



IN THE GRAND COURT OF THE CAYMAN ISLANDS

CAUSE FSD 16 OF 2009 ASCJ

IN THE MATTER OF THE COMPANIES LAW (2007 REVISION)

AND IN THE MATTER OF THE SPHINX GROUP OF COMPANIES (IN OFFICIAL LIQUIDATION) AS CONSOLIDATED BY THE ORDER OF THIS COURT DATED 6TH JUNE 2007 (“SPhinX”)

IN CHAMBERS
BEFORE THE HON. CHIEF JUSTICE
THE 2ND OCTOBER 2013; 18TH OCTOBER 2013

Appearances: Mr. Thomas Lowe QC and Ms. Ceri Bryant QC instructed by Ms. Cherry Bridges of Ritch & Conolly, Attorneys-at-Law for the Joint Official Liquidators (“the JOLs”) of SPhinX Group of Companies

Mr. Mark Phillips QC instructed by Ms. Andrea Dunsby and Ms. Charlotte Hoffman of Turners, Attorneys-at-Law for the Liquidation Committee (“the LC”)

Mr. Richard Sheldon QC (appearing by video link) instructed by Mr. Guy Manning and Mr. Guy Cowan of Campbells, Attorneys-at-Law for DPM/the Indemnity Claimants

Mr. William Trower QC (appearing by video Link) instructed by Mr. David Collier of Charles Adam, Ritchie & Duckworth (Card) Attorneys-at-Law for Deutsche Bank

Ms. Sarah Dobbyn (appearing by video link) and Mr. Allain Forget of Sinclairs, Attorneys-at-Law for hfc Limited

Mr. Ben Hobden of Conyers Dill & Pearman, Attorneys-at-Law for BAWAG

Mr. Marc Kish of Maples & Calder, Attorneys-at-Law for Refco Public

JUDGMENT

1. The joint official liquidators (the “JOLs”) of the SPhinX Group of Companies (“SPhinX”) now apply for sanction of a scheme of arrangement (the “Scheme”) by which claims of the Scheme claimants under the SPhinX estate would be settled and further, for leave to make an initial distribution of dividends.
2. It is acknowledged that the two applications involve separate issues. Sanction, for which the Court must be satisfied that it has jurisdiction, must be addressed first¹. Provided the Court is prepared to sanction the Scheme, the question of what distribution can be made pursuant to the Scheme can then be considered.
3. The JOLs’ application is supported by SPhinX’s Liquidation Committee (the “LC”). The LC’s members are all shareholders in SPhinX and stand to recover a dividend if the Scheme is sanctioned and a distribution of assets is ordered.
4. Creditors of the liquidation estate did not vote under the Scheme. This was on the basis that adequate provisions would have to be made under the Scheme to meet creditor claims and so their interests were not to be compromised under the Scheme. In effect, the Scheme thus proceeded on the basis that the SPhinX liquidation estate is solvent.
5. The Scheme was first voted on by investors – theirs being the only stakeholder rights to be compromised under the Scheme – at court convened meetings in December 2011. At that time, the statutory majorities were obtained in 20 of 22 classes. In October 2012, a re-vote was held in the two classes where the majorities had not been obtained. One class voted in favour and the other class was subsequently bought out

¹ As also explained in a written judgment delivered in this cause on the 21st December 2012 (the “December 2012 Judgment”).

in its entirety by Deutsche Bank, a major investor and one of the proponents of the Scheme (“DB”). The statutory majorities have therefore now been obtained in all classes and this was confirmed by the December 2012 judgment.

6. There was then however, still outstanding the question whether liability to creditors, in particular potential contingent creditors, could exceed the value of the assets. In that event, it was acknowledged by all interested parties that the Court would lack jurisdiction to sanction the Scheme. An indemnity reserve had been set² to cover legal costs that might be owed to the only known class of contingent creditors (the “Indemnity Reserve” and “Indemnity Claimants” or “ICs” respectively), but other possible contingent liabilities were not then provisioned.
7. In particular, contingent liabilities that could arise from potential “contribution claims” against ICs (to be discussed below), and from claims which Beus Gilbert, the JOLs’ United States lawyer might bring. These latter were apprehended by the JOLs as probably to arise for breach of contract on the basis that the Scheme, if entered into, would undermine the New York proceedings that Beus Gilbert had undertaken on behalf of the JOLs on a contingency fee arrangement. More on the New York Action below.
8. On 6th December 2012, I ordered that a jurisdictional hearing take place to determine:
 - (1) Whether upon sanction of the Scheme there is a real risk of a liability to Beus Gilbert or no risk of such a liability which, when added to the Indemnity Reserve and the other reserves to be established under the Scheme³, would

² By judgment delivered on 4th December 2010; reported at 2010 (1) CILR 234 and by which it was ordered that the reserve for those purposes should be USD117 million (approx.).

³ Including a General Reserve to cover a number of issues.

exhaust the cash assets of the SPhinX Companies (the “Beus Gilbert Reserve Issue”): and

(2) The appropriate Indemnity Reserve (for ICs), in accordance with paragraphs 9 to 18 [of the Order].

