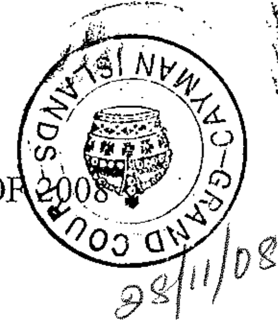
IN THE GRAND COURT OF THE CAYMAN ISLANDS



CAUSE NO: 276 OF 2008

28/11/08

IN THE MATTER OF THE COMPANIES LAW (2007 REVISION)

AND IN THE MATTER OF STRATEGIC TURNAROUND MASTER PARTNERSHIP LTD.

BETWEEN:	**STRATEGIC TURNAROUND MASTER PARTNERSHIP LTD**	**APPLICANT**
AND:	**CULROSS GLOBAL LTD.**	**RESPONDENT**

Coram: The Honourable Chief Justice Smellie

Appearances: **Mr. Anthony Akiwumi and Mr. Richard Annette (joined on the 28.10.08 by Mr. Dennis Brady) of Stuart Walker Hersant for the Applicant.**

Mr. Ross McDonough and Mr. Guy Manning of Campbells for the Respondent.

Heard on: 26th August, 4th September, and 28-29th October 2008

RULING

1. This is an application by Strategic Turnaround Master Partnership Ltd. ("the Company") for the striking out of a petition filed by Culross Global Limited ("Culross") for its winding up.

2. Culross filed its petition as an investor who claims to have redeemed its investments in the Company and now claims to stand in the position of a creditor of the Company.

3. The Company is an exempted limited liability company incorporated under the Companies Law of the Cayman Islands (now the 2007 Revision and hereinafter the "Companies Law").

4. The Company is also a regulated mutual fund pursuant to the Mutual Funds Law and as such is registered with the Monetary Authority of the Cayman Islands ("CIMA") under section 4(3) of that Law.

5. A requirement of its registration is that investments in the Company are made available only to experienced and sophisticated investors and pursuant to the Mutual Funds Law, there is a prescribed minimum equity investment of 50,000 United States dollars.

6. The Company's assets are substantially invested in a "master-feeder" fund structure in Strategic Turnaround Equity Partners L.P. (Cayman) ("the Master Fund"); an exempted limited liability partnership also formed under the laws of the Cayman Islands.

7. In addition, Strategic Turnaround Equity Partners L.P. (the "On-Shore feeder"), a limited partnership organised under the laws of the State of Delaware, the United States, also invests substantially all of its assets in the Master Fund and acts as the On-shore feeder for the Master Fund. Investors subscribe for shares in either the Company or the On-shore Feeder.

8. Culross as an investor in the Company, is thus indirectly an investor in the Master Fund as well.

9. The Feeder structure comprises an open-ended investment vehicle in which investors subscribe for shares and from which investments are redeemable at any time, by redemption notices being given to the respective feeder fund. This in the case of the Company, is effected by notice being given in keeping with the Articles and subject to the rights of the Company under the Articles and other constitutional documents, to suspend redemptions.

10. As a matter of Cayman Islands law, redemptions are permissible by virtue of section 37 of the Companies Law by which companies are allowed, in certain circumstances, to redeem or buy back their shares.

11. This case has arisen because Culross having given notice of redemption, but not having been paid for its redemption proceeds in circumstances to be described below, has filed its petition to wind up the Company claiming as a creditor on grounds under section 94 of the Companies Law, that the Company is unable to pay its debts as they fall due. The alternative ground for the petition under the same section of the Companies Law, is that it is just and equitable that the Company be wound up.

12. The Company now applies to strike out the petition on grounds that Culross has no standing to bring it and that it is an abuse of the process of the Court.

13. That change in its status from shareholder to creditor that Culross claims, is said to have come about in the following way which is disputed by the Company and which, as a matter of the construction of the constitutional documents of the Company, arises for assessment now in the context of this strike out application.

14. In May 2007, Culross through it custodian's nominee, Banco Nominees (Isle of Man) Limited ("Banco"), completed subscription for shares in the Company for which it paid a total sum of

USD1,840,000.00. By virtue of section 38 of the Companies Law, Culross was then deemed to have agreed to become a member bound by the Memorandum and Articles of Association, having subscribed to those constitutional documents of the Company.

15. On 31st October 2007, Culross in keeping with Article 31, gave notice of its intention to redeem all its shares in the Company. This notice was expressed as being due to the negative view Culross had taken of the United States markets in which the Master Fund was selectively invested in the "micro-cap" sector (traded companies with a market capitalisation of between USD50 million and USD250 million) and in the "small-cap" sector (those traded companies with capitalisation between USD250 million and USD 1 billion).

16. Pursuant to Article 31, the redemption notice was required to be served at least sixty (60) business days prior to the effective redemption date.

17. This would have resulted in a redemption date of 1st February 2008 but, as such dates are set to be at the end of each quarter, the next redemption date was identified as 31 March 2008. This was

confirmed to be the effective redemption date by an additional notice sent on behalf of Culross on 11th March 2008.

18. Further, as the Company needed time to ascertain the net asset values ("NAV's") or price at which shares were to be redeemed, the payment date was provided to be 30 days after the redemption date.

19. In this regard the Confidential Explanatory Memorandum (ie: the offering memorandum) of the Company ("the CEM") provides (at page 18):

> "Payments upon Redemption. Payment of the Redemption Price will be made as soon as practicable but, except in cases otherwise described herein, a shareholder who is making a redemption will receive at least 90% of the Redemption Price no later than 30 days following the date of redemption" (emphasis supplied).

20. Accordingly, 90% of the redemption price was due to be paid no later than 30 days following the redemption date; that is: no later than 30 April 2008 except in cases where payment may be denied in keeping with the Articles and CEM itself (as the words in emphasis suggest).

21. Mr. Gary Herman, a director of the Company and managing member of its investment advisor GCM Administrative Services, LLC, confirmed that payment would be made no later than 30th April 2008

in an e-mail sent on 24th March 2008 to Mr. Nigel Blanshard, a director of Culross, in which Herman stated:

> "We confirm your email below that we are in receipt of your redemption request for March 31, 2008. You will receive at least 90% of the cash by the end of April 2008 as per the offering memorandum. In addition, we have agreed to waive the early redemption penalties for this redemption.
>
> Thanks for your patience".

22. Further, on 11th April 2008, the Company's Administrator – Citi Hedge Fund Services (Cayman) Ltd. ("Citi") – sent an e-mail to Banco stating that:

> "Dear Investor
>
> Please find attached your initial confirmation for the full redemptions from the … fund….
>
> Kindly also be advised that these full redemptions are approved for March 31, 2008 and the fund [ie: the Company] also confirms the following:
>
> - That these redemptions are free of fees
> - 90% of the redemption proceeds will be paid within 30 days
> - Balance to follow upon completion of the annual audit."

23. Events then took a different course and that which ultimately led to the filing of this petition without further warning by Culross.

24. It is most convenient that I describe the events by adoption of the chronology which was helpfully prepared and agreed by both counsel in this matter.

25. On 17th April 2008, the directors of the Company held a meeting at which they resolved (among other things) to "suspend all redemptions at this time and that such action is in the best interests of the Company".

26. The directors expressly relied on the powers stipulated in Articles 55 and 56 of the Company's Articles of Association and which will be examined below.

