IN THE COURT OF APPEAL OF THE CAYMAN ISLANDS

Civil Appeal No 7 of 2011

BEFORE:

The Rt Hon Sir John Chadwick, President
The Hon Ian Forte, Justice of Appeal
The Hon Dr Abdulai Conteh, Justice of Appeal

ON APPEAL FROM THE GRAND COURT
FINANCIAL SERVICES DIVISION
(Cause No FSD 60 of 2011)

IN THE MATTER OF THE COMPANIES LAW (2010 REVISION AS AMENDED)

AND IN THE MATTER OF AJW MASTER FUND II, LTD

AJW OFFSHORE II, LTD
(Acting by its Official Liquidators)

Appellant

-v-

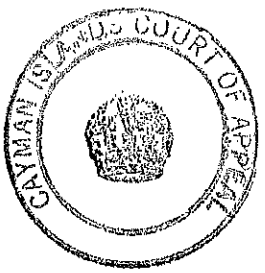
THE OFFICIAL LIQUIDATORS OF AJW MASTER FUND II LTD

Respondents

Mr Graeme Halkerston and **Ms Joanne Collett** of Appleby (Cayman) Ltd for the Appellant

Hearing: 4 August 2011
Judgment: 5 August 2011

JUDGMENT (released 15th August 2011)



Sir John Chadwick, President:

1. By his order made on 30th May 2011, on an application brought in the liquidation of AJW Master Fund II, Ltd ("the Master Fund") by the liquidators of AJW Offshore II Ltd ("the Offshore Fund"), Justice Andrew Jones QC directed that the costs of the applicants

be paid out of the assets of the Master Fund; but should be assessed in an amount which did not exceed US$25,000. This is an appeal against the "cap" imposed by that order in relation to the applicants' costs.

2. The Offshore Fund was one of two Feeder Funds: the other was AJW Qualified Partners II Ltd ("the Domestic Fund"). The Offshore Fund and the Domestic Fund were, together, the sole shareholders in the Master Fund. The interests of the underlying investors were as the shareholders of the Feeder Funds. The Feeder Funds provided a conduit for the investment by the underlying investors in the assets of the Master Fund.

3. On 13 September 2010 Field Nominees Limited, investors in the Offshore Fund, presented a petition for the winding up of the Offshore Fund on the just and equitable ground. Field Nominees Limited was, itself, was in liquidation. Its liquidators were partners of Kinetic Partners (Cayman) Ltd and Kinetic Partners LLP (together "Kinetic"). They sought appointment of themselves, or other Kinetic partners, as liquidators of the Offshore Fund. That petition was listed for hearing on 6 April 2011 before Justice Henderson. Until shortly before that date, the petition was opposed by those in control of the Offshore Fund and the Master Fund ("the Management").

4. On or about 1 April 2011 there was a change of mind by the Management. They decided that the Master Fund be put into voluntary liquidation. They appointed Mr. Simon Whicker and Mr. Chris Beighton of KPMG as voluntary liquidators of the Master Fund. On 1 April 2011, Mr Whicker and Mr Beighton, as voluntary liquidators of the Master Fund, presented a petition under s.124 of the Companies Law for the voluntary liquidation to continue under the supervision of the Court. That petition came before Justice Quin. After consideration of the papers – and without a hearing -, he made the supervision order sought. In particular, he appointed Mr Whicker and Mr Beighton as Official Liquidators of the Master Fund.

5. Following the decision to put the Master Fund into voluntary liquidation and the appointment of Mr Whicker and Mr Beighton as its Official Liquidators, the opposition to the winding-up of the Offshore Fund was withdrawn. The petition came before Henderson J on the 6 April 2011. He made the winding-up order sought. But he declined

to appoint the petitioner's nominees - partners of Kinetic - as liquidators of the Offshore Fund.