9. These questions were tried before the Rt. Hon. Sir Andrew Morritt (as a judge pro tem of this Court) during the course of a hearing from 17th June to 2nd July. By judgment delivered on 9th July 2013, he found that there is jurisdiction to sanction the Scheme (the “Jurisdiction Judgment”). In summary, he held that there was no real risk of a liability to Beus Gilbert; that the Indemnity Reserve should now be USD113,918,394 (to be reduced by USD13,763,463 if within 14 days the JOLs did not elect to commence proceedings in this jurisdiction against PriceWaterHouseCoopers (Cayman) (“PWC Cayman”) one of the ICs⁴; that USD10 million should be added to the Indemnity Reserve to cover a potential shortfall in the Net Litigation Proceeds to be recovered from the New York Action and to be provisioned to meet any potential contribution claims against ICs; and that USD15 million should be added to the General Reserve⁵.
10. At paragraph 100 he expressed his conclusion that this Court has jurisdiction to sanction the Scheme in these terms:

*“The total of the reserves I consider should be made is \$138,918,394.⁶
That is well short of the present value (\$500 million) of the assets
under the control of the JOLs. Accordingly, and in response to the*

⁴ PriceWaterHouseCoopers (United States) were already defendants to the New York action along with 35 other ICs.

⁵Para. 99 of the Jurisdiction Judgment. The General Reserve being that to be set aside for meeting the future general expenses of the liquidation, including the JOLs’ fees and expenses.

⁶ This figure does not include interest but does include the reserve for PWC Cayman.

questions posed by the order of the Chief Justice, I consider that this Court does have jurisdiction to sanction the Second Scheme⁷”.

11. Sir Andrew Morritt also declared in the following terms:

“Upon sanction of the Scheme there is no real risk of a liability to Beus Gilbert and no risk of a liability which, when added to the Indemnity Reserve and to the other reserves to be established under the Scheme, would exhaust the assets of the SPhinX Group of Companies.”

12. As the matter comes before me now there are, however, pending applications for leave to appeal against the Jurisdiction Judgment.
13. DPM Mellon Ltd and DPM Mellon LC (together “DPM”) seek to bring that appeal in their capacities as representatives of the ICs⁸. DPM complains that the Indemnity Reserve is inadequate and, in particular, that the sum of USD10 million to be added to the Net Litigation Proceeds to cover any potential contribution claims that might be made against ICs, is unrealistically low. For reasons to be examined below, DPM submits that the sum to be added to the overall reserves to cover potential contribution claims should be USD360,941,000. This sum, when added to the other sums to be reserved, would in light of recent developments since the Jurisdiction Judgment, require total reserves of USD539,941,000, shy by a mere USD1,059,000 of the sum of the value of the assets presently under the control of the JOLs⁹.

⁷ There was an earlier Scheme that failed in implementation. See 2010 (1) CILR 454 for the judgment that sanctioned that scheme.

⁸ Appointed as such by order following a judgment of this Court, delivered on 20th July 2010, reported at 2010(2) CILR 1.

⁹ That is: USD541,000,000 and which includes proceeds of USD67 million actually received by the JOLs from the settlement of the claim against PWC (U.S. and Cayman) Mayer Brown (SPhinX’s former U.S. lawyers) and others in the New York Action – and is net of the sum of USD101 million paid so far after payment of the Beus

14. DPM regards that slimmest of buffers provided by the sum of USD1,059,999 as likely soon to become a deficit on account of pre-judgment interest that might accrue on any contribution claim to be brought against an IC.
15. As the possibility of contribution claims (however “small” as the Jurisdiction Judgment found that possibility to be) must nonetheless be considered and fully provided for; DPM argues – and would seek to argue on appeal – that there will probably be a deficit between the reserves and the assets and therefore that the jurisdiction to sanction the Scheme is not established.
16. For their part, the JOLs had also sought to appeal against the Jurisdiction Judgment. This was as to the conclusion in it that there was no risk of a liability to be owed by them to Beus Gilbert to arise from the sanction and implementation of the Scheme. While not accepting that any liability to Beus Gilbert would arise, the JOLs were concerned to ensure that provision be made for any such risk of liability for which they might be exposed, having entered into the contingency fee arrangement with Beus Gilbert.¹⁰
17. The conclusion of the Jurisdiction Judgment that there is no real risk of a liability to Beus Gilbert arising has only been confirmed by subsequent events.
18. In light of the PWC (United States) (and other) settlements – from which, by reliance on its contingency fee arrangement Beus Gilbert has received (and will continue to receive as scheduled payments come in) 33% of the proceeds – Beus Gilbert can no

Gilbert contingency fee of 33% arising from those settlements. A further sum of USD37 million is due by way of scheduled payments, to bring the total sum of these settlements to USD138 million.

