IN CHAMBERS

17-01-02

IN THE GRAND COURT OF THE CAYMAN ISLANDS
HOLDEN AT GEORGE TOWN, GRAND CAYMAN
CAUSE NO. 5 OF 2002

BETWEEN: THE XEX CONSULTING COMPANY INC.

Plaintiff

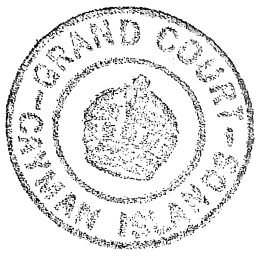
AND:
(1) MYRON GUSHLAK
(2) PRODIGIOUS (GRAND CAYMAN) LTD.
(3) TIARA MARINE LTD.
(4) IMPERIUM CAPITAL INC
(5) TYSON INVETMENTS LTD.

Defendants

Appearances:
Kenneth Farrow for Applicant XEX

Application heard January 7, 2002.

Before Kellock, J. in chambers



Reasons for Judgment

Kellock J.

Mr. Farrow counsel for the Plaintiff, (which I will call "XEX") seeks a Mareva Injunction against all of the Defendants prohibiting them from

removing their assets from the Cayman Islands and from disposing of, dealing with, or diminishing the value of their worldwide assets until judgment has been obtained in the action which provides the context for the Mareva application.

The Action

The action is brought by XEX, a Florida corporation against five defendants which I will refer to as Gushlak, Prodigious, Tiara, Imperium and Tyson. The action was commenced by Writ of Summons issued on January 4, 2002. The Writ has not been served and no Statement of Claim exists as yet. As against Gushlak, XEX seeks a Declaration that he is bound by a written Agreement entitled "Unconditional Guaranty" made between XEX and two guarantors, being Gushlak and one Joseph Quattrochi. This Agreement which I will call "the Guaranty" is in writing and appears to be signed by Quattrochi. It has not been signed by Gushlak. However the material filed in support of the Mareva application alleges that Gushlak orally agreed to sign it.

The Guaranty recites that the guarantors (Gushlak and Guattrochi) will derive substantive benefit from the purchase by XEX of "additional" shares

of a company called Global Net Inc, (the shares of which trade on "the Nasdaq Bulletin Board") and from XEX's Agreement made at the request of the guarantors to refrain from selling approximately 244,000 Global Net shares previously acquired by XEX in various open market transactions for a total purchase price of approximately $3,000,000.00 (which I assume means $3,000,000 U.S.).

The Unconditional Guaranty recites that XEX has sustained a "significant financial loss due to a significant decline in the market price" of Global Net shares during "the period of forbearance" i.e. the period of time between XEX's acquisition of approximately 244,000 Global Net shares and the date of the Guaranty which is November ------- 2000.

The Guaranty also recites that XEX has, by an Agreement of even date agreed to acquire from one Howard Appel the additional Global Net shares referred to above. The Guaranty further recites that Appel has represented, warranted and covenanted to XEX that, inter alia, the (Global Net) shares will accrue a value of at least $3,750,000 within the ... 270 day period immediately following the date of the Purchase Agreement. Gushlak and Quottrochi guaranteed that "XEX will be able to sell (all of XEX's Global

Net shares i.e. the shares, previously acquired and the shares being acquired from Appel) in the open market for an aggregate amount equal to or greater than $3,750,000.00 within .... 270 days of the closing date (as defined in the Agreement with Appel).

The Agreement between XEX and Appel which is called "Stock Purchase and Sale Agreement" is said to have been entered into on November 20, 2000 and calls for the sale by Appel to XEX of 560,000 Global Net shares at a price of US$750,000.00. It therefore appears that XEX paid something in excess of US$12.00 per share for the initial purchases of approximately 244,000 Global Net shares and the Agreement with Appel called for a price of US$1.33 per share.

Assuming that XEX's total holding of Global Net shares would be 804,000 (244,000 plus 560,000) the guaranteed price was approximately US$4.66 per share.

