

DEFENDING THE ALLEGED DEVIL

A Tale of Tainted Turkish Tycoons

**Prepared for Presentation at
Jamaican Bar Association Continuing Legal
Education Weekend Seminar**

Ritz-Carlton Hotel, Montego Bay, Jamaica

9-11 November 2012

MOURANT OZANNES

**Hector Robinson
Partner
Cayman Islands**

The "Devils" and Their Antecedents

The Uzan family is a very wealthy Turkish family with business interests in banking, television and print media and telecommunications. Among their "accomplishments" is having been found by a U.S. federal court judge to have perpetrated a "*massive swindle*" on Motorola and Nokia, through one of their holdings, Telsim, the Turkish telecommunications giant. The judge awarded damages of over US\$4 billion against Telsim.

Its most prominent member, Cem Cengiz Uzan, is also the leader of the rightist Young Party. Cem is now believed to be in France facing an extradition request from Turkey where he has been sentenced in absentia for 23 years for fraud. His brother Murat Hakan Uzan is also on the run, facing a criminal arrest warrant from Turkey for fraud and racketeering.

Very few would contest these alleged "devilish" credentials. It cannot however be said that they have not made quite a solid contribution to common law jurisprudence. In a spin off from the Motorola case,, there have been a number of reported decisions in the English courts on issues such as search orders, freezing orders, contempt of court and enforcement of foreign judgments. They have also featured in 8 decisions reported and noted in the Cayman Islands Law Reports.

Imar Bank and TMSF

Among the entities controlled by the Uzans was Imar Bank. In 2003, the chief Turkish banking regulator took control of Imar Bank for its alleged failure to comply with certain regulatory requests. The regulators soon determined that there was a shortfall of the equivalent of US\$5 billion between the actual deposits on the books of the bank and the deposits reported to the Central Bank. The reported deposits were insured by the Turkish deposit insurance agency, known as Tasarruf Mevduati Sigorta Fonu (TMSF). The unreported deposits were, as one would expect, uninsured.

TMSF, an agency of the Turkish state (the importance of which will later become clear), bailed out the both the insured and uninsured depositors of Imar Bank to the extent of the bank's deficiency in assets. Under certain provisions of the Turkish Banking Act, by virtue of bailing out the depositors, TMSF had the power to use the provisions of a law called The Procedures for Collection of Public Receivables to recover the shortfall in deposits from the bank's owners and managers, mainly the Uzans, including Cem and Hakan.

BVI Companies and "Swimming Palaces"

Cem and Hakan, through two BVI registered companies, Wisteria Bay Limited and Utterton Limited respectively, were the beneficial owners of two luxury yachts (described in the Turkish press as "*swimming palaces*"), then called "*Frequency*" and "*Airwaves*". *Frequency* and *Airwaves* were both registered as British ships on the Cayman Islands Shipping Registry.

TMSF therefore initiated proceedings in Turkey under The Procedures for Collecting Public Receivables to seize and sell *Frequency* and *Airwaves*. The powers conferred on TMSF under this law would not all be considered conventional by persons bred on Western civil and common law systems, with their emphasis on due process. Under this law, TMSF is able to issue proceedings

in the civil, commercial and criminal courts. It also has certain administrative and quasi-judicial powers which enable TMSF to make determinations and conduct proceedings in respect of those whom it was pursuing.

The Turkish Proceedings

TMSF obtained freezing orders from the Turkish criminal courts pursuant to which it seized *Frequency* and *Airwaves*. Multiple proceedings followed in Turkey in which the yachts were ordered released by one court, seized by another court, released by yet another court and seized again by the original court. Although the legal proceedings against the Uzans were incomplete, the criminal court also ordered that the yachts be sold, supposedly on the basis that they were wasting assets, and that the freezing orders should continue over the proceeds of sale, pending the outcome of the proceedings.

An auction was scheduled for 10 December 2004. TMSF officials had a widely publicised viewing of the yachts on 24 November 2004.

