Dubai."*

vii) *"Other documents taken from the computers from Kings Offices show that Martin Finch is an Employee of Oakmount and partners Ltd. It would appear that he is a figure head director only in relation to Kansas MB Project and Osage 1 Projects. The payments from the [GCEN] account would justify that assumption. Mr Finch has contacted prosecution witnesses on behalf of King informing them that their investments in the Illinois Oil wells was to be transferred to the Kansas MB Project, at no cost to them. Many people did not sign the papers, but their shares were transferred regardless of their wishes, knowledge or consent. Mr King had bail conditions not to contact directly or indirectly with 30 named prosecution witnesses, but say, to pay dividends."*

viii) *"Mr King was arrested and interviewed on 2 occasions relating to the oil well investment in Illinois and answered no comment to all questions regarding his business and brokers selling products that directly belonged to Glenn King and David Hyman. …"*

ix) *"A restraint application was considered, and withdrawn by CPS in relation to the current investigation. This has no bearing on this cash seizure as it relates to Oil wells in another region (Oaklahoma) [sic]."*

x) *"At this time I have reasonable grounds to suspect that all of the cash seized from the respondent is recoverable property and that proceeds of fraudulently sold oil well investments targeted at ordinary members of the public, in breach of the FCA guidelines or is intended for use in unlawful conduct and its continued detention is necessary to enable its derivation to be further investigated or considered given to bringing proceedings against any person for an offence with which the cash is connected."*

16. In correspondence in late 2018, Osage's solicitors provided GCEN (apparently for the first time) with a copy of an email from a Metropolitan Police solicitor dated 27 September 2016 indicating that the CDA document was a draft, that no detention had ever been applied for, and that the document had been included in a proposed hearing bundle (for what appears to have been a forfeiture hearing) due to an administrative error. Osage's solicitors also stated in the course of this correspondence that:

   i) following Mr King's arrest in January 2015 and release from bail in April 2017, the Metropolitan Police confirmed in October 2018 following a comprehensive investigation that no further action was to be taken;

   ii) Mr Finch, Osage's director, had never been a suspect in a police investigation;

   iii) there was no ongoing police investigation into any of Mr King, Mr Finch or Osage, and

   iv) Mr King did not at any time breach his bail conditions.

17. Mr Finch's second witness statement exhibits a letter from DC Buck, addressed to Mr Glenn, dated 26 November 2018 indicating that the *"investigation into oil well investment companies ... was referred to the Crown Prosecution Service for consideration. It was decided that no further action should be taken against you."* Email correspondence from October 2018 also indicates that no further police action is to be taken in relation to Mr Hyman, that Mr Finch was not a subject of the investigation, and that the forfeiture application was also to be withdrawn.

18. GCEN submits that despite these matters, it would not be reasonable for GCEN simply to disregard the allegations set out in the CDA document, because (i) it is reasonable to assume, *prima facie*, that the police are a reliable source; (ii) the allegations appear to have some evidential basis to support them, and (iii) they are of a serious nature. GCEN adds that neither Osage nor the police have provided any evidence to suggest that the allegations made in the CDA document were incorrect. The facts that the application was not pursued, and the police investigation was eventually closed, do not mean that the allegations had no basis.

19. If the allegations are well-founded, GCEN submits, a court might find that Osage and/or its agents misrepresented the investment opportunity to investors, operated a collective investment scheme without FCA permission in breach of the general prohibition under the Financial Services and Markets Act 2000, communicated financial promotions in breach of section 21 of that Act, and/or employed undue influence to procure investments. That might in turn give rise to a variety of potential common law and statutory claims by investors in respect of the Funds.

20. Further, GCEN's evidence indicates that it has conducted its own analysis of the Osage accounts held with GCEN, which is consistent with and appears to corroborate some of the contents of the CDA document. That analysis includes the three particular facets which I summarise below.

(1) Percentage of investor funds paid to operating companies

21. Apparently consistently with the 19% figure referred to in § 15.iv) above, GCEN's analysis indicates that out of total payments of the dollar equivalent of £3,282,697.90 made on Osage's behalf from the relevant accounts, only the dollar equivalent of £638,337.35, i.e. about 19% of those payments, appears to have been paid to the US operating companies "*Oklahoma HC Project LLC*" and "*Kansas MB Project LLC*". That figure contrasts with (a) the information set out in the CDA document quoted in § 15.iii) above as having been given to an investor, and (b) an Osage Prospectus dating from 2015 (which Osage provided to GCEN in the course of being taken on as a client) relating to the Oklahoma HC5A project, which suggested that 100% of investors' funds would be paid by Osage into the HC-5A project.

22. GCEN's evidence on this point was set out (along with evidence of the other matters outlined below) in the second witness statement of Ms Hinds dated 24 August 2018. On 28 November 2018 Osage's solicitors sent an email to GCEN's solicitors referring to Ms Hinds' witness statement and saying *"[w]e are now in a position to respond to the content of the statement and it would be reasonable in the circumstances for you to agree that our client should be allowed to adduce evidence in response to the witness statement dated 24 August 2018, given the content of same"*.

23. Osage's evidence in response to Ms Hinds' second witness statement was in due course set out in the second witness statement of Mr Finch dated 17 January 2019. That statement confirmed the status of the CDA document and police investigations, as outlined above, and made the point that the court should disregard any evidence upon which GCEN seeks to rely *"where that evidence is supported only by inference which Ms Hinds seeks to draw from matters set out in the draft, unissued, seizure application"*. It concludes that as no shareholder has intimated a claim for the Funds, GCEN's application should be dismissed.

24. Mr Finch's statement does not, however, address the underlying facts including, in particular, GCEN's own analysis of Osage's bank accounts. Thus it does not address GCEN's conclusion referred to in § 21 above that only 19% of investors' funds appears to have been paid to US companies engaged in the oil drilling business itself.

25. Osage's written submission dated 28 February 2019, pursuant to the order of HHJ Klein, states:

> "GCEN goes on to parrot the Metropolitan Police draft cash seizure and detention application and contend (submission para 4(d)) that only a small proportion of the investor funds paid in have been invested in the oil wells of Oklahoma. This is an entirely baseless assertion with no evidence to support it. It relies on Ms Hinds' unsubstantiated contentions and the untested and unproven comments in the draft seizure application.

> As well as being unsubstantiated, these allegations also run contrary to the evidence relied on elsewhere by Ms Hinds. This shows that over a period of 3 months Osage received (into its account with GCEN) a total of US$160,408.77. At 2015 exchange rates, annualised this would have been the equivalent of over £400,000 in income. That is a healthy return on investor payments of £3.2m but would be a stratospheric one if it were the case that only £638,337 had in fact been paid to the US operating partners as alleged."