¹⁰ On the basis that the Scheme involved compromises with scheme participants, including DB as an important defendant to the New York action for very significant claims; Beus Gilbert had asserted that the JOLs’ entering into the Scheme would undermine the possibility of recovery against those (and by association other) defendants and that Beus Gilbert would be entitled to damages for breach of contract or to a quantum meruit of up to USD250 million, being 33% of the value of the claim (i.e.: USD750 million) in the New York action.

longer assert that its contract would be repudiated. The JOLs are therefore now less concerned about a Beus Gilbert reserve and are not pursuing their appeal against the Jurisdiction Judgment. The JOLs' position now, as explained by Mr. Lowe QC, is that even taken at its highest, DPM's objection is unfounded because it must be recognized that there will be a surplus (however small) and therefore the jurisdiction of the Court to sanction the Scheme is now clearly established.

19. Mr. Lowe QC argues that there being no prospect of a successful appeal by DPM against the Jurisdiction Judgment, I should now proceed to grant sanction of the Scheme, so that the affairs of the SPhinX liquidation estate may move to the next stage of identifying the appropriate amounts for distribution.
20. The estate is to be regarded as solvent says Mr. Lowe QC and investors have been kept out of their money for far too long, the liquidation having commenced more than six years ago on 30 June 2006. There have been no distributions of dividends to date.
21. That being the background to the present state of affairs, the focus of this judgment will be to address the DPM objection.
22. Leave to appeal having been refused to DPM by Sir Andrew Morritt and its application to the Court of Appeal for leave having not yet been considered, I proceed on the basis that it would be inappropriate to allow DPM's leave application to operate as if by way of a stay of the sanction proceedings.
23. DPM has itself made no such application¹¹. Instead, Mr. Sheldon's argument proceeds on the basis that this Court has a continuing obligation to ensure that the statutory rules which mandate the priority of the interests of creditors are observed.

¹¹ And it is at least moot whether such an application could be made given that the Jurisdiction Judgment was declaratory in nature (as to the existence of the jurisdiction of the Court). The JOLs cited a recent decision of the BVI Court of Appeal to the effect that a stay cannot be imposed upon a declaratory judgment: *Cukurova Finance Int'l Limited v ALFA Telecom Turkey Limited* HCVAP 2010/018; 024, December 5, 2011.

The rules recognize the interests of contingent creditors for whom provisions must be made¹² and mandate that their interests shall take priority over those of shareholders (such as are the investors in SPhinX). The principles must be observed and faithfully applied¹³.

24. This is indeed the normal liquidation process which is recognized and enforced by the Court¹⁴ and which required that the question of jurisdiction be first framed as it was and determined by the Jurisdiction Judgment.
25. The ongoing obligation of the Court (and of the JOLs who are its officers) to ensure the due observation of the priority of claims in the liquidation process must indeed be recognized. This obligation was one that Sir Andrew Morritt himself addressed as a matter of ongoing concern in the Jurisdiction Judgment in these terms (at paras 101-102):

¹² Section 139(1) of the Companies Law (2013 Revision ("the Law") provides:

"All debts payable on a contingency and all claims against the company whether present or future, certain or contingent, ascertained or sounding only in damages, shall be admissible to proof against the company and the official liquidator shall make a just estimate so far as is possible of the value of all such debts or claims as may be subject to any contingency or sound only in damages or which for some other reason do not bear a certain value."

And, as carried into practical effect by the Companies Winding up Rules, Order 18 Rule 4(1):

- "In calculation and distribution of a dividend the official liquidator shall make provision for –
- (a) Any debts which appear to him to be due to persons who, for whatever reasons, may not have had sufficient time in which to tender and establish their proofs;
 - (b) Any debts which are the subject of claims which have not yet been determined;
 - (c) Expenses of the liquidation which are anticipated but not yet incurred."

¹³ Section 110(1) of the Law provides:

"It is the function of an official liquidator:

- (a) To collect, realize and distribute the assets of the company to its creditors and, if there is a surplus, to persons entitled to it..."

Section 140(1) also provides in this regard:

- "(1), the property of the company shall be applied in satisfaction of its liabilities *pari passu* and subject thereto shall be distributed among the members according to their rights and interests in the company."

¹⁴ Explained as it applies in this jurisdiction for instance, in *In Re Bristol Fund 2008 CILR 317*.

“101.Whether or not it is its purpose, the effect of this (S)cheme is to invert the normal liquidation processes. Normally members, for that is what the Investors are, would have to await the proper evaluation of proofs of debts submitted by creditors, actual, contingent and prospective. Those creditors, which include ICs, would have the normal rights of appeal [against rejection of proofs of debts] and the ability to compel the liquidators to wind up the company in accordance with the Companies Act (sic) (2012 Revision). The risk of an insufficiency of assets would fall on the members not the creditors.

102. Under this (S)cheme the risk of an insufficiency of assets falls on the creditors not the members because its purpose is to distribute to the members all but the reserves I have set long before the various sets of proceedings have been finally concluded. If my assessment of the necessary reserve is wrong the loss will fall on the creditors, including the ICs; the balance will have been distributed to members without possibility of recall.”

