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CILR 2004-2005
Winding up.

IN THE GRAND COURT OF THE CAYMAN ISLANDS
HOLDEN AT GEORGE TOWN, GRAND CAYMAN

CAUSE NO: 282 OF 2004

IN THE MATTER OF THE COMPANIES LAW (2004 REVISION)

AND

IN THE MATTER OF GATX FLIGHTLEASE AIRCRAFT COMPANY LTD.

Appearances: **Mr. Robin Potts, Q.C. instructed by Mr. Mark Holligan of Walkers both for the Applicant**
Mr. Simon Mortimore, Q.C. instructed by Mr. Robin McMillan of Appleby Spurling Hunter both for the Respondent

Before: **Hon. Justice Henderson**

GRAND COURT CAYMAN ISLANDS

Heard: **February 23, 24 & 25, 2005**

JUDGMENT

The Respondent, Flightlease Holdings (Guernsey) Limited ("FHG"), has filed a winding up petition in respect of GATX Flightlease Aircraft Company Limited ("GFAC"). The Applicant, GATX 3rd Aircraft Corporation ("G3AC"), applies to strike the petitioner's points of claim and to dismiss the petition on the grounds that they disclose no reasonable cause of action and are an abuse of process.

Issues

The sole purpose for which FHG seeks the appointment of liquidators is to cause GFAC to commence an action for breach of contract. The members' agreement and the articles of association of GFAC prevent such a course unless both of the two GFAC shareholders (FHG and G3AC) consent. G3AC will not consent. The liquidators, however, will operate under no such constraint. G3AC argues that this amounts to an abuse to the process of the court because the winding up petition is brought solely for the ulterior purpose of circumventing the members' agreement and articles. In addition, G3AC argues that the proposed claim has no reasonable prospect of success.

Facts

FHG is a wholly owned subsidiary of Flightlease AG, a Swiss company, which is itself a wholly owned subsidiary of Sair Group AG ("Swiss Air"). G3AC is a wholly owned subsidiary of GATX Financial Corporation ("GFC") and a part of a group of companies known as the GATX Group.

G3AC and FHG are the only two shareholders of GFAC, a joint venture company established in 1998. GFAC was set up to purchase aircraft. The members' agreement between G3AC and FHG provides that each party is to appoint two directors to the board of GFAC and hold an equal number of shares. The members' agreement and the articles of association of GFAC contain provisions which prevent the board from taking important decisions without the unanimous consent of the director nominees of the two shareholders. It is agreed that these provisions would prevent GFAC from commencing litigation without the unanimous consent of both parties.

GFAC was incorporated in the Cayman Islands to purchase aircraft from Airbus Industrie ("AI"), a major manufacturer of aircraft. Upon its inception, GFAC entered into an agreement with AI for the purchase of a number of airplanes. The purchase agreement required GFAC to make pre-delivery payments ("PDPs") to AI amounting to 20% of the gross price of each aircraft. These payments represented contributions to the construction costs of the aircraft.

GFAC has paid PDPs totalling US $227,637,864.00. There were two aircraft (referred to as nos. 5 and 7) for which FHG was exclusively liable; the sum of US $57,000,000.00 has been paid in respect of these. Aircraft no. 5 was due for delivery in November 2001; FHG was obliged to pay a further US $79,400,000.00 for it at the time of delivery. Aircraft no. 7, due for delivery in December, 2001, imposed upon FHG an obligation to pay a further US $80,200,000.00 at the time of delivery. The balance of the PDPs paid by GFAC has been contributed in equal proportions by the two shareholders, as is required by the members' agreement.

The purchase agreement is governed by the laws of the State of New York. No evidence of foreign law relating to the viability of the proposed lawsuit has been adduced before me. I proceed, therefore, on the footing that the law of the State of New York on this subject is the same as that of the Cayman Islands.