27. The minutes of that meeting, which set out the discussion among the directors, seek to address any concerns that the decision to suspend redemptions was not taken in the best interests of the members of the Company as a whole. Indeed, no express allegation to the contrary as to the bona fides of the directors at that moment in time has been raised by Culross in these proceedings. Concerns have however, been raised about the validity of the powers exercised by the directors

as they purport to have suspended, not only redemptions, but payments as well. The minutes reveal as follows:

> "Discussion
>
> The directors reviewed the current holdings of the Fund in detail and each position was discussed and reviewed. All of the directors had the opportunity to ask questions regarding the company's portfolio of investments. It was discussed and unanimously concluded that the U.S. micro-cap turnaround sector, which is the primary investment sector for the Fund, is extremely volatile and illiquid at this time.
>
> The directors discussed the high likelihood of negative ramifications if any redemption by shareholders of the company were permitted.
>
> The directors confirmed that they each reviewed or informed themselves of the contents of all the relevant documents and that they had each satisfied themselves that there was a clear corporate benefit and in the best interests of the company and its shareholders to suspend redemptions".

28. On 22 April 2008, the directors of the Company passed the further following written resolutions:

1. It is in the best interests of the company and all the shareholders in the company that, in accordance with the Articles the calculation of the net asset value of shares be suspended ("the suspension").

2. No shares in the company be redeemed nor new shares issued until such time as the directors have lifted the suspension;

3. All notices of redemption received by the company be suspended until such time as the directors have lifted the suspension…."

29. On 23 April 2008, the Company's attorneys notified the CIMA by letter that redemptions from the Company were suspended on 22 April 2008.

30. On 28 April 2008, the Company gives notice to its shareholders that redemptions have been suspended.

31. On 30 April 2008, the NAVs of the Company as at 31 March 2008 was determined. As at this date the total number of requests for redemptions, including Culross', represented 27.27% of the assets.

32. And, finally in the chronology for present purposes, on 1 May 2008, Mr. Keen on behalf of Culross sends an e-mail to Mr. Herman stating:

> "Despite your e-mail and my call to you earlier, you have not made any serious attempt to contact me today.
>
> The Administrator of your fund has given us an undertaking that our redemption notice had been received in good order and accepted and has committed in writing to pay 90% of the proceeds

due within 30 days of the effective date of the notice. Today the Administrator is in breach of that commitment. This is a very serious lapse, for which we have been provided with no explanation whatsoever…" (emphasis supplied).

[A threat of legal action then follows in this email].

33. On 14 May 2008, Culross receives notification from the Administrator that the NAV applicable to its shares which it held was, as at 31 March 2008, USD 980,508.97.

34. On 3 June 2008, by unanimous written resolution, the directors of the Company proposed amending the Articles of Association of the Company to permit the calculation of the NAVs of the Company despite the suspension of redemptions; Articles 33.9 and 56 as they then stood, not permitting that to be done. This was eventually carried by special resolution of the shareholders on 25 June 2008. Part of the Company's objection to Culross' petition as voiced by Mr. Akiwumi is that the notification of the NAV of Culross' shares (USD980,508.70) was somehow invalidated by operation of Articles 33.9 and 56 which then – on 14 May 2008 – purported to prohibit the calculation of NAVs during the suspension of redemptions.

35. That argument would however, be no answer to Culross' claim for a debt in that amount if Culross had effectively redeemed its shares on 31 March 2008 and the liability then created, before the suspension was decided upon. This is the central issue taken up in this application, going to the question whether Culross has *locus standi* to petition.

36. As matters transpired, on 10 June 2008, Culross without sending a statutory demand or further letter before action, filed its petition to wind up the Company.

<u>THE ISSUES ARISING</u>

37. Against that background, this application by the Company to strike out the petition for its winding up raises, along with the central issue of standing just identified, a number of other issues.

38. The first of course, is whether the application meets the legal test for the striking out of a petition to wind up.

39. In this regard Mr. McDonough, on behalf of Culross, raised a preliminary issue as to the jurisdiction of the Court.

40. It is that the Grand Court Rules Order 18 Rule 19, which codifies the jurisdiction to strike out on grounds of abuse of the Court's process, does not apply to winding up proceedings.

41. That this is arguable is said to be apparent from GCR Order, Rule 2(5) which provides that the only provisions of the GCR which apply to winding up proceedings (proceedings under Part V of the Companies Law) are Orders 62 (Costs) and 102 (Applications brought pursuant to the Companies Law itself). Thus, an application to strike out under Order 18, Rule 19 would be excluded.

42. Similar concerns were considered by this court in ***RCB v Thai Asia Fund Ltd.*** ***1996 CILR 9, at 28.*** There it was held that the Court's inherent jurisdiction to prevent abuse of its process applies to winding up petitions as it does to the abuse of any other process of the Court.

43. Further, the case law shows that the court possesses a complimentary inherent jurisdiction to stay insolvency proceedings where there is an alternative more appropriate remedy, such that it appears that the petition to wind up is an abuse of the process.

44. In <u>*CVC Opportunity Equity Partners Limited et al v DeMarco*</u> *[2002] UK PC 16; 2002 CILR 77*, on appeal from the Cayman Islands Court of Appeal, the Privy Council on this issue held that:

> ***"The special nature of winding up proceedings and the loss which they may cause the company and its shareholders makes it incumbent on the court to ensure that they are not brought for an improper purpose. In particular, they must not be brought simply to bring pressure on the respondents to yield to the petitioner's demands, however unreasonable, rather than suffer the losses consequent upon the presentation of a petition or the making of a winding up order.***
>
> ***Where the petitioner can achieve his object by other means, therefore, he may be restrained from bringing winding up proceedings.***
>
> ***In Charles Forte Investments Ltd v Amanda [1964] 1 Ch 240, a minority shareholder complained of the board's refusal to register transfers of his shares to a third party. He threatened to present a winding up petition unless the board registered the transfers. He was restrained from presenting a petition.***

> ***The shareholder had other and more suitable remedies available to him, namely an action for rectification of the register or proceedings by way of motion under section 116 of the Companies Act 1948, and his threat to employ the machinery of winding up was an attempt to bring pressure on the board to reverse its decision and an abuse of the process of court".***

45. See also in ***Re A Company*** ***(No. 006685 of 1996) [1997] B.C.C. 830*** (per Chadwick J as he then was) and in this context ***Parmalat Capital Finance Ltd v Food Holdings Ltd*** ***[2008] UK PC 23***, both to be discussed more fully below.

46. ***In Re a Company*** ***(No. 003096 of 1987) (1987) 4 BCC 80*** at page 81 Peter Gibson J. elaborated on the approach that the Court should generally take to deciding upon a strike out application as follows:

> ***"It is trite law that an application to strike out will fail unless it is plain and obvious that the petition will not succeed. If the Court, on a review of the material that has properly been put before it, finds that there are facts in dispute which are or may be material to a determination in the petitioner's favour of the petition, then it must let the petition go to trial.***

On the other hand, if the facts which must be taken to be true or (where evidence is admissible) are established by evidence which is not disputed lead the court to the clear view that the petition is bound to fail, then it would be pointless to allow the petition to go to a hearing and thereby to protract the uncertainty that hangs over the company".

47. It thus appears from the case law that, in summary, the jurisdiction exists to stay or strike out a winding up petition on grounds of abuse of process, such as where the petition raises a disputed claim which might cause irreparable damage to the company, and where there is an alternative more suitable recourse. A petition may also be restrained where it is without merit and patently has no prospect of success.

48. As to the irreparable harm that may be caused, the Company asserts that being an open – ended mutual fund whose affairs are constantly monitored by its sophisticated investors and by others in the market, the mere advertisement of a winding up petition would have a catastrophic impact on its investment portfolio.

49. Culross' response is that it is owed an acknowledged and indisputable debt, being the declared NAV amount of its shares; that is the sum of USD980,508.97. This debt not having been paid, it has the right to petition as any other creditor would.