The affidavits of Sal Romano (hereinafter "Romano") and Quattrochi state that the initial XEX purchase of Global Net shares was 250,000 shares (not 244,000) at a price of $12.00 per share. If XEX's total holding was 810,000

shares (560.000 plus 250,000) then the guaranteed price would be $4.62 per share.

The material indicates that the guaranty period expired August 17, 2001 which would make the effective date of the Appel sale and the Guaranty November 20, 2000.

It is apparent that XEX's claim is that, contrary to the assurances provided by the Guaranty (and by Appel in the Stock Purchase and Sale Agreement) Global Net could not dispose of its Global Net shares at the guaranteed price at any time between November 20, 2000 and August 17, 2001.

The Guaranty provides that in those circumstances the "guarantors shall immediately pay ... to XEX in immediately available funds a sum equal to the difference between (the guaranteed price) and the actual aggregate sales price for the shares".

The Guaranty does not specify the date for determination of the shortfall which is the agreed measure of the guarantors' liability.

In addition to the claim made by XEX for a Declaration XEX also seeks judgment against Gushlak for US$3,277,485.00 pursuant to the terms of the Guaranty. That amount appears in paragraph 7 of the affidavit of Robert Klein (hereinafter "Klein") the Chief Financial Officer of XEX which I will come to in due course.

As against the Defendants other than Gushlak, XEX claims Declarations that Gushlak is the sole beneficial owner of those corporations or their assets. In particular XEX claims Declarations that Gushlak is the sole beneficial owner of Prodigious or property at 222 Old Prospect Road, Prospect, Grand Cayman, of Tiara or the motor vessel known as "Prodigious" which is alleged to be moored at Magellan Quay, Governor's Harbour, and of Imperium and Tyson or their assets. No other specific relief is claimed in the Writ other than interest and costs.

The Application

The requirements to be met in order to obtain a Mareva Injunction have been rather fully developed since the decision of the English Court of Appeal in *Mareva Compania Naviera SA v. International BulkCarriers SA (1980) 1 All. E.R. 213* and ought to be well-known to all who labour at the Bar.

Similarly the requirements of the Law with respect to the form of affidavits to be used on interlocutory applications and the obligations to the court of those who seek ex parte orders should also be well-known as well.

However it appears to be necessary to set them out again in order to properly analyse the merits of this ex parte application and for the assistance of those who may in future be called upon to consider launching similar applications.

1. Before seeking an Ex parte Mareva Injunction a party must understand that the Law requires an applicant to proceed "with the highest good faith". It is imperative that the applicant make full and frank disclosure of all matters in his knowledge which are material for the judge to know. *(The Supreme Court Practice 1999 page 541-542, Third Chandris Corporation v. Unimarine S.A. 1979 QB 645 at 668* per Lord Denning MR).

   This means that the applicant must make proper inquiries before making the application. The applicant must identify the crucial points for and against the application. That includes identifying any defences to the action or the application that could reasonably be

taken by the defendant if present at the hearing of the application (See *Siporex Trade S.A. v. Comdel Commodities Ltd (1986) 2 Lloyd's Rep. 428 at 437 and Gee, Mareva Injunctions and Anton Pillar Relief 4th Edition (1998).*

Reference is made in Gee to the Practice Direction to be found in (1983) 1 WLR 433 at 434 which provides in part as follows:

> The affidavit in support (of applications for injunctions) should contain a clear and concise statement:
>
> (a) of the facts giving rise to the claim against the defendant in the proceedings;
>
> (b) of the facts giving rise to the claim for interlocutory relief;
>
> (c) of the facts relied on as justifying the application ex parte, including details of any notice given to the defendant or, if none has been given, the reasons for giving none;
>
> (d) of any answer asserted by the defendant (or which he is thought likely to assert) either to the claim in the action or to the claim for interlocutory relief;
>
> (e) of any facts known to the applicant which might lead the court not to grant relief ex parte;
>
> (f) of the precise relief sought.

(See supra at p. 122)

If these rules are not observed the applicant may be deprived of any advantage he may have derived from the making of an ex parte order. (Gee pages 139 – 140).

2. The material filed in support of an ex parte application for a Mareva Injunction must show that the applicant (the Plaintiff XEX in this case) has a good arguable case for the relief sought in the action.