6. It is common ground (as Justice Andrew Jones held) that, in cases where both a master fund and a feeder fund are in liquidation, the interests of the underlying investors are usually (although not invariably) best served by the appointment of common liquidators to each fund. In those circumstances, it is unsurprising that, on 6 April 2011, Justice Henderson was asked to appoint Mr Whicker and Mr Beighton (who had been appointed Official Liquidators of the Master Fund by Justice Quin a few days earlier) to be liquidators of the Offshore Fund also. Indeed, the decision to put the Master Fund into voluntary liquidation and to seek the appointment of the Management's nominees as Official Liquidators of that fund by petition under section 124 of the Companies Law may be seen as having been taken with that end in view. But Justice Henderson declined to make that appointment. He held that KPMG were in a position of conflict, or potential conflict, which made it impossible for Mr Whicker and Mr Beighton to satisfy the independence requirements under the legislation. He appointed two insolvency practitioners employed by PwC Corporate Finance and Recovery Cayman Ltd, Mr. Walker and Mr. Stokoe, as Official Liquidators of the Offshore Fund.

7. I should add that it seems clear that Justice Quin was not informed, when (on 1 April 2011) he was invited (without a hearing) to appoint Mr Whicker and Mr Beighton as Official Liquidators of the Master Fund, that there was a possibility that there would be a challenge to their independence on the hearing of the petition (then pending) to wind up the Offshore Fund: he did not know that, at the hearing of that petition (listed to take place in a few days time) there would be a dispute as to who should be the liquidators of the Offshore Fund. If Justice Quin had known that, he might well have taken the view that it was inappropriate to make the appointment that he did on 1 April 2011.

8. Following their appointment as Official Liquidators of the Offshore Fund, Mr Walker and Mr Stokoe invited Mr Whicker and Mr Beighton to retire as liquidators of the Master Fund so that they (Mr. Walker and Mr. Stokoe) could be appointed Official Liquidators

of the Master Fund in their place. Mr Whicker and Mr Beighton, through their attorneys Campbells, declined to do so.

9. It was in those circumstances that, on 19 April 2011, Mr Walker and Mr Stokoe caused the Offshore Fund (of which they were Official Liquidators) to issue a summons in the liquidation of the Master Fund, seeking an order for the removal of Mr. Whicker and Mr. Beighton as Official Liquidators of the Master Fund and for the appointment of themselves as Official Liquidators for the Master Fund in their place. That summons which came before Justice Andrew Jones on 30 May 2011.

10. On the hearing of that summons Justice Andrew Jones removed Mr. Whicker and Mr. Beighton from office as Official Liquidators of the Master Fund and appointed Mr. Stokoe and Mr. Walker in their place. In effect, therefore, the applicants obtained the relief which they sought.

11. It might have been expected, therefore, that Mr Walker and Mr Stokoe would have been awarded their costs against those who had resisted the relief sought in the summons (Mr. Whicker and Mr. Beighton); and, in the ordinary way, it might have been expected that those costs would have been assessed on the standard basis and paid out of the assets of the Master Fund: on the basis that, unless their conduct in resisting the summons were held by the court to have been unreasonable, Mr. Whicker and Mr. Beighton would be entitled to be reimbursed out of the assets of that fund for costs incurred while acting at its Official Liquidators. But, given that by reason of their removal and replacement under the order of 30 May 2011 it would be the new liquidators (Mr. Stokoe and Mr. Walker) who would have control of the assets of the Master Fund, it would be they who (in practice) made the payments of those costs out of those assets. No doubt it was with that in mind that the summons of the 19th April sought, simply, an order that the costs of the application should be treated as expenses of the liquidation and paid out of the assets of the Master Fund: in other words, an order that the costs of all parties should come out of the Master Fund.

12. The order of 30 May 2011 addressed the question of costs at paragraphs 9 and 10. At paragraph 9 it was ordered that the costs of the former liquidators (Mr. Whicker and Mr.

Beighton) should be paid out of the assets of the Master Fund on an indemnity basis as an expense of the liquidation, but that such costs should not exceed US$25,000 in any event: at paragraph 10 it was ordered that the costs of the successor liquidators, Mr. Stokoe and Mr. Walker be paid out of the assets of the Master Fund on an indemnity basis as an expense of the liquidation, and should be subject to the same cap (limiting those costs, also, to US$25,000 in any event.