26. Osage's approach is thus to invite the inference that much more than £638,337 of the investors' money must have been paid to the operating companies in the US, because otherwise it would not have been feasible to generate such a high return. That assumes both (a) that the US$160,408.77 was genuine investment return and (b) that it relates only to the 3 month period over which it was paid. It is notable that Osage does not take the seemingly more straightforward approach of adducing evidence to show the amount of investors' funds that was actually paid to the US operating companies. Instead, it adduces no evidence on that topic.

27. In oral submissions, Osage said it did not accept that only 19% of investors' funds had been so paid, but that even if that were the case it showed that investors had received something of value. The latter point is relevant to the discussion below of potential causes of action, but does not address GCEN's concern that there is reason to believe investors may have been misled about the use to be made of their funds and/or that investors' funds may have been misappropriated.

(2) Alleged Ponzi scheme characteristics

28. GCEN refers to the statement in the CDA document that dividends appear to have been paid to investors out of the actual sums they had invested. GCEN states, exhibiting relevant entries, that its own analysis has identified payments totalling £114,761 from Osage's main account with GCEN to 15 or more investors in small amounts consistent with purported dividend payments. GCEN states that:

    i) in some cases, these purported dividend payments occurred before any commensurate credits to the account other than credit attributable to investor funds;

    ii) there is no correspondence between non-investor fund credits and payments out of purported dividend payments;

    iii) some of the purported dividend payments refer to the names of operating companies other than Osage, such as "*Kansas MB*", "*KMB*", "*KB2*" or "*Sooner*", noting that Mr Finch was also a director of companies named Kansas B2 Investments Limited and Sooner Energy Limited; and

    iv) Osage registered four investors as shareholders and even paid them purported dividends even though it does not appear to have been notified that they had cleared GCEN's money laundering checks.

29. This topic was addressed in some detail in Ms Hinds' second witness statement dated 24 August 2018, but Mr Finch's second witness statement in response does not deal with it.

30. Osage's written submission of 28 February 2019 criticises GCEN's analysis on the basis that (a) it looks at only transactions on the Osage account over only a short period of time and *"[t]he Court has no evidence of the origins of the funds that were already in the account before those payments were made",* and (b) GCEN's analysis shows that more money was received from US operating companies than was paid out in relevant dividend payments during the period. It is, though, notable that Osage has adduced no evidence on this matter.

(3) Payments made to individuals from investor funds

31. GCEN's review of Osage's accounts indicates that £619,573.41 of the £3,282,697 apparently received from investors was paid to Mr King, Mr Hyman and Mr Finch: a figure very close to that stated in the CDA document as indicated in § 15.iv) above.

32. Osage's written submission dated 28 February 2019 states:

> "Osage's case is that these were payments of fees and for back office services provided to the Company. This is 18.8% of the totals received. It is not a significant proportion of the shareholder funds received and certainly cannot be said to evidence a fraud."

33. This is a further topic on which Osage has not to date adduced specific evidence. As a matter of impression, it strikes me that 18.8% is a very high proportion of investors' fund to be paid out to three individuals in these circumstances, particularly if fees or expenses at such levels had not been disclosed to prospective investors.

(C) APPLICABILITY OF CPR PART 86

34. CPR 86.1(1) states:

> "This Part contains rules which apply where –
>
> (a) a person is under a liability in respect of a debt or in respect of any money, goods or chattels; and
>
> (b) competing claims are made or expected to be made against that person in respect of that debt or money or for those goods or chattels by two or more persons."

35. GCEN's position is that such competing claims can reasonably be expected from investors, at least once they become aware of the relevant facts. It seeks directions on that basis, including for service on and/or notification to investors.

36. Osage submits that CPR 86 has no application, and the claim should be dismissed, because:

i) even if the allegations set out in the CDA document, and arising from GCEN's analysis, were true, there is no legal basis on which they could give investors a proprietary claim to the Funds; and

ii) in any event, given that well over three years have elapsed since the Funds were frozen, there is no reasonable basis on which to expecting competing claims to be made to the Funds.

37. I consider these two points in sections (D) and (E) below.

(D) LEGAL BASIS FOR PROSPECTIVE INVESTOR CLAIMS

38. GCEN submits that investors may bring claims to the Funds on any of the following bases:

i) that the Funds still belong in equity to investors because Osage obtained them by fraud;

ii) that investors are entitled to rescind their contracts with Osage, and then claim the Funds in equity, because Osage induced them to contract and pay over the Funds by fraud;

iii) that Osage (through its agent GCEN) holds the Funds on trust for investors because it would be unconscionable for Osage – knowing that it is operating a fraudulent scheme – to assert beneficial ownership of them and deny the investors' beneficial interest;

iv) that GCEN itself owes fiduciary duties to investors and, knowing what it now knows about Osage's conduct, would risk being be in breach of those duties were it now to pay the Funds to Osage, alternatively in breach of POCA section 327 or 328 or a *Quincecare* duty of care owed to investors, or liable for dishonest assistance or another basis set out in this paragraph;

v) that GCEN received the Funds subject to a *Quistclose* trust, for the purpose of paying them to Osage once money laundering checks were complete; however, it cannot now pay the Funds to Osage without risking being in breach of POCA section 327 or 328 or a *Quincecare* duty of care, or liable on some other basis set out in this paragraph;

vi) that Osage's scheme involves transactions at an undervalue within section 423 of the Insolvency Act 1986, and investors would be entitled to obtain an order under the Act to protect their interests; or

vii) that GCEN would be liable to investors were it to deal with the Fund in disregard of circumstances that could give rise to a claim from them unless any such claim would be an *"almost indisputably bad one"* (Lewin on Trusts, 19th edn, § 26-031 citing *Guardian Trust and Executors Company of New Zealand v Public Trustee of New Zealand* [1942] AC 115).

39. Osage submits that the evidence relied on by GCEN comes nowhere near the satisfying the standard necessary to advance a case in fraud, adding that it is notable that these serious allegations are being pursued by a supposedly neutral claimant in

stakeholder proceedings. Osage does not invite me to reach a conclusion on a summary basis on the facts underlying these suggested potential claims, and I do not consider it would be appropriate to do so. Osage nonetheless submits that none of them has any arguable legal basis even if the facts were to be as GCEN suggests or fears. I therefore consider the legal basis of each suggested potential claim below.

