



**IN THE GRAND COURT OF THE CAYMAN ISLANDS**

**FINANCIAL SERVICES DIVISION**

**CAUSE NO: FSD 108 OF 2019 (NSJ)**

**IN THE MATTER OF THE COMPANIES ACT (2022 REVISION)**

**AND IN THE MATTER OF DIRECT LENDING INCOME FEEDER FUND, LTD. (IN OFFICIAL LIQUIDATION)**

**Before: The Hon. Mr. Justice Segal**

**Appearances: Mr Tom Smith KC instructed by Matthew Dors and Rupert Stanning of Collas Crill for the Joint Official Liquidators of Direct Lending Income Feeder Fund, Ltd (in official liquidation)**

**Ms Annelise Day KC instructed by Mourant for the Eiffel eCapital US Fund, Eiffel eCapital Global Fund & Pretons Ensemble 2**

**Mr David Lewis-Hall of Appleby for the Liquidation Committee**

**Mr. Kai McGrielle of Bedell Cristin for the Bedell Cristin Funds**

**Heard: 21 September 2022**

**Draft judgment circulated: 3 November 2022**

**Judgment delivered: 10 November 2022**



## CMC JUDGMENT

### Introduction

1. This judgment deals with directions sought by the joint official liquidators (*JOLs*) of Direct Lending Income Feeder Fund, Ltd (in official liquidation) (*DLIFF*) in relation to the conduct of proceedings commenced by a summons filed by the JOLs on 23 February 2022 (the *Summons*). The directions are designed to establish the procedure leading to a hearing at which the Court will determine the first set of issues raised in the Summons (referred to as the *Priority Relief*).
2. The JOLs initially applied for directions relating to service of the Summons on DLIFF's investors (the *Investors*). That application was dealt with on the papers. On 9 May 2022 (following the filing of further information and submissions by the JOLs during April 2022) I handed down a ruling (the *Ruling*) dealing with service and, on the same date, an order (the *Order*) was made giving directions for service.
3. The Summons was served on Investors in order to give them an opportunity to come forward and make submissions and to participate in the proceedings should they wish to do so. A case management conference (*CMC*) was listed on 21 September 2022 for the purpose of giving further directions.
4. Following the service of the Summons, a number of Investors have come forward. In addition, the JOLs have applied to amend the Summons, set out the directions they ask the Court to give at the CMC and filed further evidence. The additional evidence is contained in Mr Christopher Johnson's Fifteenth Affidavit (*Johnson 15*) and his Sixteenth Affidavit (*Johnson 16*). These affidavits supplement Mr Johnson's Tenth Affidavit (*Johnson 10*) which was filed at the time of the Summons. The JOLs also relied on the First Affidavit of Mr Glenn Kennedy (*Kennedy 1*), a director of MASECO Asset Management Limited, which is the investment adviser to Maseco Alternative Credit Fund SP (*MACF*). MACF is a member of DLIFF's liquidation committee (the *LC*). Mr Kennedy's affidavit deals, on behalf of the LC, with the procedural issues raised by the summons filed by Eiffel eCapital US Fund (*Eiffel*), which I discuss below.

5. In Johnson 15 (at [13]-[15]), Mr Johnson explained that, following and in light of the Ruling, the JOLs had decided to make amendments to, and now sought leave to amend, the Summons to make it clear that the relief they seek is directed to the exercise by the JOLs of their powers. An amended version of the Summons was exhibited at pages 1-4 of the exhibit to Johnson 15 (the *Amended Summons*). The Amended Summons also sets out the further directions (the *Further Directions*) that the JOLs now seek. The JOLs wish to structure the application for the Priority Relief as an application made by them for directions on the terms set out in the Amended Summons. The JOLs will appear and advocate for those directions while Investors will be permitted to appear to oppose the orders sought by the JOLs.
  