3. The material filed must also show a real risk that the judgment sought may go unsatisfied if a Mareva Injunction is not granted. (Gee pages 183-199). The Plaintiff must adduce 'solid evidence' to support that conclusion. Mere unsupported statements to the effect that the deponent to an affidavit fears that assets may be dissipated do not satisfy the laws' requirements. (Gee page 197).

These requirements have been and remain applicable to proceedings in the Grand Court *C Corporation v. P et al (1994-95) CILR 189.*

The Evidence

The Application before me is supported by the affidavits of Romano, Appel Quattrochi, Amelia Boss and Klein and XEX relies on this evidence in order to satisfy the conditions precedent to the granting of the order sought.

The Romano Affidavit

Romano resides in New York state. He says that he is a businessman and investor. No details of his business or investing activities are given. He says that he has known Gushlak for 2 years and has had business dealings with him which includes "transactions in the stock of Global Net Inc." No details whatever are provided.

Romano then says that Global Net became a public company in May 2000 but his explanation as to how that was accomplished is unintelligible. Romano goes on to say that Gushlak was able to acquire 45% of "the public float" of a company called Rich Earth Inc., a subsidiary of which merged with Global Net and as a result acquired "45 per cent of the public float of Global Net" in or about September 2000. This evidence is also unintelligible. It appears to be based on numerous meetings and telephone conversations with Gushlak.

Paragraph 7 of his affidavit states the following:

> *"Beginning in or about March 1, 2000 Norton Herrick ("Mr Herrick") was induced by Mr. Gushlak, a director of GlobalNet, and Robert Donohue, Chairman of GlobalNet, in telephone conversations during which I was present, to purchase 250,000 shares of GlobalNet common stock for over $3,000,000.00 or $12.00 per share, in the name of an entity controlled by Mr. Herrick."*

The Romano affidavit goes on to say that in an unstated number of what seem to be conference telephone conversations between Herrick, Gushlak and Robert Donahue (the sometime president of Global Net), Gushlak or Donahue made a number of false statements about the financial health and prospects of Global Net for the purpose of inducing Herrick to purchase and then hold Global Net shares. According to Romano the purpose of these misrepresentations was to inflate the market price of Global Net stock so Gushlak could sell his own Global Net shares at such prices.

Romano swears that Herrick was in fact induced to by these misrepresentations to buy 200,000 shares of Global Net and Gushlak in fact sold his own shares at inflated prices. How Romano would know that is not

stated. Thereafter the market price for Global Net shares declined dramatically and Mr. Herrick was left holding essentially worthless stock.

Romano's affidavit appears to be based entirely on his personal knowledge except for the content of paragraph 4 which is as follows:

> *"Upon information and belief, on or about March 10, 2000 prior to the merger, Mr. Gushlak and certain of his nominees caused the GlobalNet stock certificates of Rich Earth's public shareholders, representing at least 45 percent of the public float, to be issued to a brokerage account held in the name of Bank Sal Oppenheim Jr $CE ("BSC").*

The source of this information is not identified. There is no reference in the Romano affidavit to the XEX/Appel Agreement or the Guaranty.

No information is provided as to how many Global Net shares Gushlak disposed of at inflated prices or when such dispositions were made.

The Quottrochi Affidavit

Quattrochi also lives in the state of New York and has been as stock broker and investment Banker for 14 years. He too has known Gushlak for two

years, has had business dealings with him including transactions in Global Net stock and held numerous meetings with Gushlak "regarding his efforts to obtain a controlling interest in Global Net".

His account of the circumstances which led to Global Net to become a public company and Gushlak's acquisition of 45 percent of the public float of Global Net is identical to Romano's account. Quattrochi then swears that he participated in conference telephone conversations between Gushlak, Donahue and Herrick in which Gushlak made false representations to Herrick which induced Herrick to buy and hold 250,000 shares of Global Net stock. Quattrochi says that these purchases were made through an account at silver Capital Group and that Quattrochi was a broker at Silver Capital and acted as the broker for those purchases.