26. To address this risk of the possible “(inversion) of the liquidation process”, the learned judge gave this advice; (ibid):

“It is for consideration whether distributions should be conditional on some secured obligation to repay if the reserves prove in the event to be insufficient. This did not arise from the questions I was required to

determine. If no such provision is inserted into the Scheme it may be that the court would require one as a condition of its sanction.”

27. In response to this advice, Mr. Lowe QC on behalf of the JOLs, while acknowledging that the court has the authority to impose a requirement of a secured obligation or undertaking to repay as a condition of sanction, argues firmly against it. The JOLs’ firm position is that no such condition could be either fair or practicable.
28. It would be unfair, said Mr. Lowe QC, to impose such a condition now, the Scheme having been considered and approved by the Investors without any such thing being in their contemplation. The Scheme would also likely be entirely derailed because it would be practically impossible to obtain the necessary obligations or undertakings to repay from the myriad underlying investors on whose behalf a number of the shareholders of record hold their global interests in representative capacities. These, said Ms. Dobbyn – who supported Mr. Lowe QC on this issue – could include very many pensioners who have been awaiting their dividends for years and from whom it would be both impracticable and unreasonable to require an undertaking to repay.
29. Moreover, the objection goes - and joined in with equal force also by Mr. Phillips QC and Mr. Trower QC – as in the final analysis the SPhinX estate must be regarded as solvent, the people who have the real economic interests to be protected are the investors, not the contingent creditors like the ICs. Further, the ICs are to be seen as a rapidly diminishing class and DPM as representative of that class which is likely soon to become, if is not already, a class of one – DPM itself.
30. This last assertion was made against the background of the latest developments in the New York Action where the settlements with PWC (United States) and others, have resulted in DPM (together with Mr. Robert Aaron, an individual related to it) being

one of only five defendant ICs remaining from the 36 originally sued. The other four are individuals with whom settlement discussions are being advanced and may soon be completed.

31. Given that state of affairs, Mr. Phillips urged me to view DPM's conduct in these proceedings, and in particular its estimates of the indemnity reserve as exceeding the entirety of the available assets, with scepticism.
32. In my view, having regard in particular to the fiscal impact of the recent developments described above¹⁵, the entire premise upon which the Jurisdiction Judgment was decided has indeed been confirmed.
33. In particular, it is now clear beyond serious argument, that there is no real risk of the normal liquidation processes becoming inverted and shareholders being preferred over creditors. In particular, I foresee no reasonable risk of the liabilities to ICs becoming greater than all the assets on account of the ICs becoming liable for contribution claims for which they would be entitled to be indemnified by SPhinX.
34. I explain this view as follows.
35. The ICs' concern, as expressed by Mr. Sheldon QC, is no longer primarily addressed to the amount of the Indemnity Reserves for their legal costs. It seems to be acknowledged that the costs reserve, as identified in the amount of USD113 million in the Jurisdiction Judgment, would be adequate.
36. The concern is now rather addressed to the amount of the Net Litigation Proceeds; that it should match – as to 100% - the amount of any contribution claims that could

¹⁵ On top of the net proceeds of USD67 million that have come in from the PWC (United States), Mayer Brown and other settlements and the further diminished possibility of a Beus Gilbert claim, a further consequence is that the costs aspects of the Indemnity Reserve can be reduced by USD71million. This is agreed by all sides as being attributable to the fact that there can no longer be an indemnity claim for costs or contribution by PWC (United States), Mayer Brown or by the other ICs covered by the settlements.

or might be brought by an unsuccessful defendant to the New York Action to recover from an IC the amount of any damages awarded against that defendant and in favour of the JOLs (“a contribution claimant”).

37. Mr. Sheldon QC points to the fact that the Scheme itself recognizes the obligation of the JOLs to set aside a reserve comprised of the Net Litigation Proceeds. This is so.

38. Paragraph 5.2.3 of the Scheme provides:

“...any Net Litigation Proceeds achieved after the Indemnity Reserve Ruling has been obtained will be added to and become part of the Indemnity Reserve save insofar as, upon an application by the JOLs and/or the Scheme Supervisors and/or any Scheme Claimant under Clause 5.2.5, the Court otherwise directs”; and

“Net Litigation Process” as defined is “any and all the proceeds of the Third Party Litigation received by a SPhinX Company in respect of such Third Party Litigation [(i.e.: the New York Action)] net of the amounts due to Beus Gilbert under the representation agreement between Beus Gilbert and the JOLs.”

39. The potential problem is said by Mr. Sheldon QC to possibly arise in this way: As the definition of Net Litigation Proceeds excludes recoveries payable to Beus Gilbert under its Representation Agreement, in theory, a successful claim against a defendant to the New York Action for say USD1,000, (who then becomes a potential contribution claimant) will only create an increase in the Indemnity Reserve of USD666; but the contribution claimant may have a claim over and against an IC for the full amount of USD1,000.

