

## BVI Litigation Update - First Quarter 2010 Case Notes

March 2010

### New Rules

New Commercial Court rules now apply. See link below for ease of reference. The new rules deal with a number of procedural points including case management conferences, pre-trial reviews and also include significant changes to the previous High Court costs regime.

Download the new rules [here](#).

### Insolvent Funds

There continues to be numerous issues surrounding the “creditor/investor” debate in fund’s litigation. There have been a number of cases of particular note. First of all *Citco Global v Y2K Finance* where a winding up petition was brought on two basis. First of all, alleged improper redemption payments made by the fund prior to the suspension of redemptions. The Commercial Court was of the view that it would not permit minority shareholders to wind up a company on the basis that it had, or might have, claims against its directors as this would be inconsistent with the rule in *Foss v Harbottle (1843) 2 Hare 461*.

The second ground was based on a loss of substratum argument and by the time of the hearing the fund agreed that it should be wound up, but the directors wanted the opportunity to realise assets, repay investors and then enter into a voluntary liquidation procedure. Although the Court preferred a wide definition of loss of substratum, it refused to make a compulsory winding up order as the directors were acting within the articles of association in making repayments and any investor would have the more appropriate unfair prejudice remedy.

The second major case is *Western Reserve International Ltd v Reserve International Liquidity Fund* which gave specific guidance on the “creditor/investor” issue. Although cases depend on their individual articles of association and other documents, the Court provided very useful guidance on this area and on the operation of section 197 of the Insolvency Act which provides that:

*“A member, and a past member, of a company may not claim in the liquidation of the company for a sum due to him in his character as a member, whether by way of dividend, profits, redemption proceeds or otherwise, but such sum is to be taken into account for the purposes of the final adjustment of the rights of members and, if appropriate, past members between themselves.”*

In *Reserve* the “investor” argued that it had redeemed was therefore a creditor and able to wind up the fund. The Court decided that the effect of the articles was that if a redemption request was received before 5pm on a dealing day, the redemption of the investor’s shares was completed on that day. The Court noted that the redemption was submitted before any suspension period and the investor had therefore become a creditor for the unpaid redemption proceeds in its capacity as a seller entitled to a price of shares. Accordingly section 197 did not preclude the petition.

Our Distressed Funds Group has prepared a detailed analysis of the *Reserve* case, which is available [here](#). *Reserve* has been appealed and we will bring you the result of that appeal.

In another recent decision, *Barefield Nominees Limited v Westford Special Situations Fund Ltd.*, the BVI Court held that a feeder fund electing to redeem an investor in specie must provide quantifiable assets and that, in this instance, a share in the Master Fund would not be adequate. The decision was fact specific but is an important reminder to funds seeking to make redemption payments in kind to be very wary as to exactly what is being proffered in satisfaction.

### **Cross-Border Insolvency**

Harney also recently acted for BVI and Hong Kong joint-liquidators in obtaining court sanction to enter into a memorandum of understanding (“MOU”) with a United States Receiver appointed over the same BVI company. The MOU, also approved by the California District Court, defined what assets each office holder should gather according to where they are situated.

The MOU, the first known of its kind, was important in that it manages the duties of liquidators and a receiver (not appointed via “insolvency proceedings”) to co-ordinate and streamline asset gathering activities for the benefit of the creditors.

**“Stand alone” injunctions**

In the recent case of *Black Swan Investment I.S.A. v Harvest View Limited* the BVI High Court held that it was within its discretion to grant a “stand alone” freezing injunction in support of foreign proceedings. It was previously thought, by reason of the English House of Lords case of *The Siskina* [1979] AC 210, that the Court could not grant a freezing injunction unless the injunction was made in support of a claim which the Court granting it had jurisdiction to enforce by final judgment - often referred to as “a substantive cause of action”. However, the BVI Court held that such an interpretation of *The Siskina* was incorrect and all that Lord Diplock was saying in that case was that the High Court in England had no power to grant an injunction except in protection or assertion of some legal right which it has jurisdiction to enforce by final judgment. As has subsequently been held in the English case of *Channel Tunnel Group v Balfour Beatty Ltd* [1993] AC 334, this formulation does not preclude the English court from granting an interlocutory injunction ancillary to a claim for substantive relief to be granted by a foreign court or an arbitral body. Citing the dissenting judgment of Lord Nicholls in the Privy Council decision of *Mercedes Benz Ag v Leiduck* it was held that since there was no reason in principle why a claimant could not enforce a foreign money judgment in the BVI Courts, there seemed no logical reason why he should not be able to make a claim for ancillary relief to a foreign award or judgment, such as a freezing injunction.

This decision has particular relevance in offshore jurisdictions because the business of companies incorporated in such places is invariably transacted abroad and disputes between parties who own them and others are often resolved abroad. The BVI Court noted that it would be “highly detrimental” to the reputation of an offshore jurisdiction if potential judgment creditors seeking to have resort to judgment debtors’ assets located in such jurisdictions were required to first commence substantive proceedings in order to claim ancillary relief. It was noted that similar conclusions have been reached by the Court of Appeal of Jersey and Guernsey.

*If you have any questions about these cases please contact Phillip Kite ([phillip.kite@harneys.com](mailto:phillip.kite@harneys.com)) or Andrew Thorp ([andrew.thorp@harneys.com](mailto:andrew.thorp@harneys.com)).*

*The foregoing discussion and analysis is for general information purposes only and not intended to be relied upon for legal advice in any specific or individual situation*