IN THE COURT OF APPEAL OF THE CAYMAN ISLANDS
CICA 8 of 2011

BEFORE

The Rt Hon Sir John Chadwick, President

The Hon Ian Forte, Justice of Appeal

The Hon Elliott Mottley, Justice of Appeal

ON APPEAL FROM THE GRAND COURT

IN THE MATTER OF THE COMPANIES LAW (2010 REVISION)

AND

IN THE MATTER OF RE ABC COMPANY (SPC)

BETWEEN

ABC COMPANY (SPC)

Appellant

-and-

J & CO LTD

Respondent

Mr Mac Imrie, Mr Matthew Crawford and **Ms Caroline Moran** of Maples & Calder for the Appellant
Mr Thomas Lowe QC with **Ms Laura Hatfield** and **Mr Samuel Dawson** of Solomon Harris for the Respondent

Hearing dates: 8 and 9 September 2011
Reasons released: 25 May 2012

REASONS FOR JUDGMENT

Sir John Chadwick, President:

1. This is an appeal from an order made on 1 August 2011 by Justice Andrew Jones QC in proceedings for the winding up of the appellant, ABC Company (SPC) ("the Company").

2. The proceedings were commenced by the presentation by J & Co Ltd ("the petitioner") of a petition under section 94(1) of the Companies Law (2010 Revision), The petition, which was dated 20 June 2011 and subsequently amended on 13 July 2011, alleged that the petitioner was a contributory of the Company and that, in the circumstances therein set out, it was just and equitable that the Company should be wound up pursuant to section 92(e) of the Law. By summons dated 26 July 2011 the Company sought an order that the amended petition be struck out pursuant to the inherent jurisdiction of the court on the grounds that it had no reasonable prospect of success and/or was an abuse of the process of the court. That summons came before Justice Andrew Jones for hearing on 1 August 2011. By an order made that day he dismissed the summons and gave the petitioner leave to re-amend the petition so as to seek, in the alternative, the winding up of one of the funds comprised in the Company's segregated portfolio.

3. On 5 August 2011 this Court gave leave to appeal from that order. That appeal was heard on 8 and 9 September 2011. On the completion of oral argument, this Court stated that, for reasons that would be put in writing, it would allow the appeal, set aside the order of 1 August 2011 and strike out the amended petition.

The amended petition

4. The allegations made in the amended petition, may be summarised (so far as material) as follows:
   (1) The Company was incorporated on 31 October 2003 under the laws of the Cayman Islands as an exempted limited company. On or about 29 June 2007 it converted to an exempted segregated portfolio company.
   (2) The authorised share capital of the Company is divided into management shares and participating redeemable shares. All of the management shares are

held by a Cayman Islands exempted limited company, ABC Fund Management Limited (the "Fund Manager").

(3) The Company was incorporated as "an open ended investment vehicle for the purposes of carrying on investment business globally for the benefit of its shareholders". It was said, in an offering memorandum dated 21 December 2010, that the general investment objective of the Company was to "provide investors with an opportunity to benefit from capital growth and income opportunities in the world's equity, bond, property and currency markets".

(4) The offering memorandum listed 82 segregated portfolios of the Company as at that date; and indicated that a further 16 segregated portfolios were to be launched on 1 January 2011. All of the segregated portfolios were established to operate as open ended investment funds.

(5) The petitioner is the holder of participating redeemable preference shares issued in respect of one of the Company's segregated portfolios (the German Fund). The investment objective of that fund was stated, in the offering memorandum, to be:

> "to provide investors with an opportunity to benefit from capital appreciation from investment in commercial properties or the shares in property holding companies. All real property owned either directly or indirectly by the Fund will be located in the German Federal Republic and will usually be let to large company tenants on lease terms commensurate with local market conditions. The properties will be let on a mixture of long unexpired lease terms, higher yielding properties let on shorter leases and opportunities which require active management to enhance the investment value, for example the opportunity to extend an occupational leases before lease expiry."

(6) On 26 February 2008, investors in the German Fund were advised that a decision had been taken to suspend temporarily the calculation of the Net Asset Value ("NAV") of the Fund. The effect, it is said, was to suspend all subscriptions and redemptions of shares issued in respect of the German Fund. Between February 2008 and 24 June 2011 (shortly after the presentation of the petition) the NAV of the Fund was not calculated or published; and no subscriptions or redemptions in respect of that Fund were permitted.

(7) Nevertheless, it is said, during the period of suspension the directors of the Company continued to pay management fees to the Fund Manager.

(8) On or about 12 April 2010, the directors of the Company proposed changes to the articles of association and offering memorandum. The changes were stated to be necessary as they would:

> ". . . allow the Directors to instruct the Fund Administrator to calculate and publish the NAV on a monthly basis, (the NAV is the total of the Fund's assets less the total of the Fund's liabilities) without automatically recommencing the subscription/redemption cycle for each of the sub-Funds. This will restore full transparency on values for Shareholders and may facilitate the creation of a secondary market in the Sub-Fund's shares. The changes would also allow the Directors to set redemption gates, allowing the orderly management of redemptions from the Fund once the suspension on redemptions is lifted."

The proposed changes were approved by special resolutions passed at shareholder meetings held between May and October 2010. On 14 May 2010 the Fund Manager gave notice that "within the next month [the Directors] will issue an update on the plans and timetables for the suspended real estate funds including the reintroduction of the calculation of monthly Net Asset Values".

(9) It is said that the special resolution amending the articles of association in respect of the German Fund would not have been passed by the requisite majority had it not been for the votes cast in respect of shares under the discretionary management of the ABC Group.

(10) By letter dated 29 November 2010 US counsel (Reed Smith) wrote to the directors of the Company and the Fund Manager raising a number of issues regarding the management and status of the German Fund. In response to that letter the Fund Manager provided the petitioner (through its US counsel) with a document described as a "Fund Update" in which it was stated (i) that the assets of the German Fund were to be liquidated over the following three years and pro-rata distributions of capital were to be made to shareholders as liquidity allowed (a process described as the "Liquidation"); (ii) that NAV calculation would recommence in February 2011, but redemptions of shares would remain suspended for the duration of the Liquidation (estimated to be until 2013); (iii) that the German Fund would continue to issue to investors half-yearly valuations and yearly audited financial statements; and (iv) that the investors would receive "quarterly notes about the progress of the Fund".

5. On the basis of those allegations it is said that the substratum of the Company had failed. Paragraphs 28 to 30 of the amended petition are in these terms:

> "28. The Fund Update confirms that the German Fund has permanently ceased all subscriptions and redemptions of shares, permanently ceased substantially all investment business, and is now solely engaged in the liquidation of assets and the distribution of the proceeds of such liquidation to shareholders. Therefore the German Fund has ceased to carry out any investment business as set out in its offering documents, or at all, and as such has ceased to operate as a viable open ended investment fund.
>
> 29. In addition to the German Fund, there are 18 other segregated portfolios of the Company which have ceased subscriptions and redemptions and are now in suspension (together with the German Fund the "Suspended SPs"). The combined NAV of the Suspended SPs constitutes approximately ⅓ of the aggregate NAV of all the Company's segregated portfolios.
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> 30. As a result of the failure of certain of its segregated portfolios as detailed above the Company has ceased to carry on business in accordance with the reasonable expectations of its shareholders based on the representations made in the Company's offering memorandum and therefore the substratum of the Company has failed."

6. The petition and the amended petition were verified by affidavits of Dr XX, sworn respectively on 24 June and 14 July 2011. Dr XX is (or was at the time) Chief Investment Officer at DEF AG, which (as he stated) "acts as the investment advisor to a number of underlying beneficial owners of shares in [the Company] which shares are registered in the name of [the petitioner] as custodian". Documents exhibited to those affidavits included copies of (i) the amended and restated memorandum and articles of association of the Company, (ii) the Company's amended offering memorandum, (iii) the letter dated 29 November 2010 to which reference had been made in the petition and (iv) the Fund Manager's response to that letter and (*inter alia*) the Fund Update.

The evidence filed by the Company on its application to strike out

7. The Company relied upon two affidavits of Mr McL, a director, sworn (respectively) on 11 and 21 July 2011. The first of those affidavits was sworn "for the immediate and urgent purpose of supporting the Company's application to restrain the advertisement, publication or service of the Petition to third parties

and shareholders". It was said, at paragraph 2.1, that the petition contained "serious material inaccuracies", which the deponent went on to particularise; and, further, that "without proper safeguards to prevent its dissemination, the Petition has the potential to cause the Company and its underlying investors irreparable harm, even if the Petition is eventually struck out or withdrawn or dismissed after a full hearing". It is, I think, common ground – and, if not, it is reasonably clear – that it was the evidence in that affidavit which led to the amendment of the petition on 13 July 2011.