13. It is not surprising that Mr. Whicker and Mr. Beighton should have been awarded their costs out of the Master Fund on an indemnity basis, having regard to provisions of O.62 r.6(2) of the Grand Court Rules. As I have said, they would be entitled to take their costs out of their fund unless their conduct had been found to be unreasonable. No issue arises on this appeal in relation to the costs of Mr. Whicker and Mr. Beighton; in particular, they have not challenged the cap which the judge imposed on their costs.

14. To the extent that Mr Stokoe and Mr Walker do not recover their costs of the summons form Mr Whicker and Mr Beighton – or out of the assets of the Master Fund – they would, *prima facie* at least, be entitled to be reimbursed in respect of those costs out of the assets of the Offshore Fund, as Official Liquidators of which they were successful as applicants under that summons. GCR O.62 r.6 so provides. The order of 30 May 2011 does not, as it seems to me, have the effect of depriving Mr. Stokoe and Mr. Walker of the right which they would otherwise have under O.62, r.6 to have so much of their costs as were not payable out of the assets of the Master Fund – in particular, the amount (if any) by which those costs exceeds US$25,000 - paid out of the assets of the Offshore Fund. I would not expect to find, in that order (which was made in the liquidation of the Master Fund) anything which takes from Mr. Stokoe and Mr. Walker a right which they would otherwise enjoy as liquidators of the Offshore Fund. But we have not been asked to decide that question; and I do not do so.

15. Mr Stokoe and Mr Walker appeal from the cap imposed in paragraph 10 of the order of 30 May 2011 in the circumstances that, even if that paragraph does not have the effect of depriving them of the right to recover their costs from the assets of the Offshore Fund, the cap does have the effect of shifting the burden of the costs which they incurred as

successful applicants (to the extent that the amount of those costs exceeds US$25,000) from the Master Fund to the Offshore Fund. On any basis it is punitive in nature. Some good reason was required to support an order which had that effect.

16. The appeal is brought with the leave of the judge. It said that it is impossible to find any reason, expressed in the judgment, why the judge decided to impose a cap on the costs incurred by the applicants/appellants. But the inference must be that the judge thought that the cap should be imposed to mark his disapproval of what he perceived to have been unreasonable behaviour on the part of Mr Stokoe and Walker the PwC practitioners as liquidators of the Offshore Fund. There are two indications that that was his perception. At paragraph 5.5 of his judgment the judge said this:

> "5.5 If this application had been presented as a hearing of the supervision petition, I would have set aside the ex parte order made on the papers and appointed PwC instead of KPMG. This is the way in which the issue could and should have been resolved."

That echoes an earlier passage. at paragraph 3.8 of his judgment, in which the judge had indicated that it was not necessary for the Offshore Fund, acting by its liquidators, to have issued a removal summons under s. 107 of the Companies Law.

> "It (or any ... interested party) could have fixed a hearing date ([or] sought directions) for the supervision petition to be heard for the purpose of reviewing the ex parte order. With the benefit of hindsight, I think that this would have been an easier, [or] more expeditious, less expensive and less acrimonious way of resolving the issue. In many ways I think it would have been better if the matter had been pursued by the Petitioner, whether by listing the supervision petition for hearing or issuing a removal summons."

The last sentence of that passage is difficult to understand: Mr Stokoe and Mr Walker did, in fact, issue a removal summons: Having succeeded on that summons, they were deprived of part of their costs of doing so.

17. In order to justify imposing the cap in paragraph 10 of his Order of 30 May 2011, it was, as it seems to me, necessary for the judge to conclude:

    (1) That there was an alternative route by which Mr Stokoe and Mr Walker could have sought the removal and replacement of Mr Whicker and Mr Beighton as Official Liquidators of the Master Fund.

(2) That it was unreasonable, at the time that the decision was taken to proceed by summons for removal of Mr Whicker and Mr Beighton under section 107 of the Companies Law, for Mr Stokoe and Mr Walker as liquidators of the Offshore Fund, to take that route rather than the alternative route which the judge thought he had identified.

(3) That, had the matter been pursued by restoration of the supervision petition, then the costs that would have been incurred in pursuing that alternative route would not have exceeded US$25,000. The only basis for imposing that figure as the cap would be that, if the alternative route had been pursued, then it would have been cheaper.