The Cayman Ship Mortgages

In a more than slight coincidence, on 29 November 2004, BVI agents of Abdallah Al Ayed, a Jordanian national, presented for registration to the Cayman Shipping Registry, two mortgages, one against *Frequency* and the other against *Airwaves*. The supporting documents showed that the mortgages were being granted as security for two loans, one made in November 2000 for US\$30 million to Wisteria Bay, to be secured by a mortgage over *Frequency*, the other in March 2001 for US\$25 million to Utterton, to be secured by a mortgage over *Airwaves*.

The Commencement of Cayman Litigation

There commenced the Cayman litigation. With the auction scheduled for 10 December, TMSF sprung into action. It issued proceedings in Cayman's Grand Court seeking to set aside the mortgages as mere fraudulent devices aimed at defeating the interests of TMSF. On 6 December it applied *ex parte* and obtained an injunction "*restraining all dealings*" with *Frequency* and *Airwaves*. The injunction was granted in exactly the terms sought.

TMSF proceeded with the auction on 10 December at which *Frequency* was sold, with completion of the sale conditional on the outcome of the Cayman proceedings. The attorneys for the defendants immediately applied to the Grand Court to have TMSF held in contempt for proceeding with the auction in breach of the order restraining "*all dealings*" with the vessels. The court, rejecting the argument that the order only applied to the defendants, found TMSF in contempt, and made an order that it posts security for costs in the sum of US\$500,000. It was a case of TMSF getting exactly what they asked for but not entirely liking the consequences. They appealed.

Sovereign Immunity and the Interlocutory War of Attrition

In the Court of Appeal, TMSF completely changed tack not, as it ultimately turned out, for the last time. They raised, for the first time, the argument that the Cayman Court had no jurisdiction to grant an injunction against TMSF, because it was an agent of a foreign state exercising sovereign authority, and was entitled

to sovereign immunity under the Sovereign Immunity Act, a UK statute extended to the Cayman Islands. The Court of Appeal upheld the argument and set aside the injunction to the extent that it applied to TMSF, with the subsequent consequence that the order for security for costs was also set aside.

There followed multiple interlocutory skirmishes. TMSF was quite convinced, not without evidential justification, that it was able to prove that the mortgages and the loans were entirely fictitious, created only after it became clear that TMSF intended to sell the yachts. The defendants were keen to ensure that TMSF complied strictly with every rule of pleading and procedure or to have their claims struck out.

The Orders for Disclosure and Production of Documents

TMSF obtained an order that the defendants produce all the original loan and mortgage documents for forensic ink dating testing. An expert in this field was identified in England. Such an order proved critical to the outcome of the case, not for the results of the tests, which were disputed by the defendants' expert, but for the defendants' rather bungled and misguided actions in relation to it.

First, the defendants failed to produce any documents at all, even after a year after the first order. A number of reasons were given, some of which the court ultimately found to have been not unreasonable. The court nonetheless made an "*unless order*" that all originals be produced by a later date.

On the due date the defendants proved unable to produce any originals of one of the three documents in issue. The defendants sought and obtained an order for relief from the *unless order*, and variation of the order for the production of those originals. The defendants submitted an affidavit from the BVI agent who stated earnestly that he just had no idea what happened to the originals. The *unless order* was continued in respect of the other documents, and one set of originals of the mortgages and the loan agreements was, after some delay and with much fanfare, produced.

More Interlocutory Battles

The interlocutory battles continued. There were: an application on behalf of the defendants to strike out the statement of claim for its failure to plead adequately the elements of Turkish law on which TMSF relied; an application for a stay of the Cayman proceedings pending the conclusion of the criminal proceedings in Turkey; an application to strike out on the basis that the action constituted an attempt by Turkey to enforce its penal and public laws in Cayman, contrary to established principles of international law and to Cayman Islands public policy; and finally, an application that the court certify for trial as a preliminary issue, the question as to TMSF's title to the yachts.