8. Mr McL's first affidavit contains the following statements which are not, I think, contentious:

> "2.2 It is correct that the Real Estate segregated portfolios ('SPs') of the Company ('Real Estate SPs') have suspended subscriptions and redemptions. However the Company has not ceased operations. The Company is still operating on a going concern basis and is of substantial size. The Real Estate SPs constitute 32% of the Company's SPs' combined NAV, i.e. $286m out of $864m. All other SPs with one exception noted below ('Other SPs') which represent the remaining NAV of the Company are trading normally and are accepting subscriptions and redemptions, just as they always have. The Other SPs' combined NAVs are $578 million representing approximately 68% of the Company. All of the above figures are based on current exchange rates, because the Company's SPs are denominated in Sterling, Euros and Dollars. They are also based on the Real Estate SPs' most recently struck NAV, dated 28 February 2011 and the Other SPs' NAV calculations as at 31 May 2011.
>
> 2.3 The petitioner is the registered holder of shares representing 2.8% of the SP in which it is invested, the German Real Estate Segregated Portfolio ('German SP'). That investment represents 0.85% of the Real Estate SPs'combined NAV and 0.27% of the Company's SPs' combined NAV. . . .
>
> 2.4 The Company was not given any warning of this Petition. It never received a single letter from the Petitioner in relation to the matters set out in the petition. The last it heard from the DEF AG and its representative, Dr XX, was the letter received from Reed Smith dated 29 November 2010 exhibited to Dr XX's verifying affidavit . . ."

9. At paragraph 9 of his first affidavit, Mr McL explained why it was said that the presentation and publication of the petition has the potential for "a catastrophic effect" on the Company's business and the shareholders' investments. He gave

five reasons for that view. First, that the filing of the petition might cause an event of default which would give lenders the ability to exercise their security rights over the relevant properties: if so – and if lenders did enforce their security – that "a forced sale of the properties would most likely result in a nil return on equity to investors". Second, that even if, strictly, a default has not occurred, potential purchasers of the real estate assets will know that, potentially, the ultimate beneficial owner of those properties is facing "a distressed sale scenario which will result in a depression of the potential sale prices". Third, that "the Master Funds which relate to the Other SPs are exposed to certain ISDA Master Agreements"; and that an event of default would be caused if the relevant Master Fund NAV was to drop by more than 30%. That, it is said, would be a real risk for the reason, fourth, that if the petition were advertised there would be "a run of redemptions on the relevant SPs leading to a suspension of redemptions across all SPs". Fifth, that "any rumours in the market that the Company is being forcibly liquidated is in my experience likely to destroy the secondary market for shares which the amendments to the Articles of Association were in part designed to facilitate." He concluded:

> "9.8 In short, the advertisement of the petition and/or the service (if not the mere fact of it being filed) would result in a very large destruction in value for shareholders and I would ask the Court to consider the interests of the vast majority of shareholders whose SPs are functioning as normal but will be severely affected by the Petition entering the public domain."

The procedural history

10. As I have said, the petition was dated 20 June 2011. It was, I think, presented shortly thereafter. It came before Justice Andrew Jones for directions on 11 July 2011. The matter was adjourned to enable the petitioner to make amendments to the petition in the light of the information set out in Mr McL's affidavit of that date, The petition was re-presented, as amended on or about 13 July 2011. It came back before the judge on 22 July 2011, on the adjourned hearing of the application for directions. At that hearing counsel for the Company, Mr Imrie, sought a further adjournment, so that the Company could make an application to strike out before directions were given. It was said (i) that there was a legitimate basis for making such an application and (ii) that the balance of convenience

favoured allowing the Company to do so before directions for the hearing of the petition were given. In an oral ruling, given on 22 July 2011, the judge rejected each of those submissions. As to the first, he said this:

> "I am not persuaded that there is a legitimate basis for a strike out application. I would only strike out this petition if I was satisfied, on the basis of the matters pleaded in the petition (as amended) and the undisputed evidence, that the petition was bound to fail. Counsel makes reasonable points which are relevant to the determination of the petition on its merits, but I do not see how those points can be legitimately made in support of a strike out application.
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> He says that, as a matter of Cayman Islands' law, a company cannot be said to have lost its substratum if it is capable of carrying out some commercial activity permitted by its articles, with the result that this petition is bound to fail because the Company still has at least some portfolios which are in fact carrying on business. I considered this argument and reviewed the authorities relating to it in *Re Heriot Trade Finance Fund Limited* and came to the conclusion that it does not represent Cayman Islands law. How the Court should apply these principles in the circumstances of this particular case, involving as it does a segregated portfolio company, is open to argument. However, unless and until the Court of Appeal reverses my decision in *Heriot*, it seems to me that it is Mr Imrie's intended strike out application that is bound to fail."

11. Notwithstanding the judge's strong indication, in the final sentence of the passage just set out, that an application to strike out the petition would have little or no prospect of success before him, the Company was not deterred. As I have said, the summons to strike out was issued on 26 July 2011. That summons came before the judge on 1 August 2011. It was dismissed. The judge put his Reasons into writing and handed them down on 3 August 2011.

Segregated Portfolio Companies

12. It is common ground that the Company is a segregated portfolio company for the purposes of Part XIV of the Companies Law (2010 Revision). It is convenient to set out the material provisions in that Part of the Law – and the recommendations for changes to the regime affecting companies registered under that Part which were made in 2006 (but not adopted) - before turning to examine the reasons which led the judge to dismiss the summons of 26 July 2011.

13. Section 212 of the Law provides that a "segregated portfolio company" means an exempted company which is registered under section 213(1). That subsection provides that, subject to sections 213(2) and 214 (neither of which are of relevance in the present case), any exempted company may apply to the Registrar to be registered as an exempted segregated portfolio company. Section 215 requires that a segregated portfolio company shall include in its name the letters "SPC" or the words "Segregated Portfolio Company". Section 216 is in these terms (so far as material):

> "216(1) A segregated portfolio company may create one or more segregated portfolios in order to segregate the assets and liabilities of the company held within or on behalf of a portfolio from the assets and liabilities of the company held within or on behalf of any other segregated portfolio of the company or the assets and liabilities of the company which are not held within or on behalf of any segregated portfolio of the company.
>
> (2) A segregated portfolio company shall be a single legal entity and any portfolio of or within a segregated portfolio company shall not constitute a legal entity separate from the company.
>
> (3) . . ."

Section 217(1) provides that a segregated portfolio company may create and issue shares in one or more classes or series, "the proceeds of the issue of which shall be included in the segregated portfolio assets of and accounted for in the segregated portfolio in respect of which the segregated portfolio shares are issued". Section 217(4) provides that:

> "217(4) Segregated portfolio dividends or other distributions shall be paid on segregated portfolio shares by reference only to the accounts of and to and out of the segregated portfolio assets and liabilities of the segregated portfolio in respect of which the segregated portfolio shares were issued and otherwise in accordance with the rights of such shares."

Section 219 of the Law provides that the assets of a segregated portfolio company shall be either segregated portfolio assets or general assets. Segregated portfolio assets are assets of the company held within or on behalf of the segregated portfolios of the company. General assets comprise the assets of the company which are not segregated portfolio assets. The assets of a segregated portfolio comprise (a) assets representing the share capital and reserves

attributable to the segregated portfolio and (b) all other assets attributable to or held within the segregated portfolio. Section 219(6) is in these terms:

> "219(6) It shall be the duty of the directors of a segregated portfolio company to establish and maintain (or cause to be established and maintained) procedures –
>
> (a) to segregate, and keep segregated, portfolio assets separate and separately identifiable from general assets;
>
> (b) to segregate, and keep segregated, portfolio assets of each segregated portfolio separate and separately identifiable from segregated portfolio assets of any other segregated portfolio; and
>
> (c) to ensure that assets and liabilities are not transferred between segregated portfolios otherwise than at full value."

14. Section 220 of the Law provides that segregated portfolio assets (a) shall only be available and used to meet liabilities to the creditors of the segregated portfolio company who are creditors in respect of that segregated portfolio; and (b) shall not be available or used to meet liabilities to creditors of the company who are not creditors in respect of that segregated portfolio. Section 221 is in these terms (so far as material):

> "221(1) Where a liability of a segregated portfolio company to a person arises from a matter, or is otherwise imposed, in respect of or attributable to a particular segregated portfolio –
>
> (a) Such liability shall extend only to, and that person shall, in respect of that liability, be entitled to have recourse only to –
>
> (i) firstly, the segregated portfolio assets attributable to such segregated portfolio; and
>
> (ii) secondly, unless specifically prohibited by the articles of association, the segregated portfolio company's general assets, to the extent that the segregated portfolio assets attributable to such segregated portfolio are insufficient to satisfy the liability, and to the extent that the segregated portfolio company's general assets exceed any minimum capital amounts lawfully required by any regulatory body in the Islands; and
>
> (b) such liability shall not extend to, and that person shall not, in respect of that liability, be entitled to have recourse to the segregated portfolio assets attributable to any other segregated portfolio.
>
> (2) . . ."