(1) Claim based on fraud by Osage

40. The starting point is that even where a contract has been induced by fraudulent misrepresentation, it is generally voidable rather than void, and title passes to assets transferred to the fraudster, subject to the innocent party's right to rescind where rescission remains possible (see, e.g., *In the Matter of Crown Holdings (London) Limited (in Liquidation)* [2015] EWHC 1876 (Ch) (Murray Rosen QC) § 33, citing *Shalson v Russo* [2005] Ch 281 §§ 109-119 and *Box v Barclays Bank* [1998] Ll Rep 185). See also *Lewin on Trusts* (19th edn.) § 7-030:

> "It appears that where a sale is rescinded for fraudulent misrepresentation the buyer will be held to be a trustee for the seller, but not until the representee elects to avoid the contract. It is the element of fraud which causes equity to impose a constructive trust in such circumstances, and so there is no trust when a contract is rescinded for a non-fraudulent misrepresentation. The representor cannot retrospectively be subjected to fiduciary obligations as a constructive trustee, since until the representee has elected to avoid the contract, the representor is not a constructive trustee of the property transferred and no fiduciary relationship exists between them. … The representee may of course choose to affirm the contract despite the misrepresentation. Someone with the right to rectify or rescind a document, whether because of a fraud or otherwise, and thereby to recover property, has for some purposes an equitable interest in the property, but in the present context is treated as having a "mere equity". It would therefore be going too far to say that the legal owner of the property was a trustee for him, at least before rectification or rescission was ordered." (footnotes omitted)

41. Lewin § 7-031 states as an exception to this principle that the rules relating to rescission are not requisite *"where a contract is not merely induced by fraudulent misrepresentation but is itself the instrument of fraud and no more than a vehicle for obtaining money by false pretences"*. GCEN relies on this exception. It argues that there is a real foundation for believing that Osage was operating a Ponzi scheme. If so, then investors would still own the Funds in equity without the need to rescind their investment contracts: the contract would have been merely a dishonest device to obtain money for which *"it is meaningless to impose a requirement for the fraudster to be notified as rescission"* (*Halley v Law Society* [2003] EWCA Civ 97 § 48). The situation would be *"not simply a case of a valid contract being induced by fraud; but that the fraud so infected the whole transaction that it had no legal effect at all",* i.e. where *"The 'agreements' were fictitious contracts ... merely part of an elaborate charade (or mechanism) by which the loser was persuaded to part with his money"* (ibid., § 45). On that basis, the position would be *"akin to theft"* with the result that

the Funds would be immediately traceable by investors (*Westdeutsche Landesbank v Islington LBC* [1996] AC 669, 705C-D, 715H-716D).

42. In *Halley* the Court of Appeal had to consider whether the claimant had a beneficial interest in money held in a solicitor's bank account which was said to comprise his share of fees in relation to an investment made by a company (Tidal) in a high yield 'bank instrument' that had turned out to be worthless. The Law Society had intervened in the solicitor's practice and alleged that the transaction was a fraud. It appears the victim of the fraud had not, however, rescinded the transaction. Carnwath LJ (with whom the other members of the court agreed) stated:

> "44. … Apart from the finding of fraud, it is difficult to see why the elaborate bundle of documents provided in return of the advance payment, which was precisely what was contracted for, was incapable of satisfying the minimal requirements for "adequate consideration" (see Chitty on Contracts, 27th Ed, para 3–013ff; and cf Haigh v Brooks (1839) 10 A&E 309). If that is so, there was no "total failure", because that consideration was duly provided. Furthermore, it seems clear that the parties "intended" to create legal relations; the applicant was to be under a legal obligation to pay the fee, and Tidal under a legal obligation to produce the documents.
>
> 45. The submission, as I understand it, is that this is not simply a case of a valid contract being induced by fraud; but that the fraud so infected the whole transaction that it had no legal effect at all. The "contracts" were in reality no more than devices to extract money by fraud; in Mr Dutton's words—
>
> > "The "agreements" were fictitious contracts. They were as the judge found merely part of an elaborate charade (or mechanism) by which the loser was persuaded to part with his money."
>
> The position, accordingly, is said to be "akin to theft". Where property is stolen, no beneficial interest passes to the thief. Mr Dutton submits that the same applies where money is extracted by fraud, otherwise than under a legally enforceable contract. He relies on Westdeutsche Bank v. Islington LBC [1996] AC 669 at 705C–D, 715H–716D (per Lord Browne-Wilkinson).
>
> > "I agree that the stolen moneys are traceable in equity. But the proprietary interest which equity is enforcing in such circumstances arises under a constructive, not a resulting, trust. Although it is difficult to find clear authority for the proposition, when property is obtained by fraud equity imposes a constructive trust on the fraudulent recipient: the property is recoverable and traceable in equity. Thus, an infant who has obtained property by fraud is bound in equity to restore it: Stocks v. Wilson [1913] 2 K.B. 235, 244; R. Leslie Ltd. v. Sheill [1914] 3 K.B. 607. Moneys stolen from

> a bank account can be traced in equity: Bankers Trust Co. v. Shapira [1980] 1 W.L.R. 1274, 1282C–E: see also McCormick v. Grogan (1869) L.R. 4 H.L. 82, 97."" (§§ 44-45)

43. Carnwath LJ distinguished the decision of the Court of Appeal in *Twinsectra v. Yardley* [1999] Ll Rep Bank, where Twinsectra lent money to a Mr Yardley, on the security of a solicitor's undertaking given by a Mr Sims, whom Twinsectra believed to be acting for him. Mr Yardley fraudulently failed to inform Twinsectra that, by the time of the loan, he had withdrawn Mr Sims' instructions. It was held that this was sufficient to establish Twinsectra's claim in deceit, but not, in the absence of rescission, to give them a proprietary right to the money lent. Potter LJ said:

> "It seems to me that, whatever the legal distinctions between 'theft' and 'fraud' in other areas of the law, the distinction of importance here is that between non-consensual transfers and transfers pursuant to contracts which are voidable for misrepresentation. In the latter case, the transferor may elect whether to avoid or affirm the transaction and, until he elects to avoid it, there is no constructive (resulting) trust; in the former case the constructive trust arises from the moment of transfer. The result, so far as third parties are concerned, is that, before rescission, the owner has no proprietary interest in the original property; all he has is the 'mere equity' of his right to set aside the voidable contract. That equity binds volunteers and those taking with notice of the equity, but not purchasers for value without notice; see generally Worthington: Proprietary Interests in Commercial Transactions (1996) Clarendon Press at pp 163-165 and 167. Despite dicta of Lord Mustill in Re Goldcorp (a case in which the purchase monies sought to be traced were unidentifiable), which, if generally applied beyond the context of the facts in that case, would suggest that equitable title does not (or in appropriate circumstances may not) revest on rescission, the general position seems to me that summarised in Underhill and Hayton (15 Ed) at p.372(f). It is there stated that equity imposes a constructive trust on property where a transferor's legal and equitable title to his property has passed to the transferee according to basic principles of property law but in circumstances (eg involving fraud and misrepresentation) where the transferor has an equitable right (ie mere equity) to recover the property by having the transfer set aside, and the court declares that from the outset the transferee has held the property to transferor's order, though nowadays it seems better to regard a restitutionary resulting trust as arising." (§ 99)

The Court of Appeal's decision in *Twinsectra* was reversed in the House of Lords ([2002] UKHL 12) though not on grounds directly relevant to the present case.