40. It is recognized in the Jurisdiction Judgment that a reserve needs to be made in respect of that potential shortfall and it is in this regard that it was decided that the sum of USD10 million should be added to the Indemnity Reserve.
41. As presented by Mr. Sheldon, the basis of DPM's proposed appeal therefore, is in summary that Sir Andrew Morritt erred in law by setting a reserve of only USD10 million to cover a potential shortfall in the Net Litigation Proceeds. In particular:
1. Contrary to the LC's submission that the chances of a successful contribution claim being brought against an IC for more than 2/3rds of a contribution claimant's liability were so unlikely as to be fanciful, the learned Judge held¹⁶
 - (i) That while the likelihood of such a claim "*is small, ...I cannot say that it is so small as to be ignored*";
 - (ii) *That the "solution is to supplement the 2/3rds retention;" and*
 - (iii) *"The amount is not susceptible to any logical calculation, but a supplement of \$10 million is, in my view, most likely to be more than is, in fact required."*
 2. It was established by the Chief Justice in the Indemnity Reserve Judgment¹⁷, and acknowledged by Sir Andrew Morritt in the Jurisdiction Judgment, that the amount of reserve to be made in respect of a non-fanciful liability "*should be the full amount of the liability*"¹⁸.
 3. Accordingly, having accepted that there was a non-fanciful risk of a successful contribution claim being brought for more than 2/3rds of a

¹⁶ Jurisdiction Judgment paragraph 45.

¹⁷ Reported at 2010(1) CILR 234

¹⁸ Jurisdiction Judgment para. 6(1); Indemnity Reserve Judgment para. 17.

contribution claimant's liability, Sir Andrew Morritt ought to have made a reserve for the full amount of the liability.

42. Given the hypothetical nature of the exercise involved in seeking to quantify "the non-fanciful liability" of an IC to repay 100% of a contribution claim, considerable effort was made by DPM for their part and the JOLs for their part (the latter in support of the Scheme) to illustrate what a possible quantum could be.
43. This led to DPM's estimate of the potential shortfall in the Net Litigation Proceeds of USD360,941,000 (mentioned above) and the JOLs' estimate of USD225-230 million. This would leave, in the JOLs' estimate, a comfortable buffer of about USD311 million from the available assets of USD541 million¹⁹.
44. The hypothesis adopted on both sides for the purposes of their estimates, is that potential contribution claims against an IC could be for the full amount of the damages claimed by the JOLs in the New York Action, assuming also that a contribution claimant would have been ordered to pay that full amount to the JOLs. An understanding of the hypothesis requires a further understanding of the New York Action.
45. The JOLs' claim in the New York Action is in three parts – the first, the so-called Refco claim²⁰; the second, the claim for the lost market value in the shares of Plus Funds – the parent company and promoter of SPHinx – resulting from the market's reaction to the Refco fraud²¹; the third, pre-judgment interest at the rate of 9% from

¹⁹ Notwithstanding that the JOLs say, as explained above, that even on DPM's calculations, there would be a buffer of USD1,059,000 (after taking account of the General Reserve and other reserves).

²⁰ For the sum of USD263 million, the net amount from the larger sum of USD320 million which was fraudulently misappropriated and placed with the Refco Group and lost when that ill-fated group went into bankruptcy. The sum of USD320 million was recovered at an early stage by the SPHinx estate but pursuant to a settlement with the Refco Trustee, the SPHinx estate had to repay the sum of USD263 million on the basis that the recovery of USD320 million from Refco was a fraudulent preference over its other creditors.

²¹ Said to be USD196 million.

March 2004 on the Refco claim calculated up to the present²². The maximum potential liability of a contribution claimant (and hence of an IC) therefore becomes USD680 million as also explained in paragraph 32 of the 30th Affidavit of Margot MacInnis (one of the JOLs) in these terms::

“...as to the overall figure [for the potential shortfall in the Net Litigation Proceeds] even if [DPM’s] appeal is successful, even with interest the total amount cannot exceed USD225-230 million. The JOLs’ United States Counsel advise that total damages of USD680 million were claimed in the United States Litigation, [not in fact USD750 million as was earlier estimated] made up of the following elements (i) USD263 million which SPhinX lost as a result of the settlement of the preference action with the Refco Trustee; (ii) USD196 million which is the valuation of the lost market value of Plus Funds and (iii) interest on (i) the present total amount of about USD221 (of the Refco loss still not recovered) at the rate of 9% from March 2004 (there being no interest claim in respect of the claim for the lost market value of Plus Funds, as those loses are unliquidated).”

46. Accepting for the sake of the arguments DPM’s calculations, Mr. Lowe QC for the JOLs maintain that there would still be that marginal surplus of USD1,059,000 mentioned above (at para. 13) arrived at in this way:

²² Said to be USD221 million.