By July, 2001 Swiss Air and FHG were in financial difficulty. G3AC and FHG agreed in principle to unwind the joint venture arrangement and to allocate responsibility to one or the other of the two members for each aircraft which GFAC had committed to purchase from AI. On July 16, 2001 the two shareholders entered into a separation agreement specifying that G3AC would be solely responsible for the purchase of certain aircraft which were scheduled for relatively early delivery and FHG would be solely responsible for the balance. On July 26, 2001 AI agreed in principle to this reallocation of responsibility in accordance with the separation agreement. No amendment was made to the original purchase agreement between AI and GFAC.

On October 4, 2001 G3AC and FHG entered into two agreements which modified, but did not supersede, the earlier separation agreement. These "split agreements" recite that the parties "have previously agreed to dissolve their joint venture …"

On October 1, 2001 the Swiss Air Group announced that it (and FHG's parent) "would file for bankruptcy." GFAC was due to make certain PDPs to AI on that date; it did not do so, and it is evident that it could not. FHG was insolvent and unable to provide GFAC with its 50% share of the required payments.

Both G3AC and FHG understood and agreed that they would negotiate separately with AI for individual agreements to replace the original purchase agreement. G3AC was successful almost immediately. On October 8, 2001 G3AC's parent, GFC, announced that it had reached agreement in principle with AI regarding the aircraft allocated to G3AC. FHG has not succeeded in negotiating its own agreement with AI. Presumably, FHG found itself unable to provide suitable assurances of its ability to make the required payments.

On October 9, 2001, AI, G3AC and GFC entered into an agreement for the purchase of the aircraft allocated to G3AC. G3AC (and its parent) agreed to this clause:

> "1.4 Provided Airbus is not in breach of any of its obligations under this letter, each of GFC and G3AC agrees not to dispute (and agrees not to procure that GFAC dispute) any termination of the GFAC purchase agreement or any retention by Airbus of PDPs paid by GFAC under the GFAC purchase agreement if GFC and Airbus have entered into the GFC purchase agreement in accordance with Section 1.2."

The contract also contained an indemnity from GFC to AI for any liability AI might have to GFAC. The indemnity does not extend to any award of damages to GFAC for a breach of contract by Airbus (see clause 2.3).

The aircraft purchase agreement contains termination provisions. AI was entitled to terminate in the event that GFAC was "unable to pay its debts as they come due" (clause 20.1 (6)). Alternatively, AI could terminate if GFAC failed to make any PDP on the required date; in this instance, a grace period of 15 business days from the date of the notice of non-payment was provided for (clause 20.2). Clauses 20.5.4 and 5.7.3 provided for AI's right to retain all PDPs in the event of a termination of the agreement because of a default by GFAC.

By letter dated October 3, 2001 but delivered on October 8 or 9, AI made demand for the overdue PDPs due on October 1, 2001. The letter also claims that a PDP due on August 1, 2001 remained unpaid; FHG denies that and the evidence is unclear.

On October 11, 2001, well before the expiry of the 15 business days grace period, AI delivered its notice of termination to GFAC and said it would retain all of the PDPs. The letter says:

> "You made it clear in our various conversations in recent days with senior executives of your company and its parent company, following the moratorium on debt enforcement affecting the Sair Group and its Flightlease Division announced last week, that GATX Flightlease Aircraft Company Ltd. no longer intends to fulfil its obligations to purchase the aircraft pursuant to the agreement. This amounts to a repudiation of the agreement by GATX Flightlease Aircraft Company Ltd. and this repudiation, together with your failure to make the pre-delivery payments of US $7,476,669.45 due on October 1, 2001 as described in the notice of non-payment, leave us with no option but to, and we hereby do, cancel and terminate the agreement in full with respect to all remaining undelivered aircraft."