50. Its claim for an unpaid debt notwithstanding, Culross does not dispute the Company's evidence that it is solvent on the basis of its balance sheet (its assets being more valuable than its liabilities). Culross' position however, is that the Company's failure to pay the indisputable debt owed to it is evidence of its insolvency on the basis of the cash flow test (being able to meet its debts as they fall due) and that a refusal to pay a debt is sufficient to ground a petition even if the company is solvent on a balance sheet basis. Case law cited in support will be considered below.

51. With the foregoing principles and facts in mind, one may now turn to a full examination of the two bases of the Company's objection to the petition.

52. They are as follows:

(i) Culross does not have standing to petition as a creditor. Both Mr. Akiwumi and Mr. McDonough agree that the resolution of

this issue primarily depends on the further question whether Culross had effectively redeemed its shares such that the redemption price (that of USD980, 508.87 notified on 14 May 2008) is to be regarded as a debt owed to Culross in return for its shares - in the context of this mutual fund company - having been bought back by the Company.

These are questions which can be answered only as a matter of the proper construction of the rules of the Company - here primarily the Articles of Association, the C.E. M. and the Subscription Agreement - which govern the arrangement by which shareholders subscribe for shares in the Company.

If Culross is not a creditor in the sense of being owed a provable debt, it can have no standing. Its petition would be without merit and an abuse of the process. Its alternative pleading on just and equitable grounds would also have to be considered in that light.

(ii) Is Culross' petition an abuse of the process of the Court in any event because winding up is not an appropriate remedy to seek

where there is a substantial and bona fide dispute as to whether the debt is owed in the first place?

If the answer to this question is in the affirmative, the petition should be struck on the basis identified above from ***CVC v DeMarco; Parmalat Capital Finance Ltd v Food Holdings Ltd***; and ***In Re a Company (No.003096 of 1987)*** (all above).

THE FIRST QUESTION: Is Culross a creditor?

53. The petition is filed pursuant to section 94(c) and 94(d) of the Companies Law which reads:

> "94. A company may be wound up by the court if –
>
> ...
>
> (c) the company is unable to pay its debts; or
>
> (d) the court is of opinion that it is just and equitable that the company should be wound up".

54. Section 95 goes on to provide that a company shall be deemed to be unable to pay its debts if, (a) a statutory demand for payment of the debt (more than $100) has been served on the company and the debt remains unsatisfied or (b) a judgment debt against the company

remains unsatisfied or (c) it is proved to the satisfaction of the court that the company is unable to pay its debts.

55. In this case no statutory demand was served and so Culross is unable to rely on section 95(a) when not satisfied by payment; which has been held by the courts to create an evidentiary presumption of insolvency. See ***Taylor's International Flooring Ltd v M and H Plant Hire (Manchester) Ltd.*** (more fully discussed below).

56. Nor has Culross obtained a judgment against the Company on which it can claim the debt as contemplated by section 95(b). As matters stand, Culross therefore has no definitive pronouncement of a debt from a Court upon which it relies.

57. This "failing" forms part of Mr. Akiwumi's argument on behalf of the Company, that Culross is obliged to pursue the other more appropriate remedy available to it - rectification of the register of shareholders - in the present circumstances where there is said to be a genuine dispute over the right of the Company to suspend redemptions. Had Culross pursued and succeeded in an action for rectification, it would have obtained a judgment declaring it to be no longer a shareholder but a

creditor owed a debt, presumably, in the amount of the redemption price of its shares. Culross' response will be considered below.

58. As to section 95(c) of the Companies Law, this is the provision on which Culross relies by inviting the Court to infer that the Company's failure to pay the debt - the redemption price which is claimed - is itself proof of the Company's inability to pay its debts as they fall due. The test of solvency in this context being the cash flow test and that which it seems the Companies Law presently requires; not the balance sheet test. And this it is said, is notwithstanding that Culross had not served a statutory demand under S.95 (a) of the Companies Law.

59. Mr. McDonough relies on In the Matter of Oryx Natural Resources 2007 CILR N.6 which decided that on the well established cash flow test of insolvency in this jurisdiction, a company which has failed to pay a proven debt could be wound up even if, on a balance sheet basis, it appears to have unrealised contingent assets.

60. The circuitous nature of that argument is however, readily apparent for if there is a bona fide and substantial dispute over the existence of the debt having regard to the Company's assertion of the right here at

any time to suspend redemptions, there would be no basis on which it could be said that the debt is indisputably owed.

61. It follows that in this case, Culross will not have proper standing to petition if the Company can show that there is a bona fide and substantial dispute over the debt which Culross claims.

THE REDEMPTION PROCESS UNDER THE ARTICLES

62. Despite Culross' claims that its shares were redeemed on the Redemption date (31 March 2008) and that its status thereafter has been that of a creditor and not that of member of the Company, the Company's position is that, as the shares have not been redeemed by actual payment of the redemption price, Culross continues to be a shareholder (with its name still recorded in the Company's Register of members) bound by the rules of the Company. Further, that Culross, as a consequence of the suspension of redemptions, is not owed an actual debt and is no more than a prospective creditor.

63. It follows that I must now turn to examine the directors' asserted powers of suspension.

64. They are prescribed primarily in Articles 32, 33 and 55 of the Articles of Association:

> "32. … If a suspension has been declared by the Directors the right of the Member to have his shares redeemed shall be suspended and during the period of suspension he may withdraw his Redemption Notice…."
>
> "33. Notwithstanding any other provisions of these Articles, the Directors may temporarily suspend redemptions in order to effect orderly liquidation of the Company's assets in relation to shares or if the Directors determine that the disposal of the Company's assets or the calculation of the Net Asset Value in relation to the shares is not practicable or reasonable and that it would prejudice the interests of the Members".
>
> "55. The Directors may, from time to time, in their absolute discretion and for any reason declare a suspension of the determination of the Net Asset Value of shares and the issue and redemption of the shares".

65. It must be noted here that no mention is made in those provisions of the Articles of a power to suspend payments of proceeds of shares which have already been redeemed.

66. Articles 39 and 40 explain the power to liquidate assets for redemption of shares and the transition of a shareholder upon redemption of his shares:

> "39. On a redemption of a Share the Directors shall have the power to divide in specie the whole or any part of the assets of the Company and appropriate such assets in satisfaction or part satisfaction of the Redemption Price and any other sums payable on redemption as provided in these Articles.
>
> 40. Once a share is redeemed the Member shall cease to be entitled to any rights in respect of it (except the right to receive a Dividend which has been declared prior to such redemption). The Member's name shall be removed from the Register of Members in respect of that Share and that Share shall be available for re-issue, and until re-issue shall form part of the authorised and unissued capital of the Company.

67. It is Mr. Akiwumi's argument from the foregoing that "redemption", which is not separately defined in the Articles, is a process which begins with the Redemption Notice but which is not complete unless and until the redemption price is paid; upon which event the redeeming member ceases to have the rights of a shareholder and his

name is removed from the register. This is, of course, contrary to the position taken by Culross by reference in particular to Article 53 which provides:

> "53. The price to be paid for shares which are to be redeemed shall be deemed to be a liability of the Company from the close of business on the Redemption Day [(in this case 31 March 2008)] until the price is paid".

68. This Article is seen by Culross as being pivotal; as creating the debt on which it relies by deeming the redemption price to be a liability of the Company as at the Redemption date (there being no difference for practical purposes between "Redemption Date" and "Redemption Day").

69. This argument is however subject to the practical reality that, as there were no declared NAVs as at the redemption date of 31 March 2008, there was no redemption price ascertained at that time.