	USD	USD
Current Net Assets		541,000,000
Less:		
1. Legal costs reserve as agreed to be reduced by USD71 million in light of the PWC (U.S. and Cayman) settlements	73,000,000	
2. DPM's assessment of the shortfall in the Net Litigation Proceeds	360,941,000	
3. General reserves (to cover the remaining expenses of the liquidation, etc).	85,000,000	
4. Litigation Reserve in respect of potential litigation claim such as may be presented by SPhinX's former Cayman Islands lawyers if sued for professional negligence	16,000,000	
5. Portfolio Manager's and Trade Creditors' Reserve	<u>5,000,000</u>	<u>539,941,000</u>
		1,059,000

47. Mr. Lowe QC identifies this marginal surplus as real enough to justify the grant of sanction to the Scheme but Mr. Sheldon QC disagrees.
48. He submits that this "tiny surplus" will quickly turn into a deficit if pre-judgment interest is factored in. For instance, if a contribution claimant were to wait even for a short period before bringing a contribution claim against an IC, the surplus would be eliminated: 1 month's pre-judgment interest at 9% on the maximum claim in the New York Action of USD646,462,500 (that is USD784,000,000 – USD138,000,000 of gross recoveries so far achieved²³) would be USD4,848,468.75. The position

²³ DPM's calculation of this figure of USD784,000,000 takes account of pre-judgment interest that DPM says could be due on the claim in the New York Action related to the lost market value of Plus Funds (i.e.: USD196 million) and other matters which the JOLs explain per Margot MacInnis (at para. 45 above) they no

becomes far worse he argues, if one assumes that a contribution claimant waits until near the end of the expiry period to bring a contribution claim, which would be six (6) years from the date of the award made against the contribution claimant. In that scenario, the necessary reserve for the shortfall in the Net Litigation Proceeds at 9% interest per annum would be USD710,031,312.50 being: (USD360,941,000 + ((USD646,462,500 x 0.09) x 6).

49. This sum, without any of the other reserves factored in, would therefore far exceed the available assets of USD541,000,000, even if invested at current rates of return.²⁴
50. Mr. Sheldon QC concluded thus as I am obliged to recognize a real risk that DPM could be subject to a contribution claim, it follows that the Scheme may not be sanctioned and distributions may not be allowed. The rules require that even if there is a low (but non-fanciful) risk of a contribution claim being brought against an IC, a full reserve is still required.²⁵ Moreover, submitted Mr. Sheldon QC, Sir Andrew Morritt has determined that the risk of a 66% retention being insufficient is “*small but I cannot say that it is so small as to be ignored*” (Jurisdiction Judgment paragraph 45) and it is not open to the JOLs to go behind that particular finding, which is not the subject of any appeal.
51. The awkwardness of this argument must of course, itself be recognized, having regard to DPM’s intention to challenge the ultimate conclusion of the Jurisdiction Judgment that “*there is no risk of a liability which when added to the Indemnity Reserve and the*

longer claim. The amount of USD138,000 million is as explained above at F.N. 9, the gross amount of the settlements so far achieved in the New York Action, USD67 million of which has actually been received by the JOLs.

²⁴ Recognized by the JOLs to be between 1% - 5% at current rates of return, depending on the nature of the instrument.

²⁵ See F.N. 12 above. The JOLs are required to “make a just estimate” and provision for that amount. This is as also explained in the Indemnity Reserve Judgment: 2010 (1) CILR 234.

other reserves to be established under the Scheme, would exhaust the cash assets of the SPhinX Group of Companies.”

52. As discussed above, in the present circumstances of this matter now coming before me for sanction, that conclusion reached in the Jurisdiction Judgment remains effective, no leave to appeal having yet been granted.
53. In the prevailing circumstances – not least the situation where investors in SPhinX have been awaiting a dividend for more than 6 years – I consider that I am obliged to arrive at a decision on the JOLs’ application for sanction, DPM’s foreshadowed appeal notwithstanding.
54. To that end, I consider I am able to address the present contention myself, which is whether or not there is a real risk that DPM (or any other IC) could be subject to a contribution claim that turns out to be more than the recoveries of the Net Litigation Proceeds. This is the real concern for the grant or withholding of sanction.
55. In so proceeding to find an answer to this question, I do not disregard the pending application for leave to appeal. I proceed on the basis that while the Jurisdiction Judgment stands, it must be observed and applied in the light of prevailing circumstances. I note as well for what it may be worth, that, if the enquiry as premised is resolved in favour of sanction, that conclusion may itself be taken on appeal by DPM at the same time as it seeks to appeal against the Jurisdiction Judgment, subject to leave being granted.

Analysis

56. It is clear that the number of defendants to the New York Action and so the potential for contribution claims to be brought by any, is very significantly reduced since the PWC (U.S. and Cayman) and other settlements.