15. Section 223 of the Law applies in the context of a winding up of a segregated portfolio company. It is in these terms:

> "223(1) Notwithstanding any statutory provision or rule of law to the contrary, in the winding up of a segregated portfolio company, the liquidator –
>
> (a) shall deal with the company's assets only in accordance with the procedures set out in section 219(6); and
>
> (b) in discharge of the claims of creditors of the segregated portfolio company, shall apply the company's assets to those entitled to have recourse thereto under this Part.
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> (2) Section 140 shall be modified so that it shall apply in relation to protected segregated portfolio companies in accordance with this Part and, in the event of any conflict between this Part and section 140, this Part shall prevail."

Section 140 of the Law (which is to have effect, in the case of a segregated portfolio company, subject to Part XIV) requires (*inter alia*) that, on winding up, the property of a company shall be applied in satisfaction of its liabilities *pari passu*; and subject thereto is to be distributed amongst the members according to their rights and interests in the company.

16. The effect of section 223 of the Law, read with sections 140, 216(1), 217(4), 219(6), 220 and 221(1), is that, on the liquidation of a segregated portfolio company, the assets of each segregated portfolio shall be applied in discharge of the claims of those creditors of the company (and only those creditors) "entitled to have recourse thereto" under Part XIV – that is to say, in discharge of liabilities attributable to that segregated portfolio – and, subject thereto, shall be distributed to the holders of segregated portfolio shares issued in respect of that segregated portfolio. But that is not to say that creditors of the company who are entitled to have recourse to the assets of a particular segregated portfolio may not, also, be entitled on a liquidation of the company to have recourse to the general assets of the company: see section 221(1)(a)(ii) of the Law. And it is not to say that the holders of shares issued in respect of a particular segregated portfolio may not, also, be entitled on a liquidation of the company to a distribution out of the general assets: that will turn on the terms upon which the shares are issued.

17. Sections 224 to 228 of the Law make provision for receivership orders in respect of segregated portfolios. Section 224 provides:

> "224(1) Subject to subsections (2) to (5), if in relation to a segregated portfolio company, the Court is satisfied –
>
> (a) that the segregated portfolio assets attributable to a particular segregated portfolio of the company (when account is taken of the company's general assets, unless there are no creditors in respect of that segregated portfolio entitled to have recourse to the company's general assets) are or are likely to be insufficient to discharge the claims of creditors in respect of that segregated portfolio; and
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> (b) that the making of an order under this section would achieve the purposes set out in subsection (3),
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> the Court may make a receivership order under this section in respect of that segregated portfolio.
>
> (2) A receivership order may be made in respect of one or more segregated portfolios.
>
> (3) A receivership order shall direct that the business and segregated portfolio assets of and attributable to a segregated portfolio shall be managed by a receiver specified in the order for the purposes of –
>
> (a) the orderly closing down of the business of or attributable to the segregated portfolio; and
>
> (b) the distribution of the segregated portfolio assets attributable to the segregated portfolio to those entitled to have recourse thereto.
>
> (4) A receivership order –
>
> (a) may not be made if the segregated portfolio company is in winding up; and
>
> (b) shall cease to be of effect upon the commencement of the winding up of the segregated portfolio company, but without prejudice to prior acts of the receiver or his agents.
>
> (5) No resolution for the voluntary winding up of a segregated portfolio company of which any segregated portfolio is subject to a receivership order shall be effective without leave of the Court."

Section 225(1) provides that an application for a receivership order in respect of a segregated portfolio of a segregated portfolio company may be made by the company, its directors, any creditor of the company in respect of that segregated portfolio, any holder of segregated portfolio shares in respect of that segregated portfolio or (in respect of a company licensed under the regulatory laws) the Cayman Islands Monetary Authority. Section 226 sets out the functions and

powers of a receiver appointed under a receivership order; section 227 provides for the discharge of receivership orders; and section 228 provides for the remuneration of the receiver.

18. It is necessary, in the context of the present case, to keep in mind: (i) that a segregated portfolio company is a single legal entity and that any portfolio within a segregated portfolio company does not constitute a legal entity separate from the company (section 216(2) of the Law); (ii) that the making of a receivership order in respect of a particular segregated portfolio may not have the same effect – in relation to creditors who are entitled to have recourse to the assets of that segregated portfolio or in relation to the holders of shares issued in respect of that segregated portfolio – as the making of an order for the winding up of the company (compare sections 221(1)(a) and 224(3)(b)); and (iii) that, although an application for a receivership order can be made by the holder of shares issued in respect of the relevant segregated portfolio, the basis for such an order is that the assets of the segregated portfolio are, or are likely to be, insufficient to pay the claims of the creditors in respect of that portfolio (section 224(1)). There is no provision for the making of a receivership order in respect of an individual segregated portfolio at the suit of a shareholder on just and equitable grounds.

The recommendations made in 2006

19. In April 2006 the Law Reform Commission – of which the judge (then Mr Andrew Jones QC) was a member - submitted a Report entitled *"Review of the Corporate Insolvency Law and Recommendations for the Amendment of Part V of the Companies Law*". Attached to the Report was a draft Bill; the provisions of which, if enacted as a Law, were intended to give effect to the Commission's recommendations. The Report, itself, contains no reference to Part XIV or to segregated portfolio companies. But the *Memorandum of Objects and Reasons*, which serves as an introduction to the draft Bill, contains a summary of the main provisions in the proposed new Part V which includes the following statement (at paragraph 2 on page 4):

> "Sections 243 to 248 of the principal Law will be repealed because they create a regime for the liquidation of segregated portfolios which is inconsistent with Part V. It is intended that a segregated

portfolio should be liquidated in exactly the same way as if it was a company. . . ."

20. At that date, Part XIV of the Companies Law (2004 Revision) ("the principal Law") comprised sections 232 to 248. So far as material (in the present context) the provisions in those sections were in substantially the same terms as those now found in Part XIV (sections 212 to 228) of the Companies Law (2010 Revision). In particular, section 243 of the principal Law (Winding up of company) was in the same terms as section 223 of the Companies Law (2010 Revision) – save that the references to earlier sections were re-numbered – and sections 244 to 248 of the principal Law (Receivership orders, Application for receivership orders, Administration of receivership orders, Discharge of receivership orders and Remuneration of receivers) were in the same terms – save, again, that references to earlier sections were re-numbered – as sections 224 to 228 of the Companies Law (2010 Revision).

21. The summary at paragraph 2 of the *Memorandum of Objects and Reasons* went on to explain that the intended result - "that a segregated portfolio should be liquidated in exactly the same way as if it was a company" - was to be achieved "by the combination of sections 90(2) and 91(e) [of the draft Bill]".

22. Clause 5 of the draft Bill provided that the principal Law be amended by repealing the existing Part V and by substituting new provisions (as Part V) in its place. The proposed new provisions were to include the following, as sections 90 and 91:

"90(1) A company may be wound up –
(a) compulsorily by order of the Court;
(b) voluntarily –
(i) by virtue of a special resolution;
(ii) because the period (if any) fixed for the duration of the company by its articles of association has expired;
(iii) because the event (if any) has occurred, on the occurrence of which its articles of association provide that the company shall be wound up; or
(c) under the supervision of the Court.

(2) A segregated portfolio of a company registered under Part XIV may be wound up in the same manner notwithstanding that the company of which it is part is not itself being wound up and in this Part where the context so requires –

(a) 'company' includes a segregated portfolio;
(b) 'creditor' includes creditors of a segregated portfolio;
(c) 'contributory' includes a holder of segregated portfolio shares; and
(d) 'liquidator' includes the liquidator of a segregated portfolio.

91 The Court has jurisdiction to make winding up orders in respect of –

(a) an existing company;
(b) a company incorporated and registered under this Law;
(c) a body incorporated under any other law; and
(d) a foreign company which –
    (i) has property located in the Islands
    (ii) is carrying on business in the Islands
    (iii) is the general partner of a limited partnership; or
    (iv) is registered under Part IX; and
(e) any segregated portfolio of a segregated portfolio company."