70. The suspension of redemptions also operating to suspend the calculation of NAVs is further explained by Article 56:

> "A suspension shall take effect at such times as the Directors shall specify but not later than the close of business on the Business Day next following the

declaration and thereafter there shall be no determination of the Net Asset Value of Shares until the Directors shall declare the suspension at an end. The suspension shall terminate in any event on the day following the first Business day on which the condition giving rise to the suspension shall have ceased to exist, provided that the Directors shall not have declared a Suspension on other grounds. Each declaration of suspension by the Directors shall be consistent with such official rules and regulations, if any, as shall have been promulgated by any authority having jurisdiction over the Company. To the extent not inconsistent with such official rules and regulations, the determination of the Directors shall be conclusive. The Directors shall promptly notify the Members of any such Suspension and shall promptly notify them upon termination of such Suspension".

71. Article 17 gives force to the CEM on which the Company also relies, as follows:

> "Subject to these Articles, Shares shall be issued on the terms referred to in the Confidential Memorandum, unless otherwise determined by the Directors"(emphasis added).

72. And, further as to the efficacy of the CEM, it is acknowledged by Mr. McDonough that it serves the important purpose of explaining to

investors the terms and conditions under which they invest and the risks which they assume when they do so. As to risks, a full seven pages of the CEM (pp 21-28) are dedicated to their identification and explanation.

73. Prominent among these are what are described as "Highly Volatile Markets"; at pages 22-23.

74. Specific provisions of the CEM are repetitive of and thus serve to give further notice of the Articles. These include at page 14 specific reference to the Memorandum and Articles themselves. Other provisions at page 17 stipulate the requirement of 60 days' notice of redemption and identify the last business day of each quarter as redemption days. And at page 18 there is the stipulation that at least 90% of the redemption price will be paid no later than 30 days following the date of redemption.

75. For present purposes, the provision of the CEM which must be most closely examined is that under the heading "Suspension of Redemptions" at page 19:

> "The Board of Directors may declare a suspension of the determination of the Net Asset Value or subscription or

redemption of the shares <u>or the payment of redemption proceeds</u> for the whole or any part of any period when:

(i) any market or exchange on which a substantial part of securities owned by the Fund are traded is closed ...

(ii) there exists any state of affairs which constitute a state of emergency or period of extreme volatility or illiquidity as a result of which (a) disposal of a substantial part of the investments of the Fund would not be reasonably practicable and might seriously prejudice the Shareholders or the Fund or (b) it is not reasonably practicable for the Fund to determine fairly the value of its net assets". (emphasis supplied).

76. Those provisions from page 19 are the provisions of the CEM upon which it is said by the Company that the Directors most immediately relied when they decided to suspend redemptions of shares, having at that time been confronted with the declining markets at the same time as requests to redeem as much as 27.27% of the shares of the Company.

77. Nonetheless, the words above in emphasis from page 19 of the CEM identify the provision upon which the directors must for all practical

purposes be relying (even without having so purported to do) but which, to my mind, creates the real difficulty for the Company here. It speaks of a power of the directors to suspend payments of redemption proceeds, when the Articles themselves go no further than to provide a power to suspend redemptions or to suspend calculations of the NAVs.

78. When confronted with this difficulty – which raises no less than a challenge to the validity of this provision of the CEM and to the vires of the decision of the directors taken implicitly in reliance on it – Mr. Akiwumi responded that the subscribers being all sophisticated investors, including Culross, have agreed to be bound by the CEM as part of the contractual arrangements by which they subscribe. Thus, there is no need for this provision to have been stipulated in the Articles themselves.

79. There are, in this regard, certain provisions of the Subscription Agreement signed by Banco and addressed to the Company which read in relevant part:

"Dear Sirs

The undersigned ("Subscriber") hereby acknowledges receipt of the Confidential Explanatory Memorandum dated May 2006 ("Memorandum"), as amended from time to time, of (the Company) an international business company organised under the laws of the Cayman Islands ("the Company") ....

The subscriber agrees that this subscription is being made and any shares of the Company hereby subscribed for will be held, subject to the terms and conditions of the Memorandum, the Memorandum and Articles of Association of the Company, as amended from time to time, and this Subscription Agreement ...."

80. Thus, it is the position that the relationship between the Company and Culross as subscriber, as to their rights, obligations and remedies, is governed by three inter-connected constitutional/contractual documents:

    (i) The Memorandum and Articles of Association

    (ii) The CEM and

    (iii) The Subscription Agreement.

81. In light of the foregoing provisions of those constitutional/contractual documents and in the absence of any suggestion of bad faith on their part, it is ultimately Mr. Akiwumi's argument here that, at the very least, there is no less than a bona fide and substantial dispute over the

validity of the Directors' decision to suspend. That being so, Culross is obliged to take other action to have that issue first resolved before its standing to petition can be recognised and so the petition, having regard to the principles discussed above, is an abuse of the process and should be struck.

82. Mr. McDonough's response is nonetheless forceful. It is about the timing: that, based on Article 53, once the close of business on the Redemption Date came and went (ie: the 31 March 2008), the redemption price of the shares became a liability of the Company thereby giving to Culross the status of creditor, rather than only of shareholder of the Company.

83. If he is correct, then the purported suspension of redemptions on 17 April 2008 was irrelevant to Culross' position as it had already redeemed on 31 March 2008, leaving only payment to come of what became, as at that date, also pursuant to Article 53, a deemed liability of the Company.

84. Mr. Akiwumi responded that this argument suffers from at least two flaws.

85. The first is that the redemption price of USD980,508.87 was not known or declared until 14 May 2008 and so the liability could not have been fixed in terms of a redemption price as at 31 March 2008.

86. This is only consistent, he said, with the fact that Culross had agreed that no payment was due and payable until fully 30 days after the Redemption Date; that is on 1 May 2008. At that time the NAVs were expected to be available but the suspension of redemptions intervened – and also of NAV calculations -on 17 April 2008.

87. The second is that whatever the deemed liability may be, redemption may not be regarded as having taken place until the price is paid. Only then he submitted, may the shares be regarded as redeemed and the shareholder removed from the Register. Until then he remains a shareholder and bound by the rules of the Company, including those governing suspensions.

88. While from the individual perspective of an investor in an open-ended fund expecting to be able to redeem his investment at any time, this must seem an alarming conclusion; it is one, said Mr. Akiwumi, which is based not only on the constitutional and contractual

arrangements of the Fund by which the investor is deemed to be bound, but upon established case law as well.

89. In this context, it was submitted on behalf of the Company that Culross is in no better position than that which was found by the English Court of Appeal to have been the position of members of building societies in a number of cases which dealt with the standing and priority of members vis-à-vis outside creditors. Before expressing my conclusion and the final reason for not agreeing with Mr. Akiwumi, I believe a close examination of those cases will serve to shed light on this dispute, albeit here arising in relation to a modern mutual fund arrangement.

90. The principles which these cases established have stood the test of time and are continually cited in the leading text books. See for example, Buckley on the Companies Acts, 12th Edition page 450 (citing Re Planet Benefit Building and Investment Society (below) and more recently Palmer's Company's Law 2004; para. 2.1122.1 (citing Pepe's case (below)).

91. ***In Pepe v City and Suburban Permanent Building Society*** ***[1893] 2 Ch 311***, the latest in time of these cases, the court considered the

effect of the alteration of the rules of a building society, after due notice of withdrawal had been given by a fully paid up member. In compliance with the rules, the plaintiff had given 30 days' notice in writing to withdraw/release his shares in the defendant society. However, after receipt of the notice and before the plaintiff was repaid, the rule was amended by giving the directors power to pay off in priority members holding less than GBP50 in the Society. It was acknowledged and accepted by the society that the alteration was to the plaintiff's detriment.