57. As mentioned above, it now is quite probable that DPM/Aaron (apart from three other individuals) are the only remaining IC defendants²⁶.
58. Mr. Sheldon QC reminds me nonetheless, that while proceedings brought by the JOLs against several defendants have been dismissed²⁷, the JOLs will be entitled to appeal and have in fact appealed, against some dismissals.²⁸
59. Disregarding DB and BAWAG²⁹ (as the claims against them are proposed to be withdrawn as part of the compromise under the Scheme), he submits that there is still a non-fanciful risk that the JOLs could succeed against a defendant who could then bring a contribution claim against DPM (or against any other IC) for the full amount of the damages awarded – damages which in theory could be the full amount of the SPhinX claim in the New York Action.
60. In that event DPM (or any other IC) would be at risk for liability to the full extent of the shortfall in the Net Litigation Proceeds because only 2/3^{rds} of the damages awarded would have been available to the JOLs for retention following deduction of the Beus Gilbert contingency fees.
61. Until DPM's application for leave to appeal against the Jurisdiction Judgment and any subsequent hearing of that appeal are determined, Mr. Sheldon QC submits that this Court cannot be satisfied with the required degree of certainty that it has

²⁶ Most recently, on 7th August 2013, Special Master Capra issued a Report and Recommendation in which he recommended that summary judgment be granted in favour of DPM and Robert Aaron in respect of the JOLs outstanding claims. However, Judge Rakoff, the trial judge, is yet to decide whether to adopt the Report and Recommendation. If it is adopted, the JOLs would still however, be entitled to appeal that decision.

²⁷ Sixteen in all; namely: Piggott, Liberty Corner, Ingram Micro, CIM, Credit Suisse, Merrill Lynch, Chase Manhattan, the THL entities, Thomas H. Lee, Harkins, Jackel, Shoen, the EMF entities, Delta Flyer and Flanagan.

²⁸ The first four on the list in F.N. 26. According to a letter from the JOLs' Cayman lawyers dated 25 September 2013, there are also "tolling agreements" in place with 4 parties (including Walkers ((SPhinX's former Cayman lawyers)) and Gabriel Bousbib, an IC.

²⁹ BAWAG is a significant shareholder which was also a fiduciary services provider to SPhinX and thus entitled to a contractual indemnity and became an IC.

jurisdiction to sanction the Scheme or that any distribution made to SPhinX's shareholders/investors would not irremediably prejudice the interests of SPhinX's creditors. Accordingly, that I should adjourn the sanction petition pending the outcome of DPM's appeal. Otherwise, if the Court is satisfied that it has jurisdiction, the Court should, as a matter of discretion, only be prepared to sanction the Scheme or direct a distribution if one or more members of the LC are willing to provide a secured undertaking to make good any future shortfall that might arise in the Indemnity Reserve. Such an undertaking would ensure that the statutory order of priorities is maintained and that the risk of any shortfall lies, as it should, with the SPhinX shareholders/investors (as advised by Sir Andrew Morritt in the Jurisdiction Judgment³⁰).

Conclusions

62. Events have moved on significantly further in favour of sanction since the delivery of the Jurisdiction Judgment on 9th July.
63. The halving of the legal costs reserve, the income from PWC (U.S. and Cayman) and other settlements and the virtual elimination of the risk of a Beus Gilbert claim against the estate, are tangibles which should not be ignored as they operate to reduce the risk of the assets being exceeded by contingent claims.
64. In a rational consideration of that risk, it is crucial that the JOLs have undertaken, as part of the Scheme, to reserve the Net Litigation Proceeds that any such contribution claimant would first have had to pay to them.
65. The concern therefore becomes whether there is a risk that DPM (or any other IC) sued for a contribution, would be found liable to pay more than 2/3rds of the award

³⁰ Paragraph 102 of the Jurisdiction Judgment and as discussed at paras. 24-29 above.

back to the contribution claimant. Otherwise, barring the concerns over pre-judgment interests discussed above, the IC's exposure should be covered by the reserve of the Net Litigation Proceeds.

66. That any such risk exists is, in my view, a very unlikely proposition. Mr. Karlinsky, DPM's expert on New York litigation, could report of but a single case from the annals of New York litigation, where a contribution defendant in a case of breach of fiduciary duty like that alleged against the ICs, had been required to pay more than 2/3rds by way of contribution³¹. Those results of Mr. Karlinsky's survey are not surprising for by definition, a contribution is not the same as an indemnity³². It must indeed be highly exceptional in a case like this, for a defendant to be found culpably liable while at the same time entitled to be completely indemnified by another party found culpable of the same wrongdoing.
67. No less extreme to my mind, is the notion that pre-judgment interest on such potential contribution claims could so grossly accumulate as to lead to the outstripping of the reserves of the Net Litigation proceeds themselves.
68. After so many years of the pendency of the New York Action, I consider it very unlikely that any remaining defendant ordered to pay damages and who could bring a contribution claim against an IC, would not seek to do so immediately upon being found liable and upon paying the damages to the SPhinX estate. The scenario of a significant prejudgment period during which interest could accrue is therefore also so extremely unlikely as to be ignored.

³¹ In his evidence before Sir Andrew Morritt he identified the case, some 20 years ago, where the estate of singer/songwriter Bob Marley sued for breach of fiduciary duty and a contribution claimant recovered from another party more than 66% of the damages it had paid.

³² He spoke of four cases decided over the past decade in other categories (eg: involving wrongful death or environmental breaches) where contribution awards of more than 2/3rd were made but none involving a breach of fiduciary duty.