44. Carnwath LJ in *Halley* said:

> "In my view, however, there are important distinctions between that case and the present. In that case, there was a straightforward contract of loan, under which legal and beneficial interest in the money passed to Mr Yardley (subject only to a "purpose" trust, which does not affect the present argument). The contract may have been induced by the fraud, but it was not itself the instrument of fraud. In this case, the contract has been held to be the instrument of fraud, and nothing else. The elaborate documentation was, in the words of the judge, "no more than a vehicle for obtaining money … by false pretences" (para 119). ...
>
> In such a case, it is meaningless to impose a requirement for the fraudster to be notified of "rescission". From the fraudster's point of view there is nothing to rescind; for practical purposes, he has parted with nothing of value and incurred no obligations; the victim is left with some documents which, from the outset, were known and intended by the other party to be worthless. The "election" to which Potter LJ referred is not a real option. Although the case does not fit neatly into Potter LJ's binary classification, he was not dealing with these facts. Subject to any direct authority, I see no reason why it should not be regarded as a simple case of "property obtained by fraud", in Lord Browne-Wilkinson's terms." (§§ 47-48)

45. Murray Rosen QC in *Crown Holdings* noted (§ 34(b)) that the authors of *Goff & Jones "The Law on Unjust Enrichment"* suggest that *Halley* (and the similar analysis in *Collings v Lee* [2001] 2 All ER 332, 337) should be treated with caution, and in any event should not be regarded as cases of fraudulent misrepresentation and rescission but rather as if the contracts were void *ab initio*. *Goff & Jones* (9th ed., § 40-30) suggests that the distinctions drawn in these cases between void and voidable transactions induced by fraud is unlikely to be workable in practice. However, I consider *Halley*, at least, to be binding.

46. Osage submits that the present case, even on the basis of the allegations made in the CDA document and by GCEN, does not fall within the *Halley* exception. The investors paid their subscriptions to obtain shares in Osage, which they have received, and with them the right to receive dividends, which they have likewise received.

47. On the material presently before me, I consider Osage to be correct on this point. That material does not go so far as to suggest that the subscription contract with and issue of shares by Osage, or the purported investment in oil drilling interests, were a mere charade or (as it was put in *Halley* § 47) *"the instrument of fraud, and nothing else … "no more than a vehicle for obtaining money ... by false pretences"*. I accept GCEN's point that the mere fact that some form of consideration was received by the investors does not prevent the *Halley* exception from applying: as noted above, Carnwath LJ in *Halley* considered that the package of documentation received in return for the money may have satisfied the low threshold for the existence of consideration. However, the *Halley* exception applies only where the purported transaction is in effect unreal, a pure instrument of fraud, so that the 'election' to rescind referred to by Potter LJ in *Twinsectra* is unreal (*Halley* § 48). The evidence

currently before the court does not in my view go that far: it is consistent with the existence of investors obtaining, even if as a result of fraudulent misrepresentation, real shares in a real company (Osage). I do not consider it necessary to decide, for this purpose, whether real dividends have in fact been received: whether they have or not is a matter of controversy.

48. As a result, I do not consider that the present evidence provides a basis for considering investors to have a proprietary claim based on fraudulent misrepresentation unless and until investors rescind their contracts with Osage.

(2) Investors' right to rescind and claim the Funds

49. GCEN submits in the alternative that the evidence summarised earlier indicates that investors may be entitled to rescind their subscription agreements with Osage, and would then have proprietary claims because Osage would hold the Funds on constructive trust for them. GCEN says it is artificial for Osage to argue that there can be no expectation of a claim until after rescission in circumstances where, if the investors were made aware of the circumstances, they would be likely to rescind and bring claims.

50. Osage stated in its 28 February 2019 written submission:

> "Unless and until relevant investors (that is, those 11 investors whose payments comprise the funds held by GCEN) rescind their contracts with Osage (and they have had 3 years to do so but have not and cannot), those monies belong beneficially to Osage and GCEN are contractually bound to pay them over. If it does so before any rescission is communicated, it can have no liability to the investors. Those investors have no proprietary interest in the funds of which GCEN claims to be the constructive trustee."

51. Osage does not make clear on what basis it submits that the investors "*cannot*" now rescind their contracts of subscription. If investors have been unaware of the relevant facts during the 3 years or so since they invested, then the mere lapse of time may well not prevent rescission. No other specific basis on which rescission could be barred has to date been advanced, and for present purpose it seems appropriate to proceed on the basis that investor might be entitled to rescind.

52. If investors do have a right to rescind, then they have prospective proprietary rights to the Funds contingent upon the exercise of the right to rescind. That is in my view sufficient – subject to the question I consider in section (E) below about whether there is a factual basis for expecting claims to be made – to satisfy the requirement of CPR 86 for expected competing claims. A claim that can be brought provided that the claimant takes a prior legal step, here rescission, is still in my view a competing claim which may (depending on the facts) be expected to be made for CPR 86.1(1)(b) purposes.

(3) Osage holding on constructive trust based on unconscionability

53. GCEN argues that the Funds came into Osage's control when they were paid to GCEN as Osage's agent, and that the circumstances in which that occurred (viz that Osage knew it was operating a Ponzi scheme) make it unconscionable for Osage now to assert a beneficial or exclusive interest in the Funds. GCEN cites:

    i) statements in *Lewin* §§ 7-016 and 7-019, dealing with situations where a person has taken on a fiduciary duty in circumstances where it would be unconscionable for him to assert a beneficial interest in the relevant property, and

    ii) Millett LJ's statement in *Paragon Financial v DB Thakerar* [1999] 1 All ER 400 that *"A constructive trust arises by operation of law whenever the circumstances are such that it would be unconscionable for the owner of property (usually but not necessarily the legal estate) to assert his own beneficial interest in the property and deny the beneficial interest of another."*

54. Osage responds that it cannot be a trustee of funds not in its possession, and in any event it does not owe fiduciary duties to its shareholders. On the contrary, the Funds were received beneficially for Osage, to use in its business, in return for the Osage shares that the investors have received.