92. The question for the Court was whether the plaintiff was bound by the altered rule. In answering that question in the affirmative Chitty J stated (at page 313):

> ***"Now what is the position of a member of a building society who has given notice of withdrawal? The question cannot be better answered than in the words of Lord Justice Lindley in Sibun v Pearce (1890) LR 44 Ch. D. 354 where he says: The true mode of describing him is to describe him as member who has given notice of withdrawal and is entitled to payment. That definition gets rid of the vague and***

unsatisfactory terms of quasi-member and quasi-creditor.

It has been settled by a series of authorities, that a person in such a position is still a member of the society, and it follows that, under his contract with a society, which has a power to alter its rules, he remains subject to the rules when duly altered. In this case, it is admitted that the rule was duly altered.

The plaintiff's counsel says rightly that, when the plaintiff gave notice of withdrawal he had a vested right to be paid according to the then existing rule; but this does not settle the question, because there existed also against him the power of altering the rule, so that the question assumes this form, that he had a vested right liable to be divested by any later rule duly passed. It may be wondered that the society should have such a power; but it may be also greatly for the benefit of all concerned to make alterations. And I say also, that members place reliance on the sense of justice of the three-fourths majority required to effect the alteration".

93. Here of course, all members are entitled to place reliance on the "sense of justice" of the directors exercising powers bona fide to

suspend redemptions in the best interests of the Company and of all its members as a whole, provided, of course, the directors have the power fully to do what they purport to do.

94. This is an observation also worth making as it goes as well to the public policy point raised by Mr. McDonough, which was that the generally accepted understanding of investors in the Cayman Islands' funds industry is that they expect to be paid when they exercise their rights of redemption.

95. While that is an important expectation, its limits however are to be found at the point where it comes up against that other expectation of the investors taken as a whole, relying on the directors to act, but strictly in keeping with the vires of the rules, in the best interests of the Company.

96. Nor will the Courts interfere with a proper exercise of the directors' fiduciary powers. While on the facts of the particular case holding that the fiduciary power had there been improperly exercised, Lord Wilberforce advised on behalf of the Privy Council in ***Howard Smith v Ampol Petroleum*** *[1974] A.C. 821 at 836* that:

> ***"Directors in whom are vested the right and duty of deciding where the company's interests lie and how they are to be served may be concerned with a wide range of considerations, and their judgment if exercised in good faith and not for irrelevant purposes, is not open for review in the courts".***

97. The ratio in ***Pepe*** (above) - namely the binding effect on a member of a subsequent alteration of an article of association and the continuing binding effect of the Articles on a member despite a preceding notice of withdrawal – rested on the firm foundation of earlier judicial authority not only as shown by the reliance on ***Sibun v Pearce*** (above) but also from other decisions of the Court of Appeal and the House of Lords.

98. As to one of these decided by the Court of Appeal in ***Planet Benefit Building and Investment Society** (1872) LR 14 Eq.441*, Mr. Akiwumi contends that Culross here is in no different position than was the petitioner, Mary Emerson, in that case.

99. The salient facts in that case were as follows:

    (1) The petitioner was a member of a collective investment society which invested in illiquid investments/mortgages;

    (2) In accordance with the Articles governing that Society, she had submitted a Notice of Withdrawal in respect of her investment;

(3) After the Notice of Withdrawal was received, the Directors of the Society amended the Articles so that any member seeking withdrawal was required to:-

   (i) Give 30 days' notice in writing to the Society and on expiry thereof would cease to be a member but would be entitled to receive dividends in respect of her investment shares in the manner subsequently prescribed and, in respect of the balance of her investment, would be paid when the funds of the Society permitted, in such instalments as the directors determined;

   (ii) Until the income of the Society was available for that purpose, no payment on account of profit or interest would be made pursuant to (i) above except dividends as the directors from time to time determined;

(4) Although the Society had invested in illiquid assets, consisting of as yet unfinished buildings, the Society was solvent;

(5) In light of the prevailing economic circumstances, the directors had suspended payment of interest and bonuses to members on the providential grounds that although the Society was solvent, it would take some time and care to realise assets;

(6) Other members of the Society who had sought to withdraw had in the face of the ex post facto amendment to the Articles, considered themselves bound by the Amended Articles.

100. Against that background, the Court was decisive and critical: (at pp451-452):

> "—this is a case of one of the shareholders of the company who tries to convert herself into a creditor by giving notice of withdrawal, and, in fact, does by that means attempt to gain a priority over a great many other persons who had previously given notice to retire from the company. I doubt very much whether it is a reasonable or fair thing to use the power of this Court for the purpose of carrying such a project into execution".

101. Similarly the outcome rendered by the Court of Appeal in ***Walker v General Mutual Building Society*** *(1887) LR36 Ch. D. 777*; where Cotton LJ at 783 dealt with the issue as follows:

> ***"The case as I understand it is this: There are a number of persons who have given notice of withdrawal--- and the directors say that there are not the funds available to provide for the payment to (Mr. Walker), and it is only when there are funds available that the contract into which he***

entered gives him any right to be paid. The question therefore to be determined is whether there are properly within the meaning of these rules funds available for the purpose of paying this gentleman. He however says:

> *"Rule 78 does not apply to me. I am no longer a member, I am a creditor". But the question is not whether in some sense he is a creditor but whether, if and so far as he is a creditor he is bound qua member by the rules of the Society ....*

Here in my opinion, notwithstanding the notice which has been given, which enables the plaintiff to stand in a preferential position, his claim is still qua member, depending on his rights as member, and not upon rights belonging to him as an outside creditor. The distinction was drawn in several of the cases between the position of these creditor shareholders and real creditors and it was held that though they were in a position of preference against other members of the society, they were not creditors in the sense of making a claim independent of the rules of the society. I am of opinion that this objection prevails and that

the appeal must be dismissed". (emphasis supplied)

102. This decision was unanimous and at page 786 Fry LJ in similarly trenchant terms stated:

> ***"I do not think that the plaintiff has ceased to be a member, because he has given notice; but if he (has), he, at any rate, is a person claiming on account of a member, because his sole claim is to receive back payments made by himself in the character of a member….***
>
> ***His rights arise entirely from his membership, he is a withdrawing member, and till he has received payment, it appears to me he remains a member".***

103. Finally on this point, I think I need go no further than the House of Lords decision ***In re Blackburn and District Benefit Building Society; Walton v Edge and Others (1884) L.R. Vol. X H.L. (E) 33.***

104. There the rules of the benefit Society allowed any investing member to withdraw "provided the funds permit", upon giving notice, and declared that "No further liabilities shall be incurred by the Society till such member has been repaid". The society was ordered to be wound up and the assets were insufficient to pay everybody. It was held

(affirming the decision of the Court of Appeal, as taken from the head-notes) that those investing members who had given notice before winding-up began, were entitled to be paid out of the assets (after the outside creditors) in priority to those members who had not given notice of withdrawal notwithstanding the fact that between the giving of the notices and the winding-up, there were never any funds for payment.

105. I can see no basis for refusing to follow the reasoning and analyses from the foregoing line of cases, their Victorian vintage notwithstanding. These cases present two settled and relevant principles which to my mind are applicable mutatis mutandis to a modern mutual fund arrangement such as the Company, which is comparably premised upon the subscription to shares governed by clearly expressed if more complex rules and by which subscriptions may be redeemed subject to the powers and duties of the directors as promulgated under those rules, and where little of guidance has been decided under the more modern equivalent to Section 37 of the Companies Law; that is: Section 159 of the English Companies Act 1985 (the power given a company to redeem its shares.)