23. Clause 7 of the draft Bill provided for the amendment of the principal Law by the repeal of the defined terms "receiver" and "receivership" in section 232. Clause 8 provided for the amendment of the principal Law by the repeal of sections 243 to 248.

24. Partial effect was given to the recommendations of the Law Reform Commission by the Companies (Amendment) Law 2007 (Law 15 of 2007). The new Part V of the Companies Law, introduced by Law 15 of 2007, was taken in, on consolidation and revision, as Part V of the Companies Law (2009 Revision). The provisions enacted in 2007 are now found in Part V of the Companies Law (2010 Revision). But those provisions differ in important respects from the proposals in the draft Bill. First, the Legislature did not repeal sections 243 to 248 in Part XIV of the principal Law (as had been proposed in clause 8 of the draft Bill). Those sections were retained (as sections 223 to 228) in Part XIV of the 2009 and 2010 Revisions. Nor did the Legislature amend section 232 of the principal Law by repealing the definitions of "receiver" and "receivership order" (as had been proposed in clause 7 of the draft Bill). Those definitions were retained in section 212 in the 2009 and 2010 Revisions. Second, the Legislature did not enact a subsection (2) of section 90 in the new Part V and it did not enact a paragraph (e) in section 91: both proposed in the draft Bill.

25. In those circumstances the Legislature must be taken to have decided not to give effect to the recommendation of the Law Reform Commission (set out at paragraph 2 of the summary of provisions in the *Memorandum of Objects and Reasons* and to which I have already referred) that "a segregated portfolio should be liquidated in exactly the same way as if it was a company".

The judge's reasons

26. I turn, now, to examine the reasons which led the judge to dismiss the summons to strike out the petition. The judge summarised the submissions made on behalf of the Company at paragraphs 2 and 3 of his Reasons:

> "2. The Company's principal argument, as set out in Mr Imrie's lengthy and carefully argued written submission, is that this petition is bound to fail because it is based upon the allegation that one of its many segregated portfolios, namely the German Fund, has ceased to operate as a viable economic entity since February 2008. It is said that the Court only has jurisdiction to make a winding up order in respect of the Company, as opposed to an individual portfolio, and that the Petitioner's pleaded case is bound to fail because it is not alleged that the Company has lost its substratum. Mr Imrie says that the reasoning in *Re Belmont Asset Based Lending Ltd* [2010] 1 CILR 83 should apply to an SPC in exactly the same way as it applies to any other company, a proposition about which I am not persuaded.
>
> 3. The segregated portfolios are separate economic units which exist under the umbrella of a single legal entity. If, as in this case, a majority of the segregated portfolios are trading normally in accordance with the reasonable expectations of their shareholders, the argument is that it cannot be said, as a matter of law, that the company has lost its substratum, with the result that it could never be just and equitable to make a winding up order in respect of the company as a whole. . . ."

The judge rejected that argument. He said this:

> "3. . . . Whilst I recognise the logic of this argument, it seems to me that it produces a commercially unacceptable result which is not one which could have been intended by the Legislature and that on a true construction of the relevant sections of the Companies Law, the Court does have jurisdiction to make a winding up order or grant some alternative remedy on the basis that an individual portfolio has lost its substratum and ceased to operate as a viable economic entity".

That was, he said, an important and difficult point of law which had not previously been addressed by any court in this jurisdiction. He was not prepared

to conclude that he should strike out the petition on the basis that it was bound to fail.

27. The "relevant sections of the Companies Law" to which the judge made reference in his Reasons were sections 89, 92 and 94, 95, 217, 224 and 225 to 228. At paragraph 4 of his Reasons he said this:

> "4. Mr Imrie accepted during the course of his argument that the Petitioner is a contributory of the Company, as defined in section 89, and therefore has standing under section 94(1)(c) to present a petition for a winding up order in respect of the Company, but not in respect of the portfolio. Furthermore, he says that it is not open to a contributory to apply for a receivership order under section 224(1) because this remedy is only available to a creditor on grounds of insolvency. At first glance this is an attractive argument, but it becomes less clear when one appreciates that section 217 creates two different kinds of shareholders. All shares, of whatever class, are issued by the Company which is the legal entity, but section 217 provides that it can issue either (a) 'segregated portfolio shares', the proceeds of which shall be included in the segregated portfolio assets of and accounted for in the balance sheet of the portfolio or (b) what I call 'general shares', the proceeds of which are included in the company's general assets. The petitioner is the registered holder of segregated portfolio shares, which means that it has an economic interest only in the assets of the German Fund. It follows that this Petitioner should be treated as a contributory of the portfolio, with standing to present a winding up petition against the Company by which it seeks a remedy in respect of the portfolio."

28. At paragraph 5 of his Reasons the judge went on to explain why he took the view that it followed, from the matters set out in the first five sentences in paragraph 4, that the petitioner "should be treated as a contributory of the [the German Fund]"; and that, in "a winding up petition against the company" it could seek "a remedy in respect of [the German Fund]". He said this:

> "5. Clearly, the winding up petition must be presented against the legal entity, but I see no reason why the remedy should not take effect only in respect of the portfolio which is, by definition, a separate economic entity. This is what would happen in the case of a creditor's petition on grounds of insolvency. The petition would be presented against the company which would be the counterparty to the contract out of which the debt arises, but the remedy would be a receivership order under section 224(1) because the creditor's recourse is limited to the assets of the portfolio in question. This analysis can be applied to the holder of

> segregated portfolio shares as opposed to general shares. The contributory presents its petition against the company, but seeks a remedy only in respect of the portfolio to which the shares relate. . . ."

He recorded counsel's submission that a receivership order under section 224 could be made in respect of a segregated portfolio only where the court was satisfied that the portfolio was, or was likely to be, insolvent; and that the Companies Law provided no remedy limited in effect "only in respect of the portfolio to which the shares relate" to the holder of shares issued in respect of a segregated portfolio which could not be said to be, or to be likely to be, insolvent. He rejected that submission on the ground that he was not persuaded "that this is the conclusion intended by the Legislature".

29. The judge explained, at paragraph 6 of his Reasons, why he took the view that it was, at the least, arguable that a receivership order could be made, at the suit of the holder of shares issued in respect of a segregated portfolio, notwithstanding that the court was not satisfied that the segregated portfolio assets were, or were likely to be, insufficient to discharge the claims of creditors in respect of that portfolio: that is to say, notwithstanding that the requirement imposed by paragraph (a) of section 224(1) of the Law was not met. He said this:

> "6. Section 225(1) states that an application for a receivership order in respect of a segregated portfolio of an SPC can be made by, inter alia, '(d) any holder of segregated portfolio shares in respect of that segregated portfolio'. Clearly the Legislature cannot have contemplated that shareholders should have standing to present a petition for a receivership order on grounds of insolvency. Some other purpose must have been intended. It seems to me that it is at least arguable that the Petitioner, as the registered holder of segregated portfolio shares issued in respect of the German Fund, has locus under section 225(1)(d) to present a petition against the Company for a receivership order in respect of the portfolio. It seems to me that a receivership order is nothing more or less than a winding up order which takes effect only in respect of a portfolio. If such a remedy is available to a creditor on grounds of insolvency, I can see no reason why it should not be available to a contributory on the just and equitable ground. The Legislature clearly intended to give this remedy to contributories and it would make no sense to construe sections 225-228 as applying only to insolvent portfolios. To construe the Law in this way would render the contributory's remedy useless."

30. The judge then went on to consider the position on the basis that it was not open to a contributory to seek a receivership order in respect of a segregated portfolio on the just and equitable ground. He said this, at paragraph 7 of his Reasons:

> "7. Even if the remedy of a receivership order is not available to a contributory on the just and equitable ground (in which case section 225(1)(d) would seem to serve no purpose), I do not see any reason why the same result should not be achieved in reliance on sections 92 and 94 alone. In the absence of any authority directly in point, it seems to me that it is open to the Court to conclude that it would be just and equitable to make a winding up order on the basis that some, but not all, of the portfolios of an SPC have ceased to operate as viable entities in accordance with the reasonable expectations of the shareholders, that is to say the holders of the segregated portfolio shares in question. The holders of the shares issued in respect of the other portfolios will have no interest in what happens to the German Fund, except to make the point that its liquidation should be conducted in a way which has no adverse impact upon the business of their portfolios. This argument naturally leads to consideration of an alternative remedy under section 95(3). It seems to me that the provisions of paragraphs (a), (b) and (d), taken together, are broad enough to enable the Court to achieve a result which is equivalent to making a winding up in respect of the portfolio in question. For example, the Court could order the Company to appoint a qualified insolvency practitioner having authority to wind up the German Fund in consultation with the relevant shareholders."

