Royal Court gives guidance on security enforcement

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In the recent case of In Re Bayswater Road (Holdings) Limited [2019] JRC 102, the Royal Court of Jersey gave some helpful guidance on the enforcement of a security interest created under the Security Interests (Jersey) Law 2012 (**Security Law**).

This case note briefly examines the case and the key takeaways from it.

What is the background to the case?

The background to the case is as follows.

- Stornoway Finance Sárl acting through its compartment 19/Bayswater (**lender**) lent money to Bayswater Road (Holdings) Limited (**borrower**) to assist it to buy and redevelop some London properties.
- To support the borrower's obligations to the lender:
    - the borrower gave security over the London properties; and
    - Aurium Real Estate London Ultra Prima Limited (**parent**) created a security interest over the borrower's shares in favour of Solutus Advisors Limited as security trustee (**security trustee**).
- The security trustee held the borrower's shares on the terms of an English law security trust set out in a facility agreement.
- The borrower defaulted on its payment obligations to the lender. The security trustee tried to sell the London properties, but the highest price offered was considerably less than the debt owed by the borrower to the lender (approx £162.3 million). Consequently, the lender decided to redevelop the London properties itself and then try to sell them.
- The lender instructed the security trustee to sell the borrower's shares to a company that is related to the lender for a sale price equal to the debt owed by the borrower to the lender. The sale price was in excess of the price any prospective buyer was prepared to pay for the London properties.

Why was a court application made?

Where a security taker sells a secured asset, the Security Law requires the security taker to:

- take all commercially reasonable steps to get fair market value for the secured asset at the time of sale;
- act in other respects in a commercially reasonable manner in relation to the sale; and
- enter into an asset sale agreement on commercially reasonable terms.

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The Security Law allows a security taker to apply to the court for an order supporting the enforcement of a security interest.

Similarly, the Trusts (Jersey) Law 1984 (**Trusts Law**) allows a trustee to apply to the court for directions concerning the way in which the trustee should act in connection with any matter concerning a trust and gives the court the power to make any order it thinks fit. In addition, the court has previously recognised its inherent power to approve a momentous decision by a trustee.

In the circumstances, the lender considered the sale of the borrower's shares to a related party to be a momentous decision.

To protect the security trustee, and ensure that the sale of the borrower's shares was carried out in accordance with the Security Law, the security trustee applied to the court for an order approving the sale under the Security Law and the Trusts Law.

What did the court say?

Here are the key takeaways from the case.

Security giver must be given notice of the application

Initially, the application was made on what is called an ex parte basis. In other words, without notice to the parent.

Since a security giver would be entitled to the balance of the enforcement proceeds of a security interest (if any remained after the secured obligations were repaid), the court said that an application of this kind cannot be made without the security taker giving notice of the application to the security giver. It is then a matter for the security giver to decide whether or not it wishes to attend court.

The application was adjourned to allow the security trustee to give notice of the application to the parent. The parent which chose not to attend the hearing.

Security Law

The court examined the powers given to it under the Security Law to make an order supporting the enforcement of a security interest. It said that the Security Law only gives it the power to make an order if it considers the order reasonably necessary to make it possible or practicable for the security taker to enforce its rights.

The court pointed out that the security trustee did not need the court's assistance to sell the borrower's shares – it had the power to sell them under the security agreement. It said that:

- the security trustee simply wanted the protection of a court order confirming that the sale would comply with the requirements of the Security Law; and
- this was not reasonably necessary to make it possible or practicable for the security trustee to sell the borrower's shares.

The court said that the Security Law did not give it the power to approve the terms of the proposed sale.

Trusts Law

The court examined the powers given to it under the Trusts Law to make an order regarding the sale of the borrower's shares.

The court noted that although the security trustee:

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- was required by the facility agreement to exercise its powers in accordance with the instructions of the lender;
- would not be liable for any act or omission if it acted in accordance with those instructions; and
- was entitled to an indemnity from the lender,

the security trustee was nonetheless:

- liable for any gross negligence or wilful misconduct under the facility agreement; and
- owed an unqualified duty under the Security Law to take all commercially reasonable steps to get fair market value for the borrower's shares at the time of sale and would potentially be liable to the parent if it failed to do so.

The court concluded that:

- the lender did not bear the entire economic risk; and
- the security trustee had potential liabilities,

in connection with the sale of the borrower's shares, so it was appropriate for the security trustee to ask the court to approve the sale of the borrower's shares if it considered the sale to be a momentous decision.

Sale terms

The court noted that:

- efforts had been made over a lengthy period to sell the London properties and that the highest price offered was considerably less than the debt owed by the borrower to the lender;
- in the opinion of an international valuer, it was unlikely that a higher offer would be received for the London properties if they were marketed again; and
- the proposed sale of the London properties to a party related to the lender for an amount equal to the debt owed to the lender was comfortably in excess of the market value of the London properties.

The court concluded that:

- the security trustee had taken all commercially reasonable steps to obtain fair market value for the London properties;
- the security trustee had acted in all other respects in a commercially reasonable in connection with the sale; and
- the terms of the sale contract were commercially reasonable.

The court noted the conflict of interests given the proposed buyer was related to the lender, but concluded the proposed buyer was in the same position as the other persons who made other offers to buy the London properties.

Consequently, the court approved the sale of the borrower's shares under the Trusts Law for the price, and in the manner, proposed.

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Collas Crill comment

It is helpful that the court has:

- clarified the application process by making clear that a security giver must be given notice of an application; and
- confirmed that it is possible for a security trustee to seek court approval for a proposed sale of secured assets under the Trusts Law even where the trust is governed by foreign law.

On many occasions, however, a lender will not appoint a security trustee and hold security directly itself, which is a cheaper option for the borrower. Where a lender which holds security itself enforces its security would like to sell a secured asset:

- the decision to sell (and the sale terms) may be a momentous decision for the lender; and
- may expose the lender to a potential claim from the borrower (or its liquidator) that the sale terms or process do not comply with the Security Law.

In these circumstances, the lender has a legitimate interest applying to the court for an order approving the proposed sale terms or process. It is unfortunate that the lender is currently unable to do so. It remains to be seen whether the Security Law will be amended to allow a lender to make an application.

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About this case note

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