106. The two principles most apposite to the present case and which I adopt are these:

(i) Notwithstanding the notice of redemption (withdrawal) which has been given and which enables the unpaid shareholder (here Culross) to stand in a preferential position vis-à-vis other members in the event of insolvency; the shareholder's claim is still qua member for which he depends on his rights as a member, and not upon rights belonging to him as an outside creditor. As such he continues, until paid, to be bound by the rules of the Company.

Those rules may include –it will depend upon what is permitted – rules under which a decision to suspend redemptions, and perhaps even payments, may be properly taken.

(ii) That being the case, the filing of a petition as an attempt by a member to extract payment in priority to other members is neither fair nor reasonable and the Court will not allow its powers and process to be abused for such purposes.

107. Out of concern to have the fullest examination on the present issues and cognisant of the fact that we are here dealing with a complex arrangement for a modern investment vehicle, I brought to the attention of Counsel the unreported decision of the High Court of Justice of the O.E.C.S sitting in the British Virgin Islands in ***In the matter of Livingston International Fund Ltd. (in liquidation)* Claim No. BVIHC2002/0297.**

108. ***In Livingston (in liquidation),*** a mutual fund arrangement comparable to the Company's here, involved shareholders who had submitted redemption requests prior to the fund going into liquidation but had not yet been paid.

109. Among the regulations (articles) of the fund were provisions – regulations 60 and 74(b) – similar in effect to Articles 40 and 53 of the Company's here.

110. An important question proposed for that Court and answered in the affirmative, was whether those shareholders were entitled to have their shareholdings redeemed post-liquidation as creditors of the Fund, in priority to other shareholders (but not before outside creditors).

111. This conclusion was reached on an ex facie reading of the aforementioned regulations (60 and 74(b).

112. Regulation 60 stated (in terms similar to Article 40 here):

> "Upon the redemption of a share, the holder of such share shall cease to have any rights with respect thereto (except the right to receive the redemption proceeds and the right to receive any dividend declared but unpaid prior to the redemption being effected)".

113. Regulation 74(b) provided (alike Article 53 here) that for the purpose of the calculation of the net asset value, the price for shares in the company shall be deemed to be a liability of the company from the

close of business on the Dealing Day on which they are actually redeemed, until the price is paid.

114. Thus, the Court accepted the argument that the shares were actually redeemed on the redemption date and the price for the shares became a liability of Livingston from the close of business on the Dealing Day, until the price was paid. Accordingly, the shareholders in question were owed that liability and as of that date became creditors of Livingston. They would however, be able to rank ahead only of other non-redeemed shareholders but behind outside creditors.

115. The Livingston case was decided post-liquidation and so the question of what constitutes actual redemption of shares of a company as a going concern did not need to be and was not specifically decided. Otherwise, it seems to me that the position of the shareholders there was indistinguishable from that of Culross here.

116. And so while that aspect of the Livingston case dealt with the priority rather than the *locus standi* of shareholders, the conclusion that the claims of the earlier redeeming shareholders ranked in priority to those of other shareholders but behind outside creditors is to be regarded as plain and is entirely reconcilable with the conclusion

reached in the line of Victorian cases discussed above; in particular the decision of the House of Lords in In re Blackburn and District Benefit Society (above).

117. The important point of distinction between the present case and the Livingston case, arises from the circumstance in this case where the redeeming shareholder Culross, who has not yet been paid the price for its shares but remains entered as a member on the register of members of the Company as a going concern, insists nonetheless that its shares have been effectively redeemed so as once and for all to render it a creditor of the Company, owed a liability in the amount of the price of its shares as at the expiry of the redemption date and thus entitled to petition standing in the same position as any other outside creditor.

118. The final aspect of this proposition (ie: that Culross ranks with outside creditors) is not one with which I can agree but, as we will see, it is not crucial to the position of Culross here if, and, as I have also concluded, the rest of its proposition is correct.

119. I should explain why I do not agree with that final aspect. It flies in the face of Articles 39, 40 and 53 which, together, can make practical

sense only if the process of redemption (as distinct from the deemed effective redemption of shares) is complete upon payment of the redemption price and the expunction of the member's name from the register. Only then could Culross properly claim to stand as an outside creditor and no longer a member bound by the rules of the Company.

120. But, as we have seen, treating the process of redemption as complete upon the expiry of the redemption date, is not necessary to give effect to the true entitlement of the redeeming shareholder under the constitutional/contractual arrangements of the Company. This is because the liability represented by the redeemed shares will have been struck and settled and must be paid (ie: finally redeemed by completion of the process) ahead of any subsequent liability to other shareholders; even if the Company subsequently goes into liquidation (as in ***Livingston*** above).

121. Culross is entitled to payment ahead of other members who had not yet redeemed, but does not rank with or ahead of outside creditors.

122. This conclusion is the only one which is consistent, moreover, with sections 37(7)(b) and 49 (g) of the Companies Law which generally

provide that where a company is being wound up, there shall be paid in respect of any shares which have been redeemed or any dues to members in their character as such, all other debts and liabilities of such a company.

123. Clearly thus confirming the established position that outside creditors rank before shareholders who are owed a liability as shareholders.

124. But that conclusion is not an end to this matter.

POWERS TO SUSPEND REDEMPTIONS AND PAYMENTS: ULTRA VIRES?

125. As is shown from the examination of the Articles and CEM above, the power to suspend payment of redemption proceeds, is referenced at one place only; viz at page 19 of the CEM (see above). No such power is expressly given in the Articles.

126. Nor, indeed, did the directors reference any such specific power when they resolved pursuant to Articles 55 and 56, on the 17 April 2008, to suspend redemptions. Their resolution simply declared that they had decided to "suspend all redemptions at this time and that such action is in the best interests of the Company."

127. The refusal since the 1 May 2008 – when payment of 90% was due – to pay Culross, may not therefore be regarded as a refusal which is predicated upon the resolution of the directors to suspend redemptions taken on 17 April 2008 or upon any provision in the Articles.

128. Further, had the directors sought to justify the decision to suspend payment of redemption proceeds, one would have expected to see a specific resolution to that effect relying on the provision at page 19 of the CEM; where the power to do so is purportedly expressly given.

129. Such a resolution would then have brought into play questions about its validity and the vires of the CEM provision itself not comporting with the more limited powers given in Article 55.

130. The Company's argument (also as set out in the affidavit evidence) that the resolution to suspend the redemption of shares operated so as also to suspend the payment of redemption proceeds is not persuasive.

131. In the first place, it flies in the face of the promise at pages 17 and 18 of the CEM itself, that a redeeming shareholder will be paid 90% of his redemption proceeds within 30 days of the effective redemption date.

132. That is a promise which we have seen was in this case expressly re-affirmed by the Company in Mr. Herman's e-mail of 24 March 2008 to Mr. Blanchard and in the Administrator's e-mail to Banco on 11 April 2008 (see page 7 above).

133. It is a promise which was given also against the background of the express acknowledgement that Culross had effectively redeemed its shares at the expiry of the redemption date of 31 March 2008. The only outstanding issue was payment. And this was only consistent with the email sent on behalf of Culross by Mr. Keen on 1 May 2008 (the day following the expiry of 30 days from the redemption date of 31 March 2008) to Mr. Herman as follows:

> "Today, the Administrator is in breach of the commitment. This is a very serious lapse, for which we have been provided with no explanation whatsoever." (emphasis supplied)

134. It follows that for the resolution of the 17 April 2008 to have operated as a suspension of Culross' right to redeem its shares (let alone its right to payment of the proceeds) the resolution would have to be attributed retrospective effect.