31. At paragraph 8 of his Reasons the judge expressed his conclusion in these terms:

> "8. For these reasons and in the absence of any authority directly in point, I am not persuaded that this Petition is bound to fail. I think that the Legislature must have intended that the shareholders of an SPC should have available to them the same remedies that are available to the shareholders of any other company, taking into account that they may have an economic interest in only one portfolio. I think that the petition discloses an arguable case which should be allowed to go to trial."

32. It can be seen, therefore, that the judge took the view that it was arguable that the Companies Law conferred jurisdiction on the court to make an order the effect of which was to wind up an individual portfolio in circumstances where the court was satisfied that that portfolio had lost its substratum and ceased to operate as a viable economic entity. He seems to have identified two possible routes which might lead to that conclusion.

33. First, he expressed the view that the court could make a receivership order under section 224(1) of the Law in respect of an individual segregated portfolio on the just and equitable ground, notwithstanding that that segregated portfolio could not be said to be, or to be likely to become, insolvent: paragraphs 5 and 6 of his judgment.

34. Second, he suggested that, on a contributory's petition to wind up the company on the just and equitable ground, it would be open to the court conclude that "it would be just and equitable to make a winding up order on the basis that some, but not all, of the portfolios of an SPC have ceased to operate as viable entities in accordance with the reasonable expectations of the shareholders"; and that, if the court did reach that conclusion, then it could (without recourse to section 224(1), but by way of alternative remedy under section 95(3) of the Law), "achieve a result which is equivalent to making a winding up in respect of the portfolio in question".

The re-amended petition

35. The judge was, of course, aware that the amended petition before him did not seek a receivership order in respect of the German Fund; that it did not seek the winding up of the German Fund (as distinct from the winding up of the Company); and that it did not seek alternative remedies under section 95(3) of the Law. The only remedies sought by the amended petition were the winding up of the Company, the appointment of nominated Joint Official Liquidators (with certain specified powers) and costs. It was at the judge's suggestion – and with his encouragement – that the petitioner sought leave to re-amend the petition so as to include a prayer that, in the alternative, the German Fund be wound up; and for "alternative remedies pursuant to s. 95(3) of the Companies Law (2010 Revision) concerning the German Fund". The judge granted leave to re-amend the petition in the terms sought: see paragraph 2 of the order dated 1 August 2011.

The issues for determination on this appeal

36. The Company appeals from both paragraphs 1 and 2 of the Order of 1 August 2011. It is said, in the Memorandum of Grounds of Appeal dated 16 August

2011, (i) that the judge erred in law when determining that the amended petition, "seeking a winding up order on the just and equitable ground based on the sole pleaded allegation that the Company had lost its substratum" was not bound to fail; and (ii) that the judge erred in law when granting leave to re-amend the petition so as to seek a winding up order in respect of the German Fund under section 92(e) of the Law, "such pleading being hopeless in law and bound to fail".

37. In the event, it has been unnecessary for this Court to decide whether the judge was wrong to give leave to re-amend the petition so as to seek a winding up order in respect of the German Fund. It is, I think, sufficient to refer to the position taken by the petitioner, as set out in paragraphs 7 and 8 of its skeleton argument dated 2 September 2011:

> "7 The Petitioner does not submit that a single portfolio can be would up under Section 92 of the Companies Law. The Petitioner accepts that it can only present a winding up order (*sic*) under section 225(1) when the grounds set out in Section 224(1) are satisfied. The Petitioner does, however, submit that the consequence of a winding up order of the Company would result in orders under Section 95(3) confined to the Petitioner's segregated portfolio, at least if the Petitioner were unsupported by other segregated portfolios.
>
> 8. The Petitioner accepts that it is a shareholder of the Company, albeit that its shares are referenced to a particular segregated portfolio under Section 217. The only entity capable of issuing shares is the Company itself, not any of the segregated portfolios. This has the consequence that the Petitioner does have standing, by virtue of Section 94(1)(c) to present a winding up petition in respect of the whole Company on the basis set out in Section 92(e), namely that it is 'just and equitable' for the Company to be wound up."

38. At paragraph 7 of its skeleton argument the petitioner made it clear that it did not submit that a single portfolio could be wound up under section 92 of the Companies Law. Accordingly, it did not rely on the re-amendments (to paragraphs 1 and 2 of the prayer for relief) that it had made pursuant to the leave which it had sought and obtained from the judge on 1 August 2011.

39. Nor has it been necessary to decide whether the judge was wrong to think it arguable that the court could make a receivership order under section 224(1) of

the Law in respect of an individual segregated portfolio on the just and equitable ground, notwithstanding that that segregated portfolio could not be said to be, or to be likely to become, insolvent. The re-amended petition does not seek a receivership order under section 224(1); and the petitioner accepts (at paragraph 7 of its skeleton argument) that "it can only present a winding up order (*sic*) under section 225(1) when the grounds set out in section 224(1) are satisfied".

40. It has been unnecessary, also, for this Court to decide whether the judge was wrong to give leave to re-amend the petition so as seek (at paragraph 9 of the prayer for relief) "alternative remedies pursuant to s.95(3) of the Companies Law (2010 Revision) concerning the German Fund". It is, I think, common ground that, if the court were satisfied that (in the absence of an alternative remedy) it would be just and equitable to wind up the Company, it would have jurisdiction, under section 95(3) and as an alternative to a winding up order, to make an order that the business and segregated portfolio assets of or attributable to the German Fund be managed by a receiver for the purposes of the orderly closing down of the business of or attributable to that Fund and the distribution of the segregated portfolio assets to those entitled to have recourse thereto (including, if the fund is solvent, to the petitioner): that is to say, to make an order the effect of which would be the same as that which a receivership order would have under section 224(3) of the Law. The amended petition sought, at paragraph 9 of the prayer for relief, "Such other orders as the Court considers necessary": plainly, in an appropriate case, the court could exercise the jurisdiction under section 95(3) of the Law without the need for a further amendment to add the words "including alternative remedies pursuant to s.95(3) of [the Law] concerning the German Fund".

41. It is, perhaps, less clear that the converse proposition is also common ground: that is to say, it is less clear that it is common ground that, unless the court were satisfied that (in the absence of an alternative remedy) it would be just and equitable to wind up the Company, there is no jurisdiction to make an order under section 95(3) of the Law. The petitioner's contentions in this context (so far as they go) are set out at paragraph 9 of its skeleton argument:

> "9. It is submitted that the Court does have jurisdiction to wind up a segregated portfolio company ('SPC') as a whole. The

> Companies Law expressly gives to a segregated portfolio shareholder of an SPC (who can only be affected to the extent of his segregated portfolio) an unrestricted right to petition on the well understood just and equitable ground. That would be meaningless if the shareholder had to show that these grounds applied to every other segregated portfolio. In all other jurisdictions with SPCs the shareholders are confined to 'winding up' (i.e appointing receivers) of their segregated portfolio. In the Cayman Islands that restriction was deliberately not introduced. The rights of the investor in the Cayman Islands are at large, circumscribed by the discretion of the Court under Section 95(3) to confine the remedy. Otherwise a segregated portfolio shareholder has no remedy at all."

42. Plainly, the court does have jurisdiction to wind up a segregated portfolio company "as a whole"; and, equally plainly, a petition for the winding up of a segregated portfolio company on the just and equitable ground can be presented by a shareholder whose shares have been issued in respect of a single segregated portfolio. The holder of segregated portfolio shares is not confined, under the Companies Law (2010 Revision) to seeking the appointment of receivers of the segregated portfolio in respect of which the shares have been issued: even if (which is not established on the material before this Court) that is the position "In all other jurisdictions with SPCs". In that sense it may be said that shareholder's rights are "at large": the holder of segregated portfolio shares can seek an order for the winding up of the company as a whole. And, as I have said, if persuaded that (in the absence of an alternative remedy) it was just and equitable to wind up the company as a whole, the court might think it appropriate, as an alternative to winding up the company, to make orders under section 95(3) of the Law which would have the effect of realising and distributing the assets of the individual segregated portfolio as if the portfolio were itself in liquidation.

43. Subject to the question whether there is a free-standing jurisdiction to wind up an individual segregated portfolio under section 95(3) of the Law (in so far as the answer to that question is not common ground), the issue on this appeal is whether, on the basis of such of the allegations made in the amended petition as the petitioner has any realistic prospect of establishing at a trial, the petition to wind up the company on the just and equitable ground is bound to fail.

Whether there is a free-standing jurisdiction to wind up a segregated portfolio under section 95(3) of the Law?