Quattrochi does not mention Romano anywhere in his affidavit and Romano does not mention Quattrochi in his, despite the fact that the two affidavits contain many paragraphs in exactly the same language. The telephone conference calls each witness deposes to, seem to have occurred in the same time frame.

Quattrochi does not mention the Appel/XEX purchase agreement or the Guaranty which he is a party to, and which he executed thereby exposing himself to potential personal liability of $3,750,000.00. As in the case of Romano's affidavit the basis for Quattrochi's knowledge of some of the facts disposed to can only be surmised. I must say that I am particularly concerned by Quattrochi's failure to mention the Guaranty.

The Appel Affidavit

Appel does not provide any information whatever as to where he lives or what he does for a living (if anything). Appel does state that he entered into the stock purchase agreement with XEX in order to sell 560,000 Global Net shares which he says "were all beneficially owned by Myron Gushlak". Appel swears that he participated in a telephone conference call with Gushlak, Romano, Quatrochi and two representatives of XEX, Herrick and Klein on November 7, 2000. Appel swears that Gushlak "unequivocally agreed" to execute the Guaranty (having read a copy of it), when he returned from a business trip.

Appel goes on to state that he believes that Gushlak is the "beneficial owner or has an interest in" the yacht Prodigious and Imperium. No basis for that belief is stated.

The Klein Affidavit

Klein is the CFO of XEX. The stock purchase and the Guaranty are identified and exhibited to his affidavit. As Mr. Farrow relied in particular on paragraphs 4 and 7 of this affidavit I will set them out here.

4. *On or about 7 November 2000, I was present during a telephone conversation with, among others, Norton Herrick, a director and principal shareholder of XEX, Mr. Appel, Mr. Romano, Mr. Gushlak and Mr. Quattrochi in which Mr. Gushlak unequivocally agreed to execute the Guaranty. It was made clear during this and other conversations that XEX would not enter the Agreement until Mr. Gushlak agreed to execute the Guaranty. Mr. Gushlak stated that he had received a copy of the draft Guaranty, had accepted the contents and would execute it promptly upon his return from a business trip. He urged XEX to complete the Agreement immediately.*

7. *Of the total of approximately 804,000 shares covered by the Guaranty, 102,000 were sold in November/December 2000 at an aggregate price of US$469,190.12 and a further 1,000 were sold on 5 February 2001 at an aggregate price of US$3,324.88. The aggregate value of the remaining 701,000 shares as at 15 August 2000 although nominally US$350,500 was effectively nil since, given the then volume of activity in this stock, it would have been impossible to place a holding of that size. Accordingly, the amount due under the Guaranty is US$3,277,485.*

Klein goes on to swear that Gushlak resides at 222 Old Prospect Road and that the registered owner of that property is Prodigious. This property is apparently charged to the Royal Bank of Canada as security for a Demand Loan of $2,606,000.00. The charge is dated December 12, 2000. How Klein, the CFO of a Florida company knows where Gushlak resides is not stated.

Klein then swears that Gushlak is the beneficial owner or has an interest in Imperium and Tyson. The basis for that conclusion is not stated.

As I have said the Writ of Summons does not contain any claim against Gushlak based on the misrepresentations desposed to by Romano and Quattrochi.

Mr. Farrow advised me that he was not relying on the evidence of misrepresentations for any purpose other than to establish or help establish that there was a risk that Gushlak might remove his assets from the Cayman Islands or diminish those or other assets in some way.

The Affidavits of Boss

Boss is a professor of law at Temple University in Philadelphia. She is of the opinion that a Pennsylvania court would find Gushlak liable on his oral promise to execute the Guaranty despite the requirement that such agreements are to be made in writing.

The Guaranty provides that it is to be governed by Pennsylvania law. I must assume that XEX regards the question as to Gushlak's liability on his oral promise as a matter to be decided under Pennsylvania law as well.

A Good Arguable Case

I have no reason to question let alone reject the Boss evidence but that does not automatically lead to the conclusion that XEX has established a good arguable case for the relief it seeks in this action against Gushlak.