55. I find it difficult to see how this head of liability can assist GCEN if it does not succeed under heads (1) or (2) above. The statement by Millett LJ on which GCEN relies needs to be read in its full context:

> "Regrettably, however, the expressions "constructive trust" and "constructive trustee" have been used by equity lawyers to describe two entirely different situations. The first covers those cases already mentioned, where the defendant, though not expressly appointed as trustee, has assumed the duties of a trustee by a lawful transaction which was independent of and preceded the breach of trust and is not impeached by the plaintiff. The second covers those cases where the trust obligation arises as a direct consequence of the unlawful transaction which is impeached by the plaintiff.
>
> A constructive trust arises by operation of law whenever the circumstances are such that it would be unconscionable for the owner of property (usually but not necessarily the legal estate) to assert his own beneficial interest in the property and deny the beneficial interest of another. In the first class of case, however, the constructive trustee really is a trustee. He does not receive the trust property in his own right but by a transaction by which both parties intend to create a trust from the outset and which is not impugned by the plaintiff. His possession of the property is coloured from the first by the trust and confidence by means of which he obtained it, and his subsequent appropriation of the property to his own use is a breach of that trust. Well known examples of such a constructive trust are McCormick v Grogan

(1869) 4 App.Cas. 82 (a case of a secret trust) and Rochefoucald v Boustead [1897] 1 Ch. 196 (where the defendant agreed to buy property for the plaintiff but the trust was imperfectly recorded). Pallant v Morgan [1953] Ch. 43 (where the defendant sought to keep for himself property which the plaintiff trusted him to buy for both parties) is another. In these cases the plaintiff does not impugn the transaction by which the defendant obtained control of the property. He alleges that the circumstances in which the defendant obtained control make it unconscionable for him thereafter to assert a beneficial interest in the property.

The second class of case is different. It arises when the defendant is implicated in a fraud. Equity has always given relief against fraud by making any person sufficiently implicated in the fraud accountable in equity. In such a case he is traditionally though I think unfortunately described as a constructive trustee and said to be "liable to account as constructive trustee." Such a person is not in fact a trustee at all, even though he may be liable to account as if he were. He never assumes the position of a trustee, and if he receives the trust property at all it is adversely to the plaintiff by an unlawful transaction which is impugned by the plaintiff. In such a case the expressions "constructive trust" and "constructive trustee" are misleading, for there is no trust and usually no possibility of a proprietary remedy; they are "nothing more than a formula for equitable relief": Selangor United Rubber Estates Ltd. v Cradock [1968] 1 WLR 1555 at p. 1582 per Ungoed-Thomas J."

56. The present case is not (on current evidence) one where the parties envisaged that Osage would receive investment monies as trustee. If anything, it belongs to the second class of case referred to above, where a trust is based on fraud. However, since the case law earlier indicates that a proprietary claim in these circumstances generally requires the transaction first to be rescinded, I am unable to see how this head of claim would differ in substance from those referred to under subheadings (1) and (2) above.

(4) Breach of fiduciary duties owed by GCEN itself

57. GCEN submits that the Subscription Agreement made clear that GCEN was to receive investors' funds. As a result, (a) GCEN became the investors' agent and owed duties to them, and (b) investors must be taken to have consented to GCEN acting as their agent even though it was also acting as Osage's agent in receiving the funds. Once GCEN received the CDA document, it was placed in a position of actual conflict of duties (cf *Bristol & West Building Society v Mothew* [1998] Ch 1, 19) and could not pay the Funds over to Osage without investors' further informed consent. Moreover, by doing so it would risk breaching various statutory or common law duties.

58. However, as Osage points out, the Subscription Agreement provides for GCEN to receive funds as GCEN's payment agent. Its function was to receive payments from

investors, conduct money laundering checks on behalf of Osage, and, once they were satisfied, transfer the money to Osage's account. I do not therefore consider there to be a basis for contending that GCEN became the investors' agent merely by virtue of the arrangement for it to receive their funds. Rather, any duties of a fiduciary nature must derive either on the basis of Osage's alleged fraud (see subheadings (1) and (2) above) or from the *Quistclose* trust which it is common ground arose (see subheading (5) below).

(5) Quistclose trust

59. It is common ground that pending GCEN's completion of the money laundering checks on Osage's behalf, GCEN received and held the payments made by each prospective investor on a *Quistclose* trust, to hold the funds on behalf of the investor until the checks had been satisfactorily completed by GCEN and thereafter to pay those funds to Osage to enable the investor to become a non-voting shareholder in Osage.

60. Osage submits that the money laundering checks were in each case carried out satisfactorily, and each investor has been registered and/or treated by Osage as a shareholder, thereby complying with Osage's side of the bargain, with the result that the investors cannot claim to be entitled to assert a beneficial interest in the Funds.

61. GCEN contends, however, that it is unable to fulfil the *Quistclose* trust. Now that it has knowledge of the facts set out in the CDA document, supported by GCEN's own analysis, it cannot pay the Funds to Osage. Paying the Funds to Osage would:

    i) put GCEN at risk of committing a criminal offence contrary to POCA section 327 or 328;

    ii) breach GCEN's *Quincecare* duty of care (see *Singularis Holdings (in liquidation) v Daiwa Capital Markets Europe* [2018] EWCA Civ 84); and/or

    iii) give rise to liability on one of the other basis of claim GCEN has identified.

62. Since GCEN is thus no longer able to fulfil the purpose by the *Quistclose* trust by making payment to Osage, it submits that it holds the Funds on resulting trust for the investors.

63. POCA section 327(1) and (2) provide that:

> "(1) A person commits an offence if he—
>
> …
>
> (c) converts criminal property;
>
> (d) transfers criminal property;
>
> …
>
> (2) But a person does not commit such an offence if—

(a) he makes an authorised disclosure under section 338 and (if the disclosure is made before he does the act mentioned in subsection (1)) he has the appropriate consent;

(b) he intended to make such a disclosure but had a reasonable excuse for not doing so; …"

section 328(1) and (2) provide that:

"(1) A person commits an offence if he enters into or becomes concerned in an arrangement which he knows or suspects facilitates (by whatever means) the acquisition, retention, use or control of criminal property by or on behalf of another person.

(2) But a person does not commit such an offence if—

(a) he makes an authorised disclosure under section 338 and (if the disclosure is made before he does the act mentioned in subsection (1)) he has the appropriate consent;

(b) he intended to make such a disclosure but had a reasonable excuse for not doing so; …"

64. Section 340 defines "*criminal conduct*" and "*criminal property*":

"(2) Criminal conduct is conduct which—

(a) constitutes an offence in any part of the United Kingdom, or

(b) would constitute an offence in any part of the United Kingdom if it occurred there.

(3) Property is criminal property if—

(a) it constitutes a person's benefit from criminal conduct or it represents such a benefit (in whole or part and whether directly or indirectly), and

(b) the alleged offender knows or suspects that it constitutes or represents such a benefit.

(4) It is immaterial—

(a) who carried out the conduct;

(b) who benefited from it;

(c) whether the conduct occurred before or after the passing of this Act.