135. Nothing in the Articles (or even the CEM) suggests that any such power exists. To the contrary, the binding effect of the Articles as they stand – here Article 53 in particular – is given statutory force by section 25(3) of the Companies Law which reads:

> "(3) Where registered the said articles of association shall bind the company and the members thereof to the same extent as if each member had subscribed his name and affixed his seal thereto, and there were in such articles contained a covenant on the part of himself, his heirs, executors and administrators to conform to all the regulations contained in such articles subject to this law;
> ...."

136. And by section 37(3) (c) of the Companies Law:

> "Redemption of shares may be effected in such manner as may be authorised by or pursuant to the company's articles of association."

137. And in this regard, it must be remembered that Article 17 gives force to the CEM only insofar as the CEM must be read as being subject to the Articles themselves.

138. Given then that Culross must be regarded as having redeemed its shares as at 31 March 2008, on the foregoing analysis it must be

regarded also as being a creditor which is owed a debt to which it became entitled in its character as shareholder (not having been removed from the Register) for immediate payment as at 1 May 2008, upon the expiring of 30 days after the 31 March 2008. That debt simply became quantified when the Administrator advised on 14 May 2008 – in keeping with the Company's prior obligation to identify the NAVs as at 31 March 2008 – that the value of its shares was $980,508.97.

139. That is the view of Culross' position to which I am ultimately compelled.

NO BONA FIDE SUBSTANTIAL DISPUTE

140. That being so there can, in my view, in the final analysis, be no "bona fide and substantial" dispute to be separately resolved within the meaning of the case law before Culross can claim its standing to petition (see ***CVC Opportunity Equity Partners v DeMarco*** (above) and ***Parmalat Capital Finance Ltd v Food Holdings Ltd*** (above). The words of Lord Hoffman from the ***Parmalat*** case are most instructive here (at para. 9 of the judgment delivered on behalf of the Board):

> *"If a petitioner's debt is bona fide disputed on substantial grounds, the normal practice is for the court to dismiss the petition and leave the creditor first to establish his claim in an action. The main reason for this practice is the danger of abuse of the winding up procedure. A party to a dispute should not be allowed to use the threat of a winding up petition as a means of forcing the company to pay a bona fide disputed debt. This is a rule of practice rather than law and there is no doubt that the court retains a discretion to make a winding up order even though there is a dispute; see for example, Brinds Ltd v Offshore Oil NL (1986) 2 BCC 98. But the Board does not find it necessary [in this case] to examine the limits of the discretion because they consider that there is no substantial dispute."*

141. The principle was earlier stated in equally clear terms by Chadwick J (as he then was) in **<u>Re a Company (No. 006685 of 1996)</u>** (above):

> *"There was no rule of practice in the Companies Court that a petition would be struck out or dismissed merely because the debtor company alleged that the debt was disputed. The true rule, which has existed for many years, is the rule of practice that this Court would not allow a*

winding-up petition to be used for the purpose of deciding a substantial dispute raised on bona fide grounds."

142. So, even if there is a dispute, if the Court is satisfied that it is not bona fide and substantial, it has a discretion to allow the petition to proceed, once it is first satisfied that the petitioner has standing.

143. And, in those circumstances "hardship" to the Company is irrelevant to the issue of whether the winding up order should be made. See McPherson's Law of Company Liquidation page 107.

144. Here, of course, the alleged bona fide and substantial dispute over the issue of standing also involves the Company saying that Culross is not an actual creditor, its right to payment not having crystalised during the continued suspension of the calculation of NAVs.

145. But that argument also flies in the face of Article 53 and of the Company's notification to Culross on 14 May 2008, that the redemption price is $980,580.97; being the NAV price as at the redemption date of 31 March 2008 – all in keeping with the Company's obligations under the Articles. There is no proper basis in those circumstances on which the Company can say that the debt

owed to Culross is not an actual debt but merely a prospective or contingent debt.

146. Moreover, there is nothing in the Companies Law that precludes a shareholder who is owed an actual but unpaid debt by a company, from petitioning in that capacity for its winding-up. This view is bolstered by section 37(7)(a) of the Companies Law which, while subordinating a redeeming shareholder's claim to those of outside creditors (as discussed above referencing sections 37(7)(b) (and 49(g) above), also makes plain that the shareholder's claim for the redemption proceeds of his shares is a debt that can be enforced where a company is being wound up.

147. As to proof that the Company is unable to pay its debts as they fall due (the cash flow test), that can indeed as Culross argued be a matter of inference, despite the Company's evidence of solvency to the contrary. See ***Oryx Natural Resources (above) and Cornhill Insurance PLC v Improvement Services Ltd.*** ***[1986] 1 WLR 114*** where the head note states:

> ***"Where a company was under an undisputed obligation to pay a specific sum and failed to do so, it could be inferred that it was unable to do so;***

> ***that, accordingly, the defendants could properly swear to their belief in the plaintiff company's insolvency and present a petition for its winding up ...."***

148. This view is also in keeping with decisions in other cases to the effect that an unpaid creditor of even a substantial and prosperous company is entitled to petition for its winding up even if owed only a small debt: ***Re a Company (1950) 94 SJ 369***; ***Mann v Goldstein [1968] 1 WLR 1091*** (both cited in French on Applications to wind up Companies, chapter 6, p 158).

149. According to that redoubtable jurist Ungoed-Thomas J., in Mann v Goldstein (above); the Court will not, in general, prevent an unpaid admitted creditor of a company proceeding with a petition to wind up the company even if it appears that the company is solvent.

150. There is, it must be acknowledged, the equally settled principle that a shareholder in an insolvent company will have no right to petition for its winding up because only outside creditors will have any real financial interest in the outcome: see In ***re Rica Gold Washing Co. (1879) 111 Ch. D. 35 (C.A.)*** This is a rule which has however been

more recently refined as follows by another esteemed jurist, Buckley J, in ***In re Othery Construction Ltd*** *[1966] 1 WLR 69:*

> ***"Nevertheless, it remains the rule that, before a contributory can petition successfully for the winding up of the company, he must show either that there will be a surplus of assets available for distribution amongst the shareholders or that the affairs of the company require investigating in respects which are likely to produce such a surplus."***

151. Here, while the refusal of the Company to pay may raise an inference of inability to pay sufficient to ground the petition, the evidence shows that after investigation, the Company will likely be found to be solvent and so Culross will have a financial interest in the outcome in respect of its unpaid debt, owed to it qua member of the Company.

152. This is all only in keeping with the further principle that, if there are no unpaid creditors' claims then shareholders claims become provable debts and can be the subject of a petition to wind up: ***Tottenham Hotspur PLC and Others v Edennote*** ***[1995] 1 BCLC 65.***

153. And there is no requirement that a particular method of proof must be used. A petitioner with a debt which is presently due does not have to

serve a statutory demand. See ***Taylors Industrial Flooring Ltd. v M and H Plant Hive (Manchester) Ltd.*** ***[1990] BCLC 216*** cited in French (op cit) - at page 405; where the authors doubt, with good reason in my view, the contrary view expressed in ***Re Hunza Investments Ltd.*** ***[1988-9] CILR 1.*** See also in this context ***Re Oryx Natural Resources*** (above).

154. Culross' debt is not one, from all the circumstances, about which it can in my view be said there is a bona fide and substantial dispute. I therefore conclude on the basis of the foregoing analysis, that Culross has the right to petition for its recovery.

JUST AND EQUITABLE GROUND

155. In the event that the foregoing conclusions are shown to be wrong; I must consider whether there is standing to petition on the "just and equitable" ground.

156. On the basis that Culross remains only a shareholder of a solvent company having a legitimate expectation given by the Articles and the promise of the Company in respect of the redemption of its shares, I consider that the petition should be allowed to proceed on the just and equitable ground. Here I have in mind in particular as Mr.