6. On 12 September 2022 a summons (the *Eiffel Summons*) was filed by Eiffel. Eiffel, Pretons Ensemble 2 and Eiffel eCapital Global Fund (the *Eiffel Funds*) were shareholders of DLIFF who gave notice to redeem their shareholding on 21 November 2018 but who have not yet been paid the redemption proceeds which they claim are owed to them (parties in the position of the Eiffel Funds have been referred to by the JOLs as *Late Redeemers* and I shall adopt that definition in this judgment). The Eiffel Funds have filed proofs of debt in the liquidation (on 27 September 2019) but the JOLs have not yet adjudicated the proofs. Eiffel considers that the JOLs' approach as set out in the Further Directions is unfair and unsatisfactory and therefore it opposes the JOLs' application for directions. Eiffel has put forward an alternative approach in the Eiffel Summons. Eiffel argues that the application should be structured as an *inter partes* proceeding between the competing classes of Investors, that representatives be appointed to represent each relevant class to appear on the application, that Eiffel be appointed to represent the Late Redeemers (to oppose the orders permitting creditors who claim damages for misrepresentation to prove and rank *pari passu* with other creditors, as discussed further below), and that the Court should make pre-emptive costs orders now in favour of the representatives. The evidence filed in support of the Eiffel Summons was the First Affidavit of Mr Olivier Villedey (*Villedey I*) (Mr Villedey is a director of Eiffel eCapital GP Sarl, the general partner and liquidator of Eiffel). In addition, Ms Loren Bowerman of Campbells swore an affidavit in order to adduce into evidence a letter to the Court dated 14 September 2022 from Sirius Investments SICAV, acting on behalf of Sub-Fund Reserva (*Sirius*) in which Sirius confirmed its support for the relief sought by Eiffel.

7. At the hearing of the CMC, Tom Smith KC (instructed by Collas Crill) appeared for the JOLs and Anneliese Day KC (instructed by Mourant) appeared for Eiffel. In addition, Mr David Lewis-Hall of Appleby appeared on behalf of the LC and Mr Kai McGriele of Bedell Cristin appeared on behalf of Sparkasse Bank Malta PLC-AIF Account (*Sparkasse*) and Mitsubishi UFJ Investor Services & Banking Luxembourg (together the *Bedell Cristin Funds*). Ms McKenzie of Bedell Cristin had sworn an affidavit in order to adduce into evidence a letter to the Court dated 20 September 2022 from Mr Jonathan Scott on behalf of Sparkasse and Mitsubishi. In that letter, Mr Scott explained that the Bedell Cristin Funds' preliminary position was that they did not object to Eiffel being appointed as the representative for the Late Redeemers and were themselves considering whether to act as the representative for another class of Investors, the Late Subscribers (which I explain below). The Court also received a letter dated 21 September 2021 from Carret Lumen Specialty Credit Fund SP confirming that it had instructed Bedell Cristin in relation to DLIFF and, as I understand it, Mr McGriele also appeared on their behalf. Campbells, acting for Sirius, were in attendance at the hearing.
  
8. In summary, my conclusions are as follows:
  - (a) the JOLs' sanction application (by way of an application for directions) in relation to the Priority Relief and orders sought in [4] and [5] of the Amended Summons in respect of the claims made or to be made by Investors claiming damages for misrepresentation (which I define below as the Misrepresentation Orders) should be treated as one for the benefit of the JOLs and the estate that can properly be conducted without the need for an *inter partes* proceeding and that the JOLs may advocate in favour of the making of the Misrepresentation Orders and Eiffel can be joined as a party for the purpose of opposing the making of the Misrepresentation Orders on the basis that Eiffel's reasonable costs should, subject to fee rates for Eiffel's counsel and attorneys being agreed by the parties or subsequently determined by the Court, be paid by DLIFF as an expense of the winding up.



- (b). the JOLs' sanction application in relation to the Priority Relief and orders sought in [6] and [7] of the Amended Summons in respect of the status and rights of the Late Subscribers (who are identified and defined below and which orders I define below as the Late Subscribers Contract Orders) be adjudicated as an *inter partes* proceeding between a Late Subscriber and an Investor who is not a Late Subscriber.
- (c). Eiffel's application for the Court to determine a preliminary issue be dismissed.

### **The application to amend the Summons**

9. The application to amend was not opposed and in the circumstances there can be no objection to the JOLs making changes to the form of the orders they seek from the Court. I shall therefore give leave to make these amendments and shall, when considering the JOLs' application generally, refer to and use the wording now contained in the Amended Summons.

### **The Further Directions**

10. Johnson 15 sets out the Further Directions as follows:

*"38.2.A hearing to determine the Priority Relief (as defined in the JOLs Amended Summons) (Priority Relief Hearing) shall be listed on the first available date after 19 December 2022 with a time estimate of 2 days;*

*38.3. The JOLs' role at the Priority Relief Hearing shall be to advocate for the grant of the Priority Relief;*

*38.4. Any Investor wishing to rely upon evidence in answer to Johnson 10 relating to the Priority Relief shall file such evidence by 7 October 2022;*

*38.5. The JOLs' evidence in reply (if any) shall be filed by 21 October 2022;*

*38.6. The JOLs' skeleton argument regarding the Priority Relief shall be filed by 4 November 2022;*