> (5) A person benefits from conduct if he obtains property as a result of or in connection with the conduct.
>
> …
>
> (9) Property is all property wherever situated and includes—
>
> (a) money;
>
> (b) all forms of property, real or personal, heritable or moveable;
>
> (c) things in action and other intangible or incorporeal property.
>
> (10) The following rules apply in relation to property—
>
> (a) property is obtained by a person if he obtains an interest in it;
>
> …
>
> (d) references to an interest, in relation to property other than land, include references to a right (including a right to possession)."

65. The matters set out in the CDA document, taken together with GCEN's analysis of the position, provide grounds for GCEN to *suspect* that the Funds represent a benefit obtained by Osage from criminal conduct (such as a fraud by false representation contrary to section 2 of the Fraud Act 2006). I emphasise that I make no finding of any such fraud: the issue for present purposes is simply whether GCEN has, based on the information in its possession, grounds for suspicion. Having that suspicion, GCEN could not lawfully convert or transfer the Funds, or be concerned in an arrangement which it knows or suspects facilitates Osage acquiring, retaining, using or controlling the funds, unless GCEN had first made a disclosure under section 338 (authorised disclosures) and received consent under section 335 to proceed.

66. It was not suggested by Osage that GCEN is under any form of obligation to seek consent under section 335 to pay the Funds to GCEN. Rather, Osage's position is that as no criminal prosecution is being brought against Osage or the persons connected with it, it could not credibly be said that the Funds are criminal property.

67. However, I do not consider that the problem can be so easily disposed of. There is no evidence before the court about the reasons why no prosecution is to proceed, and it is not possible confidently to infer that no offence can have been committed. GCEN's own analyses provide some grounds for suspicion that investors have been misled about the destination and/or use of their funds, and if that is the case then a crime may have been committed. In these circumstances, GCEN cannot safely pay the Funds over to Osage, particularly if (as Osage appears to envisage) the 11 investors who paid the Funds to GCEN are given no opportunity to consider the position or raise any objection.

68. As a result, I consider that the 11 investors who paid the Funds to GCEN would have a viable argument that GCEN holds those Funds on resulting trust for them. The resulting trust would exist because, from the outset, the beneficial ownership in the Funds has remained with the investors subject only to GCEN's power and/or duty to pay the Funds to Osage following satisfaction of the money laundering checks (cf *Twinsectra* [2002] 2 AC 164 § 100 per Lord Millett). Once such payment ceases to be possible, beneficial ownership is left with the investors absolutely. That would not of course relieve the investors of any contractual liabilities they may have to Osage under their respective subscription agreements, albeit such liabilities may themselves be avoided *if* the agreements were indeed induced by fraudulent misrepresentation and the investors have retained and proceed to exercise their rights to rescind.

69. GCEN also submits that paying the Funds to Osage would breach a Quincecare duty of care (see *Singularis Holdings (in liquidation) v Daiwa Capital Markets Europe* [2018] EWCA Civ 84). Steyn J in *Barclays Bank v Quincecare* [1992] 4 All ER 363, 376 stated that *"a banker must refrain from executing an order if and for as long as the banker is 'put on inquiry' in the sense that he has reasonable grounds (although not necessarily proof) for believing that the order is an attempt to misappropriate the funds of the company ... And, the external standard of the likely perception of an ordinary prudent banker is the governing one"*.

70. The principle was held to apply in *Singularis*, where the defendant equity and brokerage business held a large sum in a client account for the claimant. Over the course of a month the defendant paid amounts out on the instructions of S, its client's 100% owner, to bank accounts in the names of three other companies within S's group rather than to the claimant's own account. The judge, whose decision was upheld by the Court of Appeal, held that any reasonable banker would have realised that there were many obvious, even glaring, signs that S was perpetrating a fraud on the company when he instructed the defendant to pay the other companies.

71. However, I do not consider *Quincecare* and *Singularis* to provide an apt analogy for the present case. Those cases relate to a duty to decline to make payments to a third party where any reasonable financial institution would believe the customer was being defrauded. In the present case Osage, not the investors, was GCEN's customer, and the payment Osage seeks is from GCEN to Osage rather than to a third party.

72. More generally, I expressed surprise during the hearing at the proposition that a person such as GCEN holding funds which it has reason to believe may have been obtained by fraudulent misrepresentation could escape civil liability by paying them over to the suspected fraudster before the victim of the fraud learned the facts and rescinded the transaction. GCEN referred to the following passage from Lewin about cases where money laundering is suspected:

> "It is the practice of the court not generally to permit a trustee to distribute without notice to a claimant. But the court has jurisdiction to permit or direct a trustee to distribute notwithstanding the existence of claims or potential claims from third parties. That will not have the effect of destroying any proprietary rights of third parties, but may afford protection against personal claims against the trustees from third parties. For example, if a trustee becomes aware after taking office that

> the trust may be part of a money laundering operation instigated by the settlor, the trustee will be concerned that if he distributes the trust fund to the beneficiaries in accordance with the trust, the third party may claim against him that the distribution amounted to dishonest assistance in a breach of fiduciary duty on the part of the settlor. If in such circumstances the trustee acts in accordance with the directions of the court, having made full disclosure to the court, it could hardly be suggested by the third party that the trustee had acted dishonestly in making the distribution, being one permitted by the court after the trustee had taken such steps as the court considered appropriate in the circumstances. Hence a claim by the third party based on dishonest assistance would be bound to fail. But the trustee could not in our view be protected by order of the court against receipt-based personal claims unless the third party was made a party or given notice of the proceedings. Even so, it appears that the court may order distribution if the possibility of a claim appears to be remote or speculative, not founded on firm evidence." (§ 26-033, footnotes omitted)

73. However, that passage presupposes the existence of a trust, a breach of which the trustee risks having dishonestly assisted. It is less clear how those principles apply, if at all, to circumstances such as those of the present case.

74. It is apparent from the case law considered under subheading (1) above that pending rescission the victim of a fraudulent transaction generally has no proprietary right to the goods or money he/she handed over as a result of the fraud, and it follows that subsequent purchasers from the fraudster can obtain good title to the goods/money. Does it follow, however, that an agent holding the funds bears no risk of liability if he pays the money away after receiving notice of the fraud? The 'mere equity' which the victim has pending rescission is not regarded as giving him a proprietary interest in the funds. On the other hand, in *Twinsectra* the Court of Appeal stated at § 90 (quoted in § 43 above stated that the 'mere equity' of the right to set aside the voidable contract "*binds volunteers and those taking with notice of the equity, but not purchasers for value without notice*". It thus seems possible that a person such as GCEN, who holds funds after receiving notice of grounds for rescission, could be bound by the equity and liable to the holder of the right to rescind were it then to pay the money away. However, since this issue (a) was not the subject of argument before me, and (b) is unnecessary to decide in the light of my conclusions on right to rescind (subheading (2) above) and resulting trust (§§ 59-68 above), I prefer to express no concluded view on it.