44. In my view it must be accepted that, as the law stands in the Cayman Islands, section 95(3) of the Companies Law does not provide free-standing remedies. As this Court pointed out in *Camulos Partners Offshore Limited v Kathrein and Company* [2010] 1 CILR 303, 318-9, paragraph [38], the gateway to an order under section 95(3) is that the court is satisfied that, if no alternative remedy were available, it would be "just and equitable" to wind up the company. The judgment in *Camulos Partners* was delivered on 18 March 2010. The Companies Law (2010 Revision) was enacted on 6 July 2010, some three and a half months later. Since then, there has been a further amendment of the Law: the Companies (Amendment) Law 2011 (Law 16 of 2011) was enacted on 22 April 2011. The Legislature has had two opportunities to enact provisions which do confer the jurisdiction in respect of a free-standing remedy which, prior to the judgments of this Court in *Camulos Partners* and *In re Strategic Turnaround Partnership Limited* [2008] CILR 447, may have been thought to exist under section 95(3); but it has not chosen to do so. It must be accepted in this Court that, although an order may be made under section 95(3) "as an alternative to a winding up order", there is no jurisdiction to make an order under that section in circumstances in which the court would, if the alternative were not available, refuse to make a winding up order on the just and equitable ground.

Winding up the company on the basis of the allegations in the amended petition?

45. I turn, therefore, to the question whether, on the basis of such the allegations made in the amended petition as the petitioner has any realistic prospect of establishing at a trial, the petition to wind up the company on the just and equitable ground is bound to fail.

46. I put the question in those terms because, as it seems to me, in deciding whether the petition should be struck out, or allowed to proceed to trial, the Court should have no regard to allegations which the petitioner has no realistic prospect of being able to establish at trial. In particular, the Court should not have regard to the allegation made in paragraph 30 of the amended petition that:

> "As a result of the failure of certain of its segregated portfolios as detailed above the Company has ceased to carry on business in

> accordance with the reasonable expectations of its shareholders based on the representations made in the Company's offering memorandum . . ."

47. It is, I think, common ground that the "reasonable expectations of [the Company's] shareholders" – in the context of addressing a contention that "the substratum of the Company has failed" - are not to be determined, or (at the least) not to be determined exclusively, by reference to the Memorandum of Association of the Company. The objects for which the Company was established were stated in the Memorandum of Association in the widest terms:

> "The objects for which the Company is established are unrestricted and the Company has full power and authority to carry out any object not prohibited by any law as provided by the Companies Law."

In order to determine the reasonable expectations of the Company's shareholders it is necessary to have regard to the Company's Articles of Association and the relevant Offering Documents.

48. The Company's Articles of Association permit the issue of "Participating Shares". A Participating Share is defined as:

> "A participating redeemable share referred to as such in Article 11 issued subject to and in accordance with Section 37 of the Law and these Articles . . ."

Article 30 of the Company's Articles of Association – as they were before amendment in 2010 – provided that the Company might issue one or more classes of Participating Shares "which are to be redeemed or are liable to be redeemed at the option of the Company or the holder at such times and on such notice as is determined by the Board of Directors before the issue of the relevant class". Article 32(a) provided that members might redeem Participating Shares on a Redemption Date by giving the Company such prior written notice as the Offering Memorandum in respect of the relevant Participating Shares required. Article 32(c) was in these terms (so far as material):

> "If the determination of the Net Asset Value of Participating Shares of any class is suspended beyond the day on which it would normally occur by reason of a declaration by the Directors under Article 50 (suspension of the valuation in respect of the class) the Member's right to have his Participating Shares of that class redeemed under this Article will be similarly suspended . . ."

Article 50 gave the Directors power to declare a suspension of the determination of Net Asset Value (with a consequential suspension of the right to redeem under Article 32(c)) for the whole or any part of a period during (*inter alia*) "(b) the existence of any state of affairs which, in the Directors' opinion, constitutes an emergency as a result of which disposal of investments by the Company owned by it would not be reasonably practicable or would be seriously prejudicial to the Members, . . .".

49. Article 165 of the Company's Articles of Association provided that, "Subject to and insofar as permitted by the Law, the Company may by Special Resolution alter or amend its Memorandum of Association or these Articles in whole or in part". That provision was to be read with Article 54 which required that:

> "54(a) The rights attached to any class of Shares may be varied either whilst the Company is a going concern or during or in contemplation of a winding up, with the consent in writing of the holders of not less than three-fourths of the issued Shares of that class, or with the sanction of a resolution passed at a meeting of the holders of the Shares of that class by a majority of three-fourths of the votes cast at that meeting, but not otherwise . . .
>
> (b) No substantial change in the Company's business or affairs, nor any change of capitalization or other measure may be effected except with the prior approval of a majority of any class of Shares affected voting at a class meeting. . . ."

50. As alleged in the amended petition, the Articles of Association of the Company were amended, following class meetings held during 2010. Article 32(a) (which conferred on shareholders the right to redeem) was replaced by a new article, Article 50(a), which was in much the same terms. Articles 32(c) and 50 (suspension of the right to redeem following suspension of the determination of Net Asset Value) were, in effect, replaced by a new provision, under the heading "Suspension":

> "59. The Directors may, from time to time, in their absolute discretion and for any reason, declare a Suspension. The Directors shall promptly notify all affected Shareholders of any such Suspension and shall promptly notify such Shareholders upon termination of such Suspension."

"Suspension", in that context, has the meaning given in Article 2 ("Interpretation") of the amended Articles of Association:

> "'Suspension' – A determination by the Directors to postpone or suspend (i) the calculation of the Net Asset Value of Participating Shares of one or more Classes and/or Series (and the applicable Valuation Date); (ii) the issue of Participating Shares of one or more Classes and/or Series (and the applicable Subscription Date); (iii) the redemption of Participating Shares of one or more Classes and/or Series (and the applicable Redemption Date); and/or (iv) the payment of any redemption proceeds (even if Valuation Dates and Redemption Dates are not postponed)."

51. It is important to keep in mind that the amended Articles of Association were adopted by resolutions passed (with the requisite three-fourths majority) at class meetings of all classes of Participating Shares. The amendments must be taken to reflect the wishes of shareholders generally: their effect is not restricted to the holders of segregated portfolio shares issued in respect of the German Fund, or to the holders of segregated portfolio shares issued in respect of Real Estate Funds. A requisite majority (or majorities) of shareholders generally determined, in 2010, that the directors of the Company should have the power of suspension which was introduced by the new Article 59. That had been explained in a Notice to Shareholders dated 23 April 2010 (exhibited to Dr XX's second affidavit as part of "XX2"). That notice includes the statement that:

> "The company's original Articles were drafted nearly 10 years ago in 2000, since when the operation of offshore funds has moved on a long way.
>
> The principal changes to the Articles are:
>
> - The ability to suspend the calculation of the Net Asset Value, the issue of Participating Shares, the redemption of Participating Shares and the payment of redemption proceeds.
>
> . . ."

52. It is important, also, to keep in mind that – notwithstanding the allegations made in paragraphs 23 to 25 of the amended petition - there is no challenge to the validity of the resolutions pursuant to which the Articles of Association were amended.

53. It follows, therefore, that – if and insofar as the "reasonable expectations" of shareholders are to be determined by reference to the Articles of Association of the Company, as amended in 2010 – it is impossible for the petitioner to contend that a *bona fide* exercise by the directors of the power (conferred by Article 59 of

the amended Articles) to declare a suspension in relation to the German Fund – and other Real Estate Funds - was outside the reasonable expectations of the holders of segregated portfolio shares issued in respect of that fund or those funds; or outside the reasonable expectations of shareholders generally. Rather, it must be accepted that, when voting on the resolutions to amend the Articles of Association in 2010, shareholders appreciated, and intended, that the directors (acting *bona fide*) should be able to exercise that power if, in their discretion, they determined that the interests of the Company so required.

54. Three Offering Documents have been put in evidence: the first dated 9 July 2007; a second dated 29 May 2008; and a third dated 21 December 2010. Each contains a statement (in section III, Characteristics of Shares, paragraph (c)) that the holders of Shares have the rights set out in the Articles of Association of the Company; and each contains a statement (in section III, Constitution of the Company, paragraph (e)) that the rights attaching to any class or series of shares may be varied with the consent in writing of the holders of the majority of the issued Shares of that class or series or with the sanction of a resolution passed by a majority of the votes cast at a separate general meeting of the holders of the shares of that class.

55. The Offering Documents dated 2007 and 2008 each contains a statement (also in section III, under Risk Factors – General) that:

> "The liquidity of some of the investments held by the Portfolios cannot be guaranteed. Any illiquidity may prevent a Portfolio from concluding an investment transaction on satisfactory terms and, in certain circumstances, may prevent redemptions of (and subscriptions for) investments and Shares."