38.7. *Any Investor intending to appear at the Priority Relief Hearing shall file a skeleton argument in answer to the JOLs' skeleton argument by 18 November 2022;*

38.8. *The JOLs' skeleton argument in reply (if any) shall be filed by 2 December 2022;*

38.9. *Hearing bundles shall be filed no later than 2 weeks before the hearing date;*

38.10. *The Investors appearing at the Priority Relief Hearing shall ensure that there is no duplication in skeleton arguments and oral submissions;*

38.11. *This order, the [Amended Summons] and any evidence and skeleton arguments filed in accordance with paragraphs 1 – 8 above shall be a. served (by the same deadline as for filing) on the JOLs, the Liquidation Committee and on any Investor who has provided a completed Notice of Appearance to the JOLs confirming its intention to appear on the Application; and b. circulated by the JOLs to the Investors by email as soon as reasonably practicable.”*

11. As can be seen, the JOLs consider that the procedure to be adopted is an application by them for directions regarding the manner in which they should adjudicate proofs filed in the liquidation. The JOLs will argue in support of the directions and ask the Court to make the orders set out as Priority Relief in the Amended Summons (which I describe below). Investors will be given the opportunity to appear and oppose the application and seek alternative orders. The JOLs do not consider that it is appropriate, for reasons I shall explain, to structure the application as an *inter partes* hearing between competing Investors or classes of Investors or that any Investors who appear should be formally appointed as representatives of any class of Investors or granted pre-emptive costs orders.

### **The relief sought in the Summons – an overview**

12. In the Ruling I summarised the relief sought in the Summons as follows:

“1. *I have before me a summons dated 23 February 2022 a summons (the **Summons**) issued by the joint official liquidators (**JOLs**) of Direct Lending Income Feeder Fund, Ltd (in official liquidation) (**DLIFF**). The Summons seeks declarations relating to the claims of investors in DLIFF. These declarations concern the status and validity of claims made or to be made by investors against DLIFF based upon alleged misrepresentations by DLIFF in relation to the investors’ subscription for their shares (the **Misrepresentation Claims**) and separately claims by investors who sought to redeem their shareholdings in DLIFF with effective redemption dates*

prior to 8 February 2019 but who have not been paid the redemption price (the **Redemption Claims**). In support of the Summons, the JOLs filed the tenth affidavit of Christopher Johnson (**Johnson 10**), one of the JOLs, which sets out the background and gives details of the investors (see [20.2]).

2. The first part of the Summons sought case management directions for the conduct of the proceedings. On 23 February 2022, the JOLs' attorneys (**Collas Crill**) wrote to the Court and applied for directions in the terms set out in paragraphs 1 to 3 of the Summons. They sought directions that (a) the JOLs serve the Summons (with supporting documents) on all investors by email within 14 days of the date of the order; (b) any investors who wished to appear on the Summons be required to serve a notice of appearance with a statement of position within twenty-eight days of service of the Summons on them and (c) a case management conference be listed on the first available date no less than ten weeks after the date of order. Collas Crill requested that the application be dealt with on the papers without a hearing.
3. The subsequent parts of the Summons seek declarations relating to the rights of investors. Paragraphs 4-7 seek declarations (referred to as **Priority Relief**) with respect to the Misrepresentation Claims including a negative declaration that such claims "are not barred as a matter of law solely due to the fact that DLIFF is in liquidation"; a declaration that admitted Misrepresentation Claims "would be payable in the liquidation of DLIFF *pari passu* with any admitted redemption claims"; a declaration that "valid and binding contracts were entered into between DLIFF and each respective investor (each a **Late Subscriber**) in relation to funds received from investors for subscriptions effective 1 January 2019 and 1 February 2019 such that DLIFF did not hold the funds received from those investors on trust pending completion of those subscription contracts and was entitled to treat those funds as assets of DLIFF" and a declaration that the "JOLs be directed to treat the Late Subscribers as members of DLIFF for the purpose of distribution of DLIFF's assets." Paragraphs 8-9 seek declarations (referred to as **Subordinate Relief**) relating to the Redemption Claims, and the potential obligation on the JOLs to rectify DLIFF's register of members."