69. As to the risk that a contribution claim could be raised against DPM (or against any other IC) by a claimant who has not already been identified as a defendant to the New York Action, is also in my view, so very unlikely as to be ignored. The limitation period on direct claims for loss arising from the SPhinX collapse (and which could in turn give rise to contribution claims) has already expired and no such prospective defendant or contribution claimant can be identified by DPM.
70. The question thus comes down to whether there is a the real possibility of a contribution claim for more than 2/3rds of a damages award against a known defendant to the New York Action and so one likely to exceed the amount of the Net Litigation Proceeds.
71. When viewed objectively in the context of the present circumstances, while I may not say with absolute certainty³³ that no such risk exists, the chances of it arising has in my view crossed the threshold from the realm of reality into the fanciful.
72. I agree with the JOLs, (as stated at paragraph 31 of Margot MacInnis 30) that *“while the risk of a contribution claim is low...we see that it may still be theoretically possible for a contribution claim to be brought. However, within such a possibility it is difficult to see how the amount that would be contributed by DPM [(I would add “or any other IC”)] could be more than the 66% that the JOLs have agreed to hold back from the litigation proceeds.”*
73. I consider that the combined amount of the reserves for the legal costs and the Net Litigation Proceeds, will adequately cover any liability that could arise to an IC and represents *“a just estimate so far as is possible of the value of all such debts or*

³³ “Absolute certainty” is, of course, not the standard. As explained in the Indemnity Reserve Judgment (2010 (1) CILR 234) and acknowledged in the Jurisdiction Judgment, the court is obliged to set the reserves at “the maximum sums that might reasonably be incurred” to cover the liability of the estate to ICs.

claims”, within the meaning of section 139(1) of the Law and the “*maximum sums that might reasonably be incurred*” in that regard, being the test identified by the case law.

74. I proceed upon the basis of the conclusion reached at paragraph 100 of the Jurisdiction Judgment³⁴.
75. When the sum of the reserves of USD138,918,394 is taken with the Net Litigation Proceeds from the settlements attained since then (USD67 million), the result is a reserve of USD206 million (approx.). That figure itself is to be regarded as containing an additional buffer of USD71 million in light of the reduction in legal costs generated by the settlement but which had been factored into the reserves of USD138,918,394 set by the Jurisdiction Judgment.
76. The JOLs should nonetheless proceed on the basis of reserves of at least USD206 million until further order.
77. I also conclude that in the now known circumstances of the SPhinX estate and the New York Action, it would be both unfair and impracticable to impose, as a condition of sanction, a requirement that an investor or investors undertake to repay any shortfall, in order to obtain dividends to which there would otherwise be an entitlement.

Proposed Modifications to the Scheme

78. Since the Scheme was first circulated in November 2011 and approved by scheme participants at the Court Meetings held in December 2011, it has become clear that the Scheme requires various minor modifications. These fall into the following groups:-

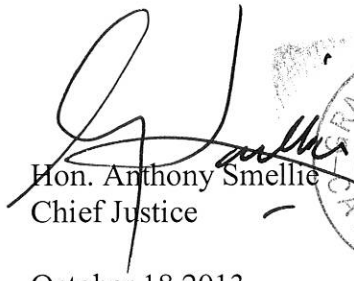
³⁴ See paragraphs 9 and 10 above.

- (1) Modifications which are the outcome of discussions between the JOLs, the ICs and the LC, and which are intended to address concerns raised by the ICs;
- (2) Modifications which will be necessary if the Indemnity Reserve Ruling pre-dates the Bar Date, by virtue of a direction authorizing a distribution (contrary to the timing assumptions in the original Scheme);
- (3) Modifications proposed by hfc (a significant shareholder) to enable hfc (and possibly DB) to make *a revised Cash Out Offer* to other Scheme participants at an increased rate, to which the JOLs have no objections;
- (4) Modifications to increase the cap on the sum to be paid to DB and hfc (as the two initial promoters of the Scheme) in respect of their Scheme costs from US\$1 million each to US\$1.7 million each;
- (5) Modifications to correct typographical and other errors in the drafting of the Scheme; and
- (6) Modifications identified as necessary around the time that the original Scheme was circulated. Most of these were mentioned in Margot MacInnis' 15th affidavit dated 22 December 2011. The need to amend the list of experts in Appendix 9, which had been agreed between the JOLs, hfc and the LC in November 2011, was overlooked when that affidavit was sworn.

79. It was submitted by Ms. Bryant QC and I accept, that the Court can make these modifications without re-convening Court Meetings to consider the modified Scheme, provided the Court is satisfied that no reasonable investor would change their decision as to how to act on the Scheme if the modifications were to be circulated: *Re Jessel Trust plc* [1985] BCLC 119 and *Re Minster Assets plc* [1985] BCC 99,299 both as considered and applied in the December 2012 Judgment.

80. I accept that none of the proposed modifications would have prompted the reasonable investor to vote differently on the Scheme had they been notified of them, and that it is appropriate for the Court to sanction the Scheme with the proposed modifications.

81. Being satisfied that the jurisdiction continues to exist as declared by the Jurisdiction Judgment, I grant sanction of the Scheme, modified as proposed.


Hon. Anthony Smellie
Chief Justice



October 18 2013