(6) Claims under Insolvency Act 1986

75. GCEN submits that the scheme operated by Osage involved investors' money being used (i) to make purported dividend payments to those same investors, (ii) to make purported dividend payments using Osage funds even though the payment references suggest they were dividends from investments in companies unconnected with Osage, and/or (iii) to make payments to the operators of the scheme and their associated companies. GCEN argues that all three types of transaction were transactions at an undervalue for the purposes of section 423 of the Insolvency Act 1986:

> "(1) This section relates to transactions entered into at an undervalue; and a person enters into such a transaction with another person if—
>
> (a) he makes a gift to the other person or he otherwise enters into a transaction with the other on terms that provide for him to receive no consideration;
>
> … or
>
> (c) he enters into a transaction with the other for a consideration the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by himself.
>
> (2) Where a person has entered into such a transaction, the court may, if satisfied under the next subsection, make such order as it thinks fit for—
>
> (a) restoring the position to what it would have been if the transaction had not been entered into, and
>
> (b) protecting the interests of persons who are victims of the transaction.
>
> (3) In the case of a person entering into such a transaction, an order shall only be made if the court is satisfied that it was entered into by him for the purpose—
>
> (a) of putting assets beyond the reach of a person who is making, or may at some time make, a claim against him, or
>
> (b) of otherwise prejudicing the interests of such a person in relation to the claim which he is making or may make.
>
> …
>
> (5) In relation to a transaction at an undervalue, references here and below to a victim of the transaction are to a person who is, or is capable of being, prejudiced by it; and in the following two sections the person entering into the transaction is referred to as "the debtor" ."

76. GCEN says payments of purported dividends drove Osage further into insolvency and, being discretionary and not in satisfaction of existing rights, can amount to transactions at an undervalue (*BTI 2014 LLC v Sequana SA* [2016] EWHC 1686 (Ch)); dividend payments in respect of other companies' liabilities were also clearly transactions at an undervalue, and payments to the scheme operators were also in excess of any value received; further, all these types of payment had (GCEN submits) the purpose of damaging investors' interests by misappropriating their assets.

77. GCEN argues that section 423(5) is broad enough to include persons capable of being prejudiced by proposed future transactions, such as the 11 investors who paid the Funds to GCEN; and section 425 provides a broad range of orders the court may make, including an order that may *"affect the property of, or impose any obligation on, any person whether or not he is the person with whom the debtor entering into the transaction"* (section 425(2)).

78. However, the starting point for any order under section 423 is that a transaction at an undervalue has been entered into. Although on GCEN's analysis Osage has entered into such transactions with various parties including previous investors, it has not necessarily entered into any transaction at an undervalue with the 11 investors who paid the Funds to GCEN. The orders which the court can make under section 423 (read with section 425) are for the purpose of reversing the effect of undervalue transactions that have occurred (section 423(2)(a)) and protecting the interests of the victims of undervalue transactions (section 423(2)(b)), including by requiring any property transferred as part of the transactions to be vested in another person (section 425(1)). I do not read section 423 as empowering the court to make an order for the control or revesting property such as the Funds that has not so far been the subject of any undervalue transaction albeit it might in future become the subject of such a transaction. I do not therefore consider that reliance on section 423 can assist GCEN in establishing a risk of competing claims to the Funds.

(7) Guardian Trust claim

79. GCEN submits that it would be liable to investors were it to deal with the Funds in disregard of circumstances that could give rise to a claim from them unless any such claim would be an *"almost indisputably bad one"* (Lewin on Trusts, 19th edn, § 26-031 citing *Guardian Trust and Executors Company of New Zealand v Public Trustee of New Zealand* [1942] AC 115(PC)).

80. In *Guardian Trust* Lord Romer said:

> "[I]f a trustee or other person in a fiduciary capacity has received notice that a fund in his possession is, or may be, claimed by A, he will be liable to A if he deals with the fund in disregard of that notice should the claim subsequently prove to be well founded." (p127)

81. In that case a bank executor paid legacies under a will after it had received notice from the next of kin that they intended to challenge the will, and was made personally liable to account for the amount of the legacies so paid after the next of kin's challenge proved successful and the grant to the executor was revoked.

82. Lewin states at § 26-031:

> "It has proved awkward to reconcile the Guardian Trust principle with the decision in Carl-Zeiss Stiftung v Herbert Smith & Co. (No.2), that solicitors were not liable for receiving payments for fees and disbursements out of funds which, to their knowledge, were being claimed by the plaintiff in proceedings against the solicitors' client. It is true

> that Carl Zeiss turned on the scope of liability for knowing receipt of property transferred in breach of trust and Guardian Trust did not; but it would be unsatisfactory if the rules applied were different when in each case the effect of notice of a claim is in issue. Where liability for knowing receipt is alleged, it seems that the principal claim must be sufficiently clear to have justified the court in preventing the person against whom the claim is made from dealing with the property and the claimant must give some good reason why he had not sought such an order before proceedings against the present defendant, neither criterion being satisfied in Carl Zeiss. Our view is that the same limitation should apply to the Guardian Trust principle, though it may then be that in cases falling within it, as in cases of knowing receipt, the court will be readier to impose liability on a recipient who is a volunteer. It has indeed been said that the Guardian Trust principle is meant to apply to a "reasonably arguable claim" and not to one which is specious, with no arguable foundation. Even so, trustees will not be able to distribute safely on their own authority once they have notice of a claim, or of circumstances which could give rise to a claim, unless they are able to take the view that the claim is almost indisputably a bad one. ..." (footnotes omitted)

83. However, the operation of the *Guardian Trust* principle depends on the fiduciary being on notice of a claim to the funds in question. It is not a head of claim in itself. As a result, I do not consider it adds to the analysis when considering whether or not there are any legally viable actual or expected competing claims in the present case.

(8) Conclusion on this issue

84. For the reasons set out above, although several of the potential causes of action put forward by GCEN could not in my view found legally viable competing claims by investors, such claims could in my view arise on the basis that (a) investors may have proprietary claims to the Funds contingent upon rescission of their subscription contracts with Osage (and the need for the prior step of rescission would not prevent them from being expected competing claims for CPR 86 purposes); and/or (b) the Funds, having been paid subject to a *Quistclose* trust, are held by GCEN on resulting trust for investors because GCEN cannot lawfully pay the Funds to Osage (thus fulfilling the purpose for which they were paid to GCEN), because the suspicions GCEN has would make such payment contrary to POCA section 327 and/or 328.