A statement in similar terms appears in the Offering Document dated 2010 (in Section I, under General Risk Warnings):

> "The liquidity of some of the investments held by the Segregated Portfolios cannot be guaranteed. Any illiquidity may prevent a Segregated Portfolio from concluding an investment transaction on satisfactory terms and, in certain circumstances, may prevent redemptions of (and subscriptions for) investments and Shares."

Those statements (although properly included) are, if I may say so, statements of the obvious: in that it would be obvious to an experienced investor (to whom the Offering Documents are addressed) contemplating investment in an open-ended

investment portfolio that the ability of the investment vehicle to redeem his investment from time to time would depend on the liquidity of that portfolio. Illiquidity – whether a consequence of inability to realise investments (or inability to do so save on the basis of a "forced sale" price) in a depressed market or of a lack of new investors – is likely to lead to an inability to "pay out" those who wish to redeem. An appreciation that that is a feature of an open-ended investment fund must, in my view, be part of the reasonable expectations of those who chose to invest in such funds.

56. The Offering Document dated 2010, to which reference is made in the amended petition, contains three statements of particular relevance in the context of the present petition. First, it contains a statement, under the heading "Suspended Net Asset Value Calculations", that:

> "Owing to unfavourable conditions in the real estate markets the Directors suspended the calculation of Net Asset Values of the UK Real Estate and the UK Public Sector Real Estate Segregated Portfolios in October 2007 and of the German Real Estate Segregated Portfolio in February 2008. The position is unchanged at the date of this Offering Document and accordingly no applications for shares in any of these Segregated Portfolios can be accepted until further notice."

Second, it contains a statement, under the heading "Suspension", that "The Directors may, from time to time, in their absolute discretion and for any reason declare a Suspension"; and, for that purpose, "Suspension" is defined in the same terms as those in the amended Articles of Association. Third, it contains a statement (in Section III, under "Notice of Redemption") that:

> "If a Suspension of Redemptions of Participating Shares of the Relevant Class and/or Series has been declared by the Directors, the right of a Shareholder to have its Participating Shares redeemed shall be suspended . . ."

57. It is, of course, the fact that, as alleged at paragraph 16 of the amended petition, the investment objective of the German Fund – and the Company's other Real Estate Funds – is stated, in the 2010 offering document (as in the earlier offering documents), to be to provide opportunities to benefit from capital appreciation from investment into a range of commercial properties or the shares in property holding companies. But the documents must be read as a whole; and no informed investor, reading the documents as a whole, could fail to appreciate that the rights to redeem segregated portfolio shares were subject to the terms of the

Company's Articles of Association - which were stated in the offering documents to be available for inspection – and might, in certain circumstances, be suspended.

58. The Offering Document dated 2010 was an amended version of the earlier (2008) document: indeed, the version of the 2010 document exhibited (as part of "XX2") to the second affidavit of Dr XX is a made up copy, with "red-line amendments", of the document which was put before shareholders for approval in or about October 2010. It is common ground that the amendments were approved by majorities of the holders of segregated portfolio shares. Again, there is no challenge to the validity of the resolutions pursuant to which the offering documents were amended.

59. In those circumstances it is impossible for the petitioner to contend that the Company has ceased to carry on business in accordance with the reasonable expectations of its shareholders (or even in accordance with the reasonable expectations of the holders of segregated portfolio shares issued in respect of the German Fund or, more generally, in respect of the German Real Estate Funds) "based on the representations made in the Company's offering memorandum"; or to contend , on the basis of statements made in the offering documents, that a *bona fide* exercise by the directors of the power (conferred by Article 59 of the amended Articles) to declare a suspension in relation to the German Fund was outside the reasonable expectations of the holders of segregated portfolio shares issued in respect of that fund; or outside the reasonable expectations of shareholders generally.

60. Paragraph 27 of the amended petition refers to the "Fund Update" provided by the Company as an attachment to its letter of 7 December 2010 to the petitioner's United States attorneys (Reed Smith). The Fund Update takes the form of a report by the Investment Manager to the board of directors of the Company. It reports the approval of the shareholders, at a general meeting held on 10 September 2010, to the changes to the Articles of Association of the Company and the Offering Document. It is said that "We now have the flexibility to manage the Fund in the way that best responds to market conditions"; and that

the vote enables the Investment Manager to follow the strategy set out in the Fund Update.

61. That strategy is described in paragraph 1.2 of the document:

> "1.2 Strategy for German Real Estate Fund
>
> Our goal is to maximise and return capital to shareholders during the liquidation of the Fund over the next three years.
>
> To achieve this, our strategy is to manage the properties to increase their value and then sell them.
>
> We are developing a schedule of planned sales from now until 2013. The exact timing of each sale will depend on when we can achieve the best price for the individual properties.
>
> During the remaining three years of the Fund, we expect to be able to increase its value. We will do this through loan amortisation, the run-down of break costs on loans and value events on individual properties (e.g. lease extensions).
>
> We have performed a detailed analysis on each property. We compared current values to expected values at the end of December 2012 so that we could set a sales strategy. On the basis of assumptions made, the returns available to shareholders will improve significantly over the period.
>
> We expect the sum available to be returned to shareholders will be significantly in excess of the current equity in the Fund. We will write further on this in the next quarterly update. The current estimate on this is that cash returned to shareholders could improve by over 35% from €120 million at present to over €150 million."

In the following paragraph (paragraph 1.3: Implications for shareholders) it is said that:

> "Suspension of redemptions will continue for the next 3 years while the Fund is liquidated.
>
> The Directors intend to make a pro rata distribution of capital each time there is sufficient liquidity within the Fund
>
> This course will enable us to manage the Fund and wind down the portfolio in an orderly manner."

62. It is plain that the references in those paragraphs to "the liquidation of the Fund" are not to a liquidation of any corporate body in the sense understood in the context of the Companies Law. Rather, those references are to a process of realisation of assets, payment of debts and distribution of surplus (if any) in

relation to each segregated portfolio within the "German Real Estate Fund" comparable to that which would take place if receivership orders were made in respect of those segregated portfolios under section 224(1) of the Law. There is no challenge in the amended petition to the *bona fides* of the strategy proposed in the Fund Update; nor to the Investment Manager's view that, to pursue that strategy, is to "manage the Fund in the way that best responds to market conditions". In particular, there is nothing in the amended petition to suggest that the "liquidation" of the individual segregated portfolios in the sense which I have described – that is to say, the process of realisation of assets, payment of debts and distribution of surplus (if any) in relation to each portfolio – would be more advantageous to the holders of segregated portfolio shares (in that it would be quicker or lead to a more substantial distribution) if carried out pursuant to an order made under section 95(3) of the Law than the pursuit of the strategy proposed in the Fund Update.

Conflicting decisions in Caribbean Courts

63. The petitioner relies heavily of the judge's earlier decision in *In re Belmont Asset Based Lending Limited*. It is convenient to take the facts from the headnote in the report at [2010] (1) CILR 83:

> "The petitioner owned a number of shares in the respondent open-ended mutual fund, which had an investment objective of providing long-term capital appreciation to shareholders by investing in asset-based lending or related schemes. General market conditions, together with the effects of a serious fraud which had significantly reduced the value of the fund's investments, had an adverse impact on the fund to the extent that it was no longer able to pursue its investment objective. The fund's board of directors passed a resolution recommending that the investment manager place the fund into voluntary liquidation but this was not done. Instead, the investment manager began informally liquidating the fund by realizing its assets and making distributions to shareholders."

The petitioner sought a compulsory winding-up order, under section 92(e) of the Companies Law (the "just and equitable" ground) on the basis (*inter alia*) that there had been a loss of substratum. It was said that the purpose for which the fund was established could no longer be carried out and that the fund had therefore ceased to be viable. The petition was not opposed.