None of the applications had more than the most modest success. The court: allowed TMSF to amend its pleadings to cure the defects in the pleading of Turkish law; ruled that the international law and public policy point merely raised a triable issue; and ruled that the issue as to TMSF's title was too intricately bound to the facts to be certified for trial as a preliminary issue.

All was then in place for a battle royal at a trial scheduled for 5 weeks before Chief Justice Smellie in April 2008.

A Good Arguable Case

Although the case against the defendants appeared pretty strong on the issue whether the loan and mortgage documents were created after the fact, they had fairly strong arguments as to whether that issue should even properly arise. In the skeleton argument for the trial the defendants argued with some force that the case was in effect a title dispute, and the issue as to fraud could only arise if it was found that TMSF had a good claim to title to the yachts which was capable of being defeated by the allegedly fraudulent mortgages. The argument imported issues of maritime law, public and private international law and the domestic law of both the Cayman Islands and Turkey.

Elements of the Defendants' Argument

The defendants argued that as an exception to the normal rule of international law that the law governing movable property was the *lex situs* of that property, the law governing a ship registered in accordance with the rules of maritime law, is the law of the port of registration. Consequently, it was argued, title to the yachts was governed by Cayman Islands law.

Under the Cayman Islands Merchant Shipping Law, the owner of a ship has absolute power to dispose of a ship including, the defendants argued, the power to grant a mortgage. Such a mortgage would only be subject to: interests appearing on the register; interests arising by contract; equitable interests enforceable against the owners of the vessels; and maritime claims enforceable *in rem* against the vessels.

Under Cayman Islands law, Wisteria and Utterton were the legal owners of the vessels. There was no challenge in any proceedings in Cayman, Turkey or in the BVI to the companies' title or to their registration as owners. The yachts had been acquired and registered well before the circumstances of the alleged fraud at Imar Bank arose and there was no suggestion that they were acquired with the proceeds of fraud.

There were no contractual or equitable claims (such as a compensatory constructive trust which might arise in a tracing claim) against either Wisteria Bay or Utterton. There was no final or conclusive judgment in Turkey against Wisteria Bay or Utterton which was enforceable in Cayman. In fact, Wisteria Bay and Utterton had not been named in any of the proceedings brought by TMSF as holders of property belonging to the Uzans. The defendants argued therefore that TMSF had no claim to title to the yachts which was capable of recognition or enforcement in the Cayman Islands.

The defendants further argued that even if Turkish law applied, under Turkish law (and for this there was expert evidence), the law governing the title to a ship not registered in Turkey is the law of the place of registration. The defendants had fairly cogent expert evidence that the acts on which TMSF relied were insufficient under Turkish law to convey title of the yachts to TMSF.

Even TMSF appeared tacitly to have conceded that point, as the basis on which they ultimately claimed in Cayman to have title to the vessels was completely different from the basis on which all their claims in Turkey had proceeded.

To those main arguments was added the argument that in any event, the court had no jurisdiction to entertain the claim, as it was an attempt by Turkey to enforce its penal or public laws in Cayman. After all, TMSF had claimed and had

been accorded sovereign immunity for the very acts which formed the basis of the claim. The order pursuant to which the yachts were seized was made as part of criminal proceedings, and the law under which they have proceeded was unhelpfully (for them) titled "The Procedures for Collection of Public Receivables".

A Massive "Own Goal"

But alas, the defendants never got a chance to deploy those arguments at the trial. Before the commencement of the trial it was revealed that before producing the documents which they were ordered by the Cayman court to produce, (and without their lawyers' knowledge) the defendants had taken the documents to their own expert to be tested. The plaintiff's expert regarded the testing as "destructive" as it involved punching tiny holes in the document. The Chief Justice took the most unfavourable view of this and found that the defendants had deliberately prevaricated with respect to the orders for production, in order to arrange their own testing, which, it was said, changed the condition of the documents.

Even worse, however, it became clear on the first day of the trial that the one set of originals which the defendants had produced was not the only set of originals created. The defendants had never revealed this fact to anyone, including their Cayman lawyers, despite having been carefully advised in writing about their disclosure obligations. The defendants obtained affidavits in which they attempted to explain that one set of the originals was in fact with Hakan Uzan who was by then, rather unhelpfully, on the run from Turkish criminal justice.