To that, no immediate response was given. Eventually, by letter dated October 31, 2001, Mr. Peter Gysel, a director of GFAC representing FHG on the board, advised AI:

> "We do not accept that Airbus is entitled to terminate the agreement. Airbus has failed to give formal notice of non-payment and has totally ignored the grace periods provided by the agreement. We received a fax on 9th October, 2001 which was dated 3rd October, 2001. GATX Flightlease Aircraft Company Ltd. ("GATX Flightlease") was entitled to a grace period of 15 days from the date of issue of notice. Even if the facsimile had been sent on 3rd October, Airbus was not entitled to terminate until it had given GATX Flightlease 15 days to pay.
>
> <u>We do not consider that a termination would be fair under the circumstances given that we are still willing to continue the agreement</u> and had relied in good faith upon Airbus being willing to do the same

and to work with us in these difficult circumstances." (underlining added)

AI responded to GFAC on November 15, 2001. It said:

> "Our cancellation and termination of the agreement within the 15 day grace period provided by clause 20.2 thereof was justified by your repudiation of the agreement in the days preceding October 11th. Our decision to terminate was legally valid in the circumstances, and has been confirmed by your subsequent failure to pay the outstanding pre-delivery payment of US $7,478,669.48 owed since October 1, 2001 had you intended to cure your default within the original contractual grace period. In any event, the applicable grace period for this payment has expired and we hereby reiterate that the agreement has been cancelled and terminated."

In due course, FHG was placed into voluntary liquidation in Guernsey. Its liquidators have caused FHG to present this winding up petition in relation to GFAC and seek their own appointment as liquidators of it.

GFAC has no liabilities and only one purported asset, its potential claim against AI for wrongful termination of the purchase agreement. FHG argues that, having delivered a demand for payment on October 9, AI could not terminate the agreement until the grace period of 15 business days had expired. The letter of October 11, it says, amounted to a wrongful termination of the contract which entitles GFAC to a return of the PDPs.

Standing

FHG made capital contributions to GFAC from time to time in accordance with clause 4.2.1 of the members' agreement; these constituted a subscription for shares:

clause 4.4. FHG therefore has standing to present this petition as a contributory of the company.

Analysis

If they were in agreement, the directors of GFAC could cause it to initiate an action against AI. The company has no liabilities and no assets except for its potential claim. In this sense, the "need" for a winding up results solely from the fact the quasi-partners are deadlocked – FHG wishes the action to proceed and G3AC does not. The deadlock provisions in the members' agreement and in the articles of association require unanimity before the company can initiate such a lawsuit. Installing the FHG liquidators as liquidators of GFAC would have the effect of rewriting this important aspect of the agreement between the two founders.

I find this aspect of the application troubling. While it may not demonstrate that the process of the court is being abused, it does provide a solid reason for scrutinizing the merits of the proposed law suit with considerable caution. I turn to that now.

The Court will dismiss a contributory's petition unless it is satisfied there will be a substantial surplus of assets available for distribution among the shareholders. The contributory must show that it has a tangible interest in the winding up: *Rica Gold Washing Co. (1879)* 11 Ch. 36; *Deloitte and Touch AG vs. Johnson*

[2000] 1 BCLC 485, 491 (PC). The petitioner must establish to the satisfaction of the Court a probability of surplus assets being returned to the contributory and in which it will share. The asset of substance here is said by FHG to be a claim by GFAC against AI for wrongful termination of the purchase agreement and for the return of the PDPs.

To what standard of cogency must the evidence in support of the claim rise? It is clear that wholly speculative claims will not suffice. A number of decisions say a petitioner must show that there is "likely" to be a surplus: see *Re Othery Construction Ltd. [1966]* 1 All ER 145; *Re Harris Simons Construction Ltd. [1989]* BCLC 202; *Black v. Sumitomo Corp. [2003]* All ER 643 (CA); *Re Diamond Fuel CA. (1879)* 13 Ch. 400 (CA). Other authorities have suggested that there must be a "realistic prospect" of a distribution to the petitioner (*Re Greenhaven Motors Ltd. [1999]* 1 BCLC 635 (CA)) or a "reasonable possibility" of that (*Stocznia Gdanska v. Latreefers (2) [2001]* 2 BCLC 116, 137, 141). There is little real difference in these various formulations.