64. The judge addressed the issue whether "loss of substratum" in the circumstances alleged should, of itself, justify a winding up order on the just and equitable ground. He said this:

> "12. The issue is whether a finding of 'loss of substratum' is, by itself, sufficient to justify the court in making a winding-up order on the just and equitable ground under s.92(e) of the Companies Law (2009 Revision). The expression 'loss of substratum' or 'failure of substratum' are derived from English case law dating back to a decision of the Court of Appeal in *In re Suburban Hotel Co* (LR 2 Ch App at 750). Whilst it may be helpful for the court to categorise circumstances in which it will be considered just and equitable for a company to be compulsorily wound up, I question whether it is sensible to adopt terminology invented in the context of England's 19th century economy. A company was said to have "lost its substratum" if the purpose for which it was formed can no longer be carried out (*In re Bristol Joint Stock Bank* (44 Ch D at 712, *per* Kekewich J)); if the company has practically ceased to carry on business because it has become impractical to do so (*In re Diamond Fuel Co* (13 Ch D at 408, *per* James LJ)); or if the company was formed to pursue a specific business opportunity which is no longer available to it (*In re Haven Gold Mining Co* (20 Ch D 151). To translate these statements into a modern context, it can be said that it is just and equitable to make a winding-up order in respect of an open-ended corporate mutual fund if the circumstances are such that it has become impractical, if not actually impossible, to carry on its investment business in accordance with the reasonable expectations of its participating shareholders, based upon the representations contained in its offering document. If such a company, organised as an open-ended mutual fund, has ceased to be viable for whatever reason, the court will draw the inference that it is just and equitable for a winding- up order to be made."

65. At paragraph 15 of his judgment in *Belmont* the judge reaffirmed that "Wherever it is proved that a company established as an open-ended mutual fund is no longer viable as such, for whatever reason, the court will ordinarily conclude that it is just and equitable to make a winding-up order". He went on to express the view that there were sound policy reasons for making a winding-up order in respect of non-viable mutual funds, in spite of the fact that this situation has arisen without fault on the part of its management. At paragraphs 16 and 17 of his judgment he explained why he took that view:

> "16. Typically, mutual funds are established in the Cayman Islands by foreign financial services companies which then act as investment manager or adviser pursuant to a contract, the

terms of which will be summarized in the offering document. The skill set required of a successful investment manager is wholly different from that required of professional liquidators. Investment management agreements are invariably made on the assumption that the fund is a going concern and that the investment manager will be responsible for making investment decisions and managing investments, with the result that the terms may be inappropriate to the situation where the fund is being liquidated. Typically, the investment managers are remunerated on the basis of a percentage of NAV, often coupled with performance fees calculated as a percentage of realized gains. This basis of remuneration will become inappropriate if the fund ceases to be viable and the investment manager ceases to perform at least some of the functions contemplated by the investment management agreement and instead attempts to adopt a liquidation role. Investment management agreements rarely, if ever, contemplate the scenario in which the service provider's role changes from that of an investment manager to that of a liquidator.

17. An investor's decision to subscribe for shares will be based upon the reputation and past performance of the investment manager. So long as the fund's assets are being invested and managed in accordance with investment criteria and guidelines set out in the offering documents, shareholders cannot and do not expect to have any say in the investment decisions. The position changes if the fund ceases to be viable with the result that the NAV is suspended and the principal or only function left for the management is to realize the assets for the benefit of creditors and shareholders. This exercise may involve an investigation and pursuit of claims against the investment manager and other professional services providers which can only be undertaken by professional independent liquidators. Even if a fund is solvent on a balance sheet test and there is no apparent cause of complaint against any of its service providers, its investors should not be deprived of the advantages of having the task performed by professional independent liquidators. Nor should they be deprived of having the protections provided by the Companies Winding Up Rules simply because the investment manager (who may not have been at fault) chooses to undertake the task itself."

The judge concluded, in *Belmont*, by saying that, for the reasons he had given, he was satisfied that it was just and equitable to make a winding-up order in respect of the fund "simply on the basis that it is no longer viable as an open-ended mutual fund and notwithstanding that the allegations of breach of duty made against its investment manager have been withdrawn".

66. The judge's approach in *Belmont* was considered by Justice Bannister, sitting in the Eastern Caribbean Supreme Court (British Virgin Islands) in *Aris Multi-Strategy Lending Fund v Quantek Opportunity Fund* (unreported, 15 December 2010). It is, I think, sufficient in the present context to note that he disagreed with that approach. In *In re Heriot African Trade Finance Fund Limited* (unreported 4 January 2011) Justice Jones, in turn, considered the decision in *Aris v Quantek*. He said this:

> "35. Having reviewed what I said in *Re Belmont Asset Based Lending Ltd,* the learned judge [Justice Bannister] concluded as follows:
>
> > ' If Jones J was deciding (as I think he was) that it is just and equitable to wind up an open-ended investment fund on substratum grounds in circumstances where the company has yet to reach the limit of its possible existence, then unfortunately I have to disagree with him. In my judgment the only purpose for which liquidators are appointed by the Court is in order to manage the final moments of companies which the Court has decided, according to established principles, ought to be put out of existence . . ."
>
> He went on to describe *Quantek* as being in run-off". As I understand it Bannister J would say that it will not be just and equitable to appoint liquidators (the equivalent of making a winding-up order) on loss of substratum grounds in respect of an investment fund under the law of the British Virgin Islands unless and until its management have realized all the assets and distributed all the proceeds to its shareholders. If I have understood his judgment correctly, the law of the British Virgin Islands is not the same as that of the Cayman Islands."

He then went on to say this:

> "36 Counsel referred me to *Re Perfectair Holdings Ltd* [1990] BCLC 423 in which Scott J (as he then was) said (at page 437) 'The directors were not put in office and cannot claim to be maintained in office for the purpose of liquidating the company. That is not the function of managers. That is the function of a liquidator'. This must be right as a general statement of principle. However I do recognize that there may be circumstances in which it can be said that a liquidation is being carried out in the ordinary course of a company's business, as contemplated by its articles of association and offering documents. A fund may be set up for the very purpose of liquidating distressed assets. A fund may be set up as a limited duration company, in which case its articles of association will set out when, how and by whom the company is to be liquidated at the end of its pre-determined life. In those

> circumstances, it may be said that the liquidation is itself part of the company's business, in which case it would not be appropriate for the Court to interfere in the process by making a compulsory winding up order, at least in the absence of a serious breach of duty or serious mismanagement on the part of those responsible for the company's liquidation. The present case is wholly different. . . . In my judgment it cannot be said that an ad hoc liquidation of the Fund, conducted informally by management, is something which, in these circumstances, the participating shareholders should have anticipated in the ordinary course of business."

67. It must be anticipated that an appeal will come before this Court in which it will be necessary to choose between the approach of Justice Jones in *Belmont* and *Heriot*, on the one hand, and that of Justice Bannister in *Aris v Quantek* on the other hand: or, perhaps, to decide that the true approach in this jurisdiction should lie somewhere between the approaches respectively adopted in those cases. But this is not that appeal. The reason why it is not is that – as I have sought to explain earlier in this judgment - the issue in this appeal is not whether it would be just and equitable to wind up the German Fund. The issue in this appeal is whether (absent an alternative remedy under section 95(3) of the Law) it is arguable that it would be just and equitable to wind up the Company on the basis of such of the allegations made in the amended petition as the petitioner has any realistic prospect of establishing at a trial.

Conclusion

68. For the reasons which I have set out I am satisfied that the petitioner has no realistic prospect of establishing the fundamental proposition on which it relies: that, as a result of the failure of certain of its segregated portfolios (as described in the amended petition) the Company has ceased to carry on business in accordance with the reasonable expectations of its shareholders based on the representations made in the Company's offering memorandum. There is no other basis upon which it is or could be said that the substratum of the Company has failed; and no other basis alleged in the amended petition upon which the court could hold that it was just and equitable to wind up the Company.

Sir John Chadwick, President

Justice Forte, Justice of Appeal

69. I agree.

Justice Mottley, Justice of Appeal

70. I also agree.

[Note: The appeal was heard in private. At the conclusion of the oral hearing on 9 September 2011 the amended petition was struck out. The Court directed that its written Reasons, when delivered, were not to be made public for a period of 30 days; so as to give the Company the opportunity to make representations seeking the "anonymisation" of the written Reasons. The Company made such representations in a letter dated 24 April 2012. Anonymisation is not opposed by the petitioner.

Having considered the representations made on behalf of the Company, the Court is satisfied that it is in the interests of the administration of justice that the written reasons are anonymised to the extent reflected in the Reasons now released for publication.

The Court recognises the potential for oppression that exists when a petition for the winding-up of an open-ended investment vehicle is presented without proper grounds. It accepts that there is real fear, in such cases, that the fact that a petition has been presented, when known to investors and potential investors, will give rise to such a loss of confidence that, in practice, the business of the company will be destroyed – with consequential loss to investors – whether or not the petition could be successfully resisted; and that, given that fear, the company will be forced to accede to the petitioner's demands before the petition is advertised rather than fight the petition in the courts.

It is not in the interests of the administration of justice that a company should find itself in a position that it cannot resist a winding up petition presented without proper grounds for fear of the commercial consequences which will ensue. The Court is satisfied, from the representations made to it on behalf of the Company, that, notwithstanding that the petition has been struck out, there remains a real fear of adverse consequences if the Company is now identified.