18. Plainly, the judge thought that there was an alternative route to the removal of Mr Whicker and Mr Beighton as Official Liquidators of the Master Fund which "could and should" have been pursued. But it is difficult to find a finding that effect Mr Walker and Mr Stokoe acted unreasonably in choosing, at the time, not to proceed by that route. The judge's finding, at paragraph 3.8 of his judgment, was reached "with the benefit of hindsight". Further, although the judge took the view that, had the supervision petition been restored, he would have set aside the ex parte orders and appointed PwC in the place of KPMG, the restored petition would not, necessarily, have been listed before him. It is a matter of speculation as to what would have happened if the restored petition had been listed before another judge.

19. There is no analysis by the judge in his judgment of the factors which Mr Stokoe and Mr Walker, as Official Liquidators of the Offshore Fund, and their advisers needed to have in mind when deciding, in April 2011, how best to proceed. In particular, there is no consideration of the possibility that if they taken the judge's alternative route, the issue might have come before the court later than it did; and that that would have been a factor (and perhaps a powerful factor) in a determination that the liquidators in office (Mr Whicker and Mr Beighton) should not be removed. The view could well have been taken that the longer Mr Whicker and Mr Beighton remained in office as Official Liquidators of the Master Fund, the less likely it would be that a court would decide to replace them by the applicants. Those were factors which Mr Stokoe and Mr Walker, with those advising

them, had to take into account when deciding how to proceed. As I have said, there is no finding by the judge that Mr Stokoe and Mr Walker acted contrary to advice; and no finding that whatever advice they did receive (which, no doubt, would be privileged) was unreasonable in the circumstances. The judge's observation that, with the benefit of hindsight, it might have been better to proceed by an alternative route does not support a finding that it was unreasonable to proceed by the route chosen.

20. In those circumstances the second of the matters necessary to support a punitive costs order was not established. Nor was it established that proceeding by the judge's alternative route would have been cheaper; in particular, that the costs which would have been incurred by Mr Stokoe and Mr Walker if they had proceeded by that alternative route would not have exceeded US$25,000. It is impossible to identify in the judgment why the judge adopted that figure: it cannot be regarded as other than speculative.

21. There is nothing before us to suggest that the judge was referred - as we have been - to the guidance given in decisions of the Court of Appeal in England and Wales as to the circumstances in which a punitive costs order of the nature imposed in this case can be appropriate: in particular, to the observations in *Straker v Tudor Rose* [2007] EWCA Civ 368 and *SCT Finance v Bolton* [2002] EWCA Civ 56. It is unnecessary to set out those observations: it is sufficient to note that they do emphasise that it is dangerous, and inherently undesirable, for a judge, when deciding what order to make as to costs, to speculate as to what might have happened if a different course had been taken. That, as it seems to me, is the error which led the judge to make the order under appeal. It is for that reason that I would allow this appeal; and direct that the order of 30 May 2011 be varied by the removal from paragraph 10 of the US$25,000 cap.

22. It was submitted on behalf of the appellants that the judge was wrong to take the view that an alternative route - the restoration of the supervision petition - was a route that was available to Mr Stokoe and Mr Walker. It was explained to us that there would have been considerable doubt whether the Offshore Fund (or its Official Liquidators) would have had a right, as a contributory of the Master Fund and not a creditor, to be heard and make their representations on the supervision petition; and further, that there was doubt

whether, on the review of the order already made on the supervision petition, the court would have had power to replace the Official Liquidators already appointed by other liquidators (as distinct from deciding whether they should be confirmed in office). Those points are not without force. They were not addressed by the judge. It is unnecessary for this Court to decide them. The outcome of this appeal does not turn on the question of whether, in fact, there was an alternative route available to Mr Stokoe and Mr Walker; but on the absence of (i) any finding that it was unreasonable for them to pursue that alternative route and (ii) any material to support a cap in the amount of US$25,000. But, in fairness to the arguments that have been addressed to us, I think it right to mention that it is not clear that the judge was correct to think that the alternative route was available to Mr Stokoe and Mr Walker.

Justice Forte, Justice of Appeal:

23. I agree.

Justice Conteh, Justice of Appeal

24. I agree for the reasons given by learned Chadwick P that the judge's order imposing the cap on the liquidators' costs should be set aside.

Chadwick P

Forte JA

Conteh JA