McDonough describes it, the Company's "volte face" – on the one hand confirming both on the 24 March 2008 and through its Administrator on 11 April 2008, that Culross would be paid its redemption proceeds and then, contrarily, resolving on 17 April 2008 to suspend redemptions and subsequently implicitly asserting that such suspension also operated to suspend the payment of redemption proceeds (notwithstanding that neither the director's resolution nor the letter sent to investors on 28 April 2008 said any such thing).

157. Further, by the time this application came on for hearing, the Company had had a year's actual notice of Culross' intention to redeem (first indicated on 31 October 2007) but maintains that it is not going to pay Culross "until the market recovers". Having no idea when that will be, the Company appears unwilling even to purpose a long-stop date by which it proposes to pay. Thus, the Company says it is entitled simply to disregard the fact that Culross has a legitimate expectation that, provided it complied with the rules in relation to notice, its redemption request would be honoured.

158. Culross also asserts, without demurer from the Company, that the Company can of course arrange for sale of some of the Master Funds'

assets to pay its claim now but chooses not to do so, because it deems that to be disadvantageous to the remaining investors, the largest of which is said to be controlled by two of the Company's directors. While this still does not necessarily suggest that the purported decision to suspend was taken in bad faith, it does suggest that the subsequent refusal to pay Culross the proceeds of its redeemed shares may be one influenced by the directors' being in a position of conflict of interest.

159. If the Company's position is correct, the effect would be that Culross would be exposed to the risk of the Company's assets declining below the level at which it could pay Culross' claim in full. Effectively therefore, the Company's position is that Culross should continue to be exposed to the declining market (but with no corresponding opportunity to benefit from an increase in the value of the assets), notwithstanding that Culross has given the required notice for the effective redemption of its shares from the Company in keeping with the Articles. Moreover, the Company would then continue to have use of Culross' money without cost of interest as Culross has no express right under the Articles to be paid interest on the outstanding redemption proceeds.

160. In these circumstances, even if the directors have a strict legal right to suspend payments and to impose a retroactive suspension upon redemptions, the Court might well find that it is just and equitable that the Company be wound up so that the assets may be realised to enable the payment of the redemption proceeds owed to Culross.

161. As was re-stated in ***O'Neill and Another v Phillips*** ***[1999] 2 All E.R. 761*** by the House of Lords (considering the more modern but broadly equivalent provisions of section 459 of the Companies Act 1985 (UK):

> ***"… although a member of a company would not ordinarily be entitled to complain of unfairness unless there has been some breach of the terms on which he had agreed that the company's affairs be conducted, equitable considerations might make it unfair for those conducting the affairs of the company to rely on their strict legal powers. That would be so where the exercise of the power in question would conflict with the promises the parties had exchanged, and it was not necessary that such promises should be independently enforceable as a matter of contract …."***

(Citing and applying the earlier House of Lords decision in ***Ebrahimi v Westborne Galleries Ltd*** *[1972] 2 All E.R. 492).*

162. And, as stated by the Privy Council in ***Gamlestaden Fastigheter AB v Baltic Partners Ltd and others*** *[2007] 5 LRC 500, 511:*

> ***"Where relief is sought via an unfair prejudice application .... the purpose of...section 459 or of (its) counterpart in (Jersey) or Hong Kong, [(or here in Cayman)] the jurisdiction to wind up a company on just and equitable grounds is to provide a means of relief to persons unfairly prejudiced by the management of the company in which they hold shares."***

163. Given all the circumstances of this case, on the basis that Culross, despite having complied with all the applicable rules and despite having had the assurances of the Company that it had redeemed its shares and would be paid, nonetheless remains a shareholder and bound by those rules, it clearly has *locus standi* to petition and a creditable case on the just and equitable ground.

164. The Company being also likely solvent, Culross has a clear financial interest in the outcome.

165. Culross may also well be heard to say that the Company should be estopped from denying its position, Culross having acted to its detriment by reliance on the Company's assurances (in the Company's email of 24 March 2008) and that of the Administrator (in its email of 11 April 2008) that the Company would be paid at least 90% of its redemption proceeds.

166. As Mr. Keen puts it in his affidavit filed on 2 July 2008 on behalf of Culross:

> "I can confirm however that if the Petitioner ("Culross") had not received the assurances from the Company – and from Citi (the Administrator) Culross would have been likely to have engaged attorneys to have taken steps to enforce Culross' legal rights and to protect Culross' position immediately after the Redemption Date had passed [(ie: 31 March 2008)] and I believe that Culross would have presented a winding up petition in respect of the Redemption Proceeds immediately the Redemption Date had passed and before any purported suspension of the payment of redemption proceeds by the Company."

167. Having received and acted to its detriment on the assurance that payment would be made, Culross it seems to me is now entitled to rely on the just and equitable ground by further reliance on principles of equitable estoppel to say that it is no longer open to the Company to rely on the purported suspension of payment of redemption proceeds (if it ever actually purported to do so which is denied by Culross).

See in this regard Chitty on Contracts 29th Edition, paragraphs 3-085 – 3-102 and in particular ***Hughes v Metropolitan Ry (1877) 2 App. Cas. 439 (cited at paragraph 3-094 op. cit).***

SUMMARY OF CONCLUSIONS

1. The Court undoubtedly has the jurisdiction to stay or strike out a winding up petition on grounds of abuse of process; including where the petition is disputed on bona fide and substantial grounds and such that the petitioner should pursue an alternative and more appropriate remedy which may be available.

2. Culross, having complied with the rules of the Company, had effectively redeemed its shares as at the redemption date of 31 March 2008. At that time a liability of the Company was created in favour of

Culross in the amount of the value of its shares –the redemption proceeds.

3. Until payment of the redemption proceeds and removal of its name from the register, Culross remained a shareholder bound by the rules of the Company when validly exercised.

4. Thus, Culross became a creditor of the Company in its capacity as a member owed a liability in the amount of the redemption proceeds. Culross would therefore rank ahead of other non-redeemed shareholders but after third party creditors, in the event of winding up.

5. The purported exercise by the directors on 17 April 2008 of a power of suspension which would prevent Culross' redemption of its shares was ultra vires the Articles. So too the purported reliance upon the CEM as a basis for "suspending" the payment of the redemption proceeds.

6. As at 1 May 2008 Culross was owed 90% of the redemption proceeds and the actual full amount was confirmed by the Administrator on 14 May 2008 to be $980,508.97.

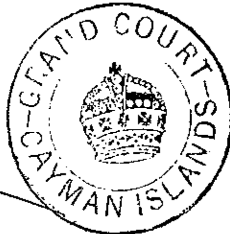
As creditor (qua member) owed an actual debt which is due and payable but not paid, Culross has standing to petition.

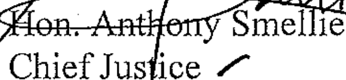
As there is no bona fide or substantial dispute over whether it has standing to petition to recover the debt owed it, Culross' petition is not an abuse of the process of the Court.

7. Alternatively, Culross should be allowed to petition on the ground that it is just and equitable to do so, even if the powers of suspension exercised by the directors are intra vires the Articles.

This is on the basis that the directors have used their powers to the unfair prejudice of Culross which has a legitimate expectation of redemption of its shares, the Company having acknowledged that it has redeemed and in light of the Company's promise to pay. The petition on this ground may also be justifiable on the basis that the Company should be estopped from denying Culross' right to assert that it has fully redeemed its shares.

For all the foregoing reasons, the application to strike out the petition is refused.





Hon. Anthony Smellie
Chief Justice

Dated 28st day of November 2008