I must ask whether it is likely that a claim for breach of contract by GFAC against AI would succeed. Does such a claim have a realistic prospect of success? Is there a reasonable possibility of a recovery of the PDPs?

It is hard to escape the conclusion that, by the date of AI's notice of termination (October 11, 2001), GFAC was hopelessly insolvent. It had failed to make the required payments on October 1, 2001.The members' agreement required each of the two members to contribute capital equally to fund the required payments. GFAC's failure was due to the insolvency of FHG and its consequent inability to inject the necessary capital. G3AC had no obligation or intention to make up the deficiency.

Under the purchase agreement, AI was entitled to terminate the contract without any grace period if GFAC was unable to pay its debts as they fell due. Indeed, the separation agreement and the split agreements were put in place, with AI's knowledge and acquiescence, because the parties could foresee that GFAC would default on its obligations.

AI's termination letter of October 11, 2001 does not refer expressly to the insolvency provision in clause 20.1 (6) of the purchase agreement. Instead, it invokes GFAC's "repudiation" of the contract. Given the language (quoted above) in the letter and the factual circumstances in which it was sent, one might be tempted to conclude that AI was also asserting a right to terminate on the ground of GFAC's insolvency, but I do not base my conclusion on that assumption.

I will assume, in FHG's favour, that there could be no valid termination of the agreement by AI until the grace period had expired. On this assumption, AI's attempt to terminate the agreement on October 11 was a wrongful repudiation of the contract. GFAC had two options: it could accept the repudiation and treat the contract as at an end, demanding the return of the PDPs. It did not do that. The other alternative was for GFAC to reaffirm the contract and perform its obligations under it. Mr. Geysel's letter of October 31st adopts this second course.

The result, on this hypothesis, is that AI's unaccepted repudiation has no legal effect. It does not operate to absolve GFAC of the need to tender further performance: *Fircometal v. Mediterranean Shipping Co. [1989]* AC 788 (HL); *Chitty on Contracts*, 29th edition, volume 1, page 1365 ff.

The result is that, once the grace period had expired at the end of October, GFAC was required to perform. The October 1st PDPs were still outstanding. FHG's November payment was now due. A further large payment was due in December. FHG and GFAC were insolvent, and there was no reasonable prospect of any further performance by them.

As at November 15, 2001, the date of the second termination letter, AI was entitled to end the agreement and retain the PDPs either on the ground of GFAC's insolvency or because of its failure (after notice) to satisfy the demand for payment. Either was a good and sufficient reason at that point.

After the argument concluded, the parties agreed to adduce further evidence and argument in writing. In fact, the additional evidence, which concerned the new arrangements made between G3AC, GFC, and AI in October, 2001, contained little novelty. FHG had reviewed these documents well before the hearing of its application and made reference to them during that hearing.

The agreement between counsel was a limited one: it permits me to consider the effect of the new arrangements on the arguments already advanced at the hearing, but does not constitute a mandate to consider new points of argument.

In general, the new arrangements are in terms which all three parties (G3AC, AI and FHG) must have contemplated in July, 2001 when they first agreed in principle to a separation of responsibilities for the various aircraft. FHG takes particular exception to the clause in the new agreement (quoted above) whereby G3AC agrees "not to procure that GFAC dispute" any termination of the GFAC purchase agreement or any retention by AI of the PDPs. This clause, and the indemnity from GFC to AI, strike me as an entirely predictable result of the restructuring of responsibility for the aircraft purchases. It should not have come as any surprise to FHG, which was a party to the July negotiations and agreed to the result. Overall, I am of the view that the fresh evidence concerning the new arrangements has little impact on the conclusion I have reached.

My conclusion is that there is no realistic or reasonable prospect that a claim by GFAC against AI for breach of contract would succeed. There is no likelihood of success.

For these reasons, the application is allowed, the Petitioner's points of claim are struck, and the petition is dismissed.

Dated this 23rd day of June, 2005

Henderson, J.

GRAND COURT CAYMAN ISLANDS

Henderson, J.
Judge of the Grand Court