The Chief Justice found that the defendants were deliberately deceptive, that their conduct constituted an abuse of the process of the court which rendered a fair trial no longer possible. He ruled that they had forfeited their right to defend the claims, struck out the defences and gave judgment to TMSF for all the relief they sought on the statement of claim.

A very interesting appeal clearly loomed, but irreconcilable differences between the defendants and their successive attorneys, resulted in the appeal not being pursued.

The Lessons

The irony of *TMSF v Wisteria Bay Limited et al* is that had the defendants done nothing prior to the auction of the yachts, TMSF, or a purchaser, would have been obliged to contact the Cayman Islands Shipping Registry with respect to the registration of a transfer or the change of the registration of the yachts. The Registrar would quite likely not have proceeded without a court order, as all the shares in each vessel were owned by Wisteria and Utterton respectively. That would then have set the stage for a straight title dispute without the taint of allegations of fraud arising from the attempt to register the mortgages.

Wisteria and Utterton had an eminently winnable case on title as the Turkish authorities had obviously given no consideration to proceedings in the Cayman Islands when they initiated their Turkish proceedings to acquire the yachts. Needless to say, it is never attractive to be running a case the effect of which is, "*I may well have had fraudulent intent but in the end I did not defraud the plaintiff.*"

Ethical Considerations

In a case such as this, as an attorney trying to ensure that you stay on the right side of the ethical lines, you die a thousand deaths. You steadfastly represent the interests of the clients even with the knowledge that they may force you at some point to have to withdraw. In such circumstances one needs to be clear in one's own mind as to where the line lies and should not hesitate to withdraw if it is likely to be overstepped.

The case also underscores the importance of carefully written advice to clients at the outset on issues such as their disclosure obligations in proceedings. It is particularly important in cases involving clients from foreign jurisdictions where the concept that you must honestly and fairly disclose every relevant document in your possession or power is completely alien. Had the attorneys not provided clear, written advice to the clients on this issue, they might have had difficulty extricating themselves from the clients' seemingly deceptive web.

Risk and Compliance Issues

One other factor especially relevant in the Cayman Islands, and certainly in my firm, is the importance of risk and compliance issues in the acceptance of new business. Every client and every matter has to undergo positive scrutiny as to the nature of the business and the purpose of the representation before new business is accepted. This is both a part of the anti-money laundering regime which is required by statute and regulations, as well as a guard against "*reputational risk*" to the firm.

TMSF v Wisteria Bay would have attracted the attention of the risk and compliance police within the firm on two grounds: first the fact that WorldCheck would reveal the multiple criminal and civil proceedings which were underway against the companies' beneficial owners; and secondly, the fact that Cem Uzan was a "*politically exposed person*" or PEP. Had this been a transactional matter, the business would in all likelihood have been refused. The anti-money laundering regulations however regard the provision of advice and representation in or in relation to ongoing proceedings as "*non-relevant financial business*". As such, although this matter would be determined as "*high risk*" the business can be accepted on condition that there is a constant review of the risk

Effective Use of Tactical Procedural Applications

The case is also a perfect example of how tactical procedural applications can be used to great effect in commercial litigation proceedings. The defendants certainly made all the procedural applications which we could reasonably have made in the case. As it turned out, an uncertain case for the plaintiff turned into a winner mainly because the plaintiff's lawyers were persistent in holding the defendants to their disclosure obligations to the plaintiff and the court. They obtained an order for production of the original documents well before the pleadings were closed, because the documents were at the centre of an important issue in the case. When the documents were not produced on time they sought an "*unless order*". They resisted every attempt to vary the orders and had them reinforced at every opportunity. They could not have anticipated that the defendants would have failed to comply. In the absence of the repeated unless orders, the failure to comply would have been just another procedural irregularity which could either have been explained or remedied.