Whether or not XEX purchased 244,000 shares or 250,000 shares of Global Net in early 2000 at a price equal to or above $12.00, it is clear that by November the price obtainable for Global Net shares was significantly less. Indeed, the shares purchased from Appel were priced at $1.33 per share. The Guaranty price was something in excess of $4.60 a share and the

guarantors' obligations under the Guaranty would have been discharged if the market price reached or exceeded the Guaranty price at any moment in time between November 20, 2000 and August 17, 2001.

I must assume that information as to the market prices for shares traded through the facilities of Nasdaq would be available from a multiplicity of sources on a daily basis. I have not been provided with any such data whatsoever. Klein says that XEX sold 103,000 Global Net shares for an average price of $4.58 a share (by my calculation), between November 2000 and February 5, 2001. 1002 shares were sold for 469,190.12 or $4.59 per share. 1000 shares were sold on February 5, 2001 for $3324.88 or $3.32 per share. Klein swears that the market value of 701,000 shares was $350,000.00 as at August 15, 2000 or $0.5 per share.

I could assume that the guaranteed price was not achieved during the Guaranty period but the court should not be required to speculate or assume that this is so. It seems that the damages claimed in the Writ which paragraph 7 of Klein's affidavit purports to explain, are in reality calculated as follows.

It is first assumed that the 804,000 Global Net shares which were orginally subject to the Guaranty are worthless as of January 2002 and accordingly XEX is entitled to damages in the amount of $3,746,640.00 less the amounts realized by the sales made in November/December 2000 and February 2001, i.e. $472,515.00 ($469,190.12 plus $3324.88). That is $3,274,125.00 not $3,277,485.00 as Klein states.

I would have thought that by selling 103,000 shares of Global Net prior to August 17th, 2001, at prices less than the guaranteed price the Guaranty no longer extended to those shares. Accordingly, even if the market value of Global Net Shares was nil as at August 17th, 2001, the guarantors were only required to pay XEX $707,000.00 X $4.66 or $3,266,660.00.

The problem is that XEX still holds 707,000 Global Net shares and there is no evidence as to what the market for those shares might be. The material does not indicate that the shares no longer trade or have been de-listed. There is no evidence as to whether Global Net still exists or what its prospects might now be. There is no evidence as to whether XEX now controls Global Net and might be in a position to obtain a control premium.

While I might conclude that XEX has a good cause of action under Pennsylvania law for some amount, I must make assumptions in order to place a value on that cause of action.

The Risk of Dissipation

Mr. Farrow conceded that the he was obliged to show that Gushlak had assets in the Cayman Islands and that there was a risk that those assets might be removed.

I was asked to come to those conclusions on the basis of the evidence I have described.

Again I can surmise that the Royal Bank of Canada would be unlikely to make an ordinary residential mortgage loan equal to or in excess of the value of the security of the real property charged. However, the loan for which the Prospect Road property is charged may or may not be a conventional residential mortgage. Residential mortgages are not usually payable on demand. For all I know this property has been charged as security for a line of credit and the obligations for which the charge was given far exceed the value of the property.

Similarly, if the loan is payable on demand the bank might seek immediate payment as soon as it learned of this litigation and that could lead to a forced sale producing an amount which would be insufficient to cover the indebtedness. There can be no question that XEX armed with the information provided to me could have quite easily undertaken some inquiries as to who in fact lives in the Prospect Road house and who in fact makes use of Prodigious. Those inquiries could have been made and the necessary information obtained without alarming Gushlak.

There does not appear to have been any contact by any of the witnesses with Gushlak since November, 2000. That seems to me to be unlikely and it requires explanation. If there were such contacts they ought to have been disclosed and it would be surprising if those contacts did not yield some additional information of relevance to this application and therefore of interest to the Court.

At the conclusion of Mr. Farrow's submissions I indicated that I would not consider granting the injunction sought without the posting of security for

the undertakings XEX is required to give as to the damages the defendants might suffer.

I also indicated that if I were to make an order it would be for a very short period of time. A period of time sufficient only to allow for service of the necessary papers on the defendants and sufficient to allow the defendants to properly instruct counsel in order to put the Defendants' case to the Court.

I indicated that I had a letter of credit for $1 million U.S. in mind by way of security. Mr. Farrow advised that he would need to get instructions. He has now told me that XEX will not provide this security.