(E) WHETHER COMPETING CLAIMS ARE EXPECTED

85. CPR 86 applies only where competing claims *"are made or expected to be made"* in respect of the relevant money or other asset. *"Claims"* in this context includes, in particular, claims in the English courts but has been held to extend also to claims brought in arbitration or proceedings abroad (*ST Shipping and Transport Pte Ltd v Space Shipping Ltd* [2018] EWHC 156 (Comm)).

86. As noted earlier, Osage submits that now that well over three years have elapsed since the Funds were frozen, there is no reasonable basis on which to expecting competing claims to be made to the Funds.

87. In *Watson v Park Royal (Caterers) Ltd* [1961] 1 W.L.R. 727 Edmund Davies J said:

> "There is ample authority for the proposition that the discretionary relief of interpleader will not be granted unless there appears to be some real foundation for the expectation of a rival claim: see Isaac v. Spilsbury; Harrison v. Payne; and Sharpe v. Redman. The fact that these are, in the words of the district registrar, "somewhat elderly authorities" I think adds to their weight rather than diminishes it. Applying them, in my judgment, while there were intimations of a sort that Wood and Waite were entitled to the £918, no sufficient claim had been advanced on their behalf until the letters of April 7 and July 22, 1960, already referred to. From the receipt of the earlier letter, however, although the defendants had not actually been sued by Waite's trustee, there was a real foundation for the expectation that they would be sued (Morgan v. Marsack). Accordingly, while the matter becomes academic in the light of the decision I have come to on the section 8 point, it is obviously convenient to the parties that I should now state that, had the defendants applied for interpleader relief on receipt of the letter of April 7, 1960, or say within twenty-eight days thereafter, they would, in my judgment, have acted with reasonable promptitude, and I should in any event have awarded them their costs of action up to that date." (p734, footnotes omitted)

88. The letter of 9 July 1958 had indicated the defendants' knowledge that a Mr Waite (who later laid claim to the funds) *"was associated with the business, and ... gave the [defendant's] staff to understand that he was 'Brays' as an earlier partner or associate had dropped out"*, '*Brays'* being the name of the business to whom the defendant owed the debt; whereas the 7 April 1960 letter had positively laid claim to the funds (p733).

89. *Watson* was thus a case where it was the receipt of a letter explicitly claiming the funds that was held to give a real foundation for the expectation of a rival claim. However, whether there is such a foundation must be a question of fact in each case.

90. CPR 86.2(5) and (6) provide that the stakeholder must serve the claim form or application notice *"on all other persons who, so far as they are aware, asserts a claim to the subject matter of the stakeholder application"*, and that a respondent so served must within 14 days provide a witness statement *"specifying any money and describing any goods and chattels claims and setting out the grounds upon which such claim is based"*.

91. It might therefore be argued that CPR 86 can operate only where a third party has actually asserted a claim, because otherwise there will be no-one who can be served under CPR 86.2(5) and become the competing claimant for the funds.

92. However, CPR 86.1(1)(b) uses the phrase "*claims are made or expected to be made"* and not, for example, *"claims are made or threatened"*. As a matter of ordinary language, it is possible for a claim to be "*expected*" even if it has not yet been asserted. An example of such a case could be where the prospective competing claimant is known to the stakeholder but has not yet asserted a claim because it has not yet learned of the full facts, analysed them or taken advice. In such a case, the prospective competing claimant would not be a person required to be served under CPR 86.2(5), but would nonetheless be a person who ought to be notified of the proceedings (if necessary, pursuant to the court's general case management power in CPR 3.1(2)(m) to *"take any other step or make any other order for the purpose of managing the case and furthering the overriding objective"*) given his/her obvious interest in the issue. CPR 86.3(2), setting out the court's powers when hearing a stakeholder application, makes clear that nothing in that rule limits the court's case management powers to make any other directions permissible under the CPR.

93. Osage submitted that there was no real foundation in fact for expecting any claims, and the court should simply dismiss the case, leaving Osage to sue GCEN for the Funds in the ordinary way. Osage expressed concern that notification to investors might damage its business. In response to the point that were Osage to sue GCEN then GCEN would be entitled to apply to join investors to the proceedings, Osage replied that it might actually choose to abandon the Funds rather than incurring the risk of reputational damage.

94. The difficulty with that course of action, though, is that it does not resolve the question of where GCEN should pay the Funds. GCEN does not claim to be entitled to the Funds itself, but does not consider that it can safely pay them over to Osage. For the reasons set out earlier in this judgment, I consider GCEN to have coherent reasons for its concerns, and that there are reasonable grounds to believe that once appraised of the facts investors would make claims in respect of the Funds (while emphasising, again, that I make no finding as to whether or not any such claim would necessarily succeed). In these circumstances, I consider that (a) the case does fall within CPR 86, and (b) in any event, apart from CPR 86, GCEN would be entitled to seek the court's assistance, for example by suing for a declaration that it is obliged to return the funds to the 11 investors who paid the Funds originally. On either approach, it would clearly be appropriate for those investors to be notified of the proceedings, because the case would concern the ownership and disposition of Funds they had paid over and in which they may retain an interest.

95. Clearly, if none of the 11 investors were to come forward and assert a claim, then in practice the action could proceed only if GCEN were prepared itself to pursue a claim for declaratory relief; and in those circumstances the action would no longer have the characteristics (including the costs consequences) of a stakeholder application. However, the possibility that expected claims will not in fact be made is inherent in a CPR 86 case brought on the basis of expected (as opposed to actual) claims, and does not prevent the case from proceeding at least in the first instance under CPR 86.

96. GCEN raised the question of which body of investors would need to be involved in the proceedings. It states that it has used its best endeavours to trace the Funds to 11 particular investors on a *"first in first out"* basis, albeit the reconciliation process is said not to be straightforward. GCEN notes that it might also be argue that a *pari passu* distribution would instead be the appropriate way of distributing the Funds

among all, or a wider group of, investors. GCEN informed the court that there were something of the order of 400 investors altogether. The reasons why *pari passu* distribution might be appropriate were not elaborated, and in my view it would not be proportionate (at least in the first instance) to direct notification of 400 or so investors, bearing in mind also that the total Funds amount to little more than £100,000. Were the court to conclude at a later stage than the Funds in fact belong to the investors as a whole, the matter could be revisited.

(F) CONCLUSIONS

97. For the reasons set out in this judgment, I have come to the conclusions that:

i) there are at least some legally viable bases on which investors may be entitled to the Funds;

ii) there is a real foundation for expecting competing claims in fact to be made to the Funds; and

iii) notification should be given of the proceedings to the 11 investors who GCEN has identified as having paid in the Funds, and they should be directed to indicate within a specified period whether they claim any part of the Funds and, if so, on what grounds.

98. I shall invite submissions on the question of precisely which documents should be served on the 11 investors, and by what means. I am currently inclined to the view that they should include the existing parties' evidence and this Judgment.