Consequently, the fate of this application has been determined. I have however, carefully reviewed the record since the oral argument in the light of Mr. Farrow's submissions and I will set forth my conclusions now;

> I do not believe that I have been provided with full and frank disclosure. The material before me is exceedingly weak in terms of meeting the essential pre-conditions which must be met in order to establish a case for Mareva relief, even if I were to ignore the many

troubling questions which are raised but not answered. These questions include the following;

1) Why was an attempt made to establish that the initial purchases of Global Net stock by Herrick/XEX were induced by fraudulent misrepresentations?

2) Why, if the Court is being asked to rely on the affidavits of Romano and Quattrochi to establish these misrepresentations, do the recitals in the Guaranty contradict their evidence as to the number of shares purchased and the identity of the seller of those shares. Both Romano and Quattrochi swear that they participated in telephone conversations in which Herrick agreed to purchase 250,000 Global Net shares implying that Gushlak was the seller of those shares?

   The recitals in the Guaranty put the number of shares at 244,000. That number is confirmed by Klein the CFO of the purchaser XEX. The recital in the Guaranty indicates that XEX acquired those shares, "in various open market transactions." No affidavit sworn by Herrick was provided and rather than complaining about the drop in value of Global Net shares from approximately $12.00 U.S. at the time the initial purchases were made to $1.33 U.S. per share by November 2000, Henrick/XEX agree to buy 560,000 more shares.

3) Why did counsel for XEX disclaim any reliance on these alleged misrepresentations as a basis for substantive relief in the action? I take the following from page 320 of the 1999 White Book . "It is the duty of counsel not to enter a plea of fraud on the record" unless he has clear and sufficient evidence to support it (See Lord Denning *in Associated Leisure Ltd. v Associated Newspapers Ltd. (1970) 2 QB 450 at 456).*

4) Why do the affidavits of Romano and Quattrochi provide essentially the same evidence concerning statements made by Gushlak in conference telephone conversations, but neither identifies the other as a participant in those conversations?

5) Why do the Romano and Quattrochi affidavits fail to state how and why these gentlemen became involved with Gushlak and exactly what their relationship to each other and to Gushlak was?

6) Why is there no mention in Quattrochi's affidavit of the Guaranty or why he signed it?

7) Why were no proceedings instituted or claims made against Appel or Quattrochi?

8) Why did XEX wait until January 2002 to institute this proceeding?

9) Why was Appel the seller of the 560,000 shares and if the shares were registered in his name why was that the case?

10) Why did XEX sell 103,000 Global Net shares for less than the Guaranty price before the expiration of the guaranty period?

11) Why were the requirements for affidavit evidence based on information and belief all but ignored?

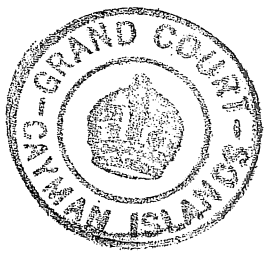
12) If the proper inquiries were undertaken but further information concerning Goshlak's assets could not be obtained, why does the material not disclose the nature, extent and timing of those inquiries?

It is to be expected that affidavits will be prepared by lawyers. It follows that the Court can expect that those affidavits will be prepared in the light of the relevant requirements of the law. I believe that the Court is in addition entitled to expect that the affidavit evidence will provide a reasonably clear

statement of the relevant and material facts. The affidavits of Romano and Quattrochi contain statements which are unintelligible (See paragraphs 3, 4 and 5 of those affidavits.)

I have now concluded that it would be inappropriate to make the order sought or grant Mareva relief in any form even if XEX had been prepared to provide the security I indicated was necessary. Based on Mr. Farrow's advice I understand that the security suggested was not offered, but that was not because XEX lacked the necessary financial resources. In other words XEX has the means but simply does not wish to incur the cost or the exposure to liability that the posting of security and the making of the required undertakings would involve. That speaks volumes as to the real merits of this application.

The application is therefore dismissed.



Kellock, J. (Actg)
Judge of the Grand Court

Dated 17th January, 2002