### The Priority Relief

13. The orders that the JOLs wish the Court to make by way of Priority Relief are set out in the Amended Summons as follows:

- "4. An order that the JOLs be directed to exercise their function of adjudicating claims on the basis that any claims from investors of DLIFF based upon asserted misrepresentations by DLIFF in relation to their subscriptions for shares in DLIFF are not barred as a matter of law solely due to the fact that DLIFF is in liquidation;
5. An order that, in the event that any claims from investors of DLIFF based upon asserted misrepresentations by DLIFF in relation to their subscriptions for shares

- in DLIFF are admitted, then the JOLs be directed to pay such claims pari passu with any admitted redemption claims;*
6. *An order that the JOLs be directed to exercise their function of adjudicating claims on the basis that valid and binding contracts were entered into between DLIFF and each respective investor (each a **Late Subscriber**) in relation to funds received from investors for subscriptions effective 1 January 2019 and 1 February 2019 such that DLIFF did not hold the funds received from those investors on trust pending completion of those subscription contracts and was entitled to treat those funds as assets of DLIFF;*
  7. *An order that the JOLs be directed to treat the Late Subscribers as members of DLIFF for the purposes of the distribution of DLIFF's assets.”*

#### **The different types of stakeholder who have claims in the liquidation**

14. In Johnson 10, Mr Johnson conveniently summarised the different categories of investors, creditors and stakeholders as follows:

“19. By way of a short overview, over the course of its trading life (October 2016) to February 2019), DLIFF accepted approximately US\$287.7m in subscriptions (including the Late Subscribers) and paid out approximately US\$128.3m in redemptions and monthly distributions. These redemptions include those of investors who were fully redeemed prior to December 2018 (who, in effect, withdrew from the fund with an aggregate of US\$4.7m net profit). DLIFF’s net investment value by reference to the remaining Investors (but excluding redemption requests effective after 30 November 2018) is therefore approximately US\$164.1m. As noted above, its last stated NAV (for 30 November 2018) was approximately US\$180m. However, as will be addressed below in more detail, the JOLs have good cause to believe that the NAV was materially mis-stated for much, if not all, of the life of DLIFF. For that reason, the JOLs consider it more appropriate to refer to investment values by reference to net investment.

20. The stakeholders of DLIFF can be most conveniently categorised as set out below:

20.1 unsecured, third-party creditors who were not investors of DLIFF, such as former service providers (**Trade Creditors**) [who will be paid in full in any event];

20.2 DLIFF’s current investors (**Investors**), comprising the following sub-groups:

- a) those Investors who sought to redeem their shareholding in DLIFF with effective redemption dates prior to the suspension of withdrawals and voluntary redemptions on 8 February 2019 (**Suspension Date**), but who remain unpaid (**Late Redeemers**); and



- b) *those Investors who provided cash to DLIFF in respect of either initial or additional subscriptions for shares in DLIFF with subscription dates of 1 January 2019 or 1 February 2019 (**Late Subscribers**);*
- c) *those Investors not falling into the above two categories (**Unredeemed Investors**)”*

15. Mr Johnson also noted (in footnote 7 to Johnson 10) that:

*“It should be noted that these groups are not mutually exclusive: an Investor could be, for example, a Late Subscriber in respect of part of its investment, and an Unredeemed Investor in respect of the remainder. Further, certain of the Late Redeemers only sought to redeem part of their shareholding in DLIFF with effective redemption dates prior to the Suspension Date, and so, at least to some extent of their investments, are also categorised as Unredeemed Investors.”*

16. Accordingly, there are three main groups of Investors. After the last NAV was struck on 30 November 2018 but prior to the suspension of redemptions on 8 February 2019, there were various redemption requests received from Investors. These are the Late Redeemers. There is also a category of Investors who subscribed for shares in DLIFF in January and February 2019. These are the Late Subscribers. In addition, there is a broad category of Investors who simply remained invested in DLIFF. They are the Unredeemed Investors. All other things being equal, the Late Redeemers would be paid in full first as creditors, and the Unredeemed Investors, as shareholders, would then be paid from any remaining assets by reference to their shareholdings, as recorded in the register of members at the date of commencement of the liquidation. However, there are three main issues which may in this case give rise to a deviation from that position:

- (a). the first is whether some or all of the Unredeemed Investors have claims for damages for misrepresentation against DLIFF in respect of their share subscriptions, in relation to which they would be creditors of DLIFF.
- (b). the second issue is whether the register of members of DLIFF would fall to be rectified so that distributions by the JOLs to shareholders are made not by reference to the recorded shareholdings of each shareholder in the register, but rather by reference to their net cash

investments into DLIFF. The JOLs explained that typically in the United States, in the case of a fraudulent investment fund like DLIFF distributions are made by reference to the net cash invested by each investor. The reason for this approach is that it is considered to be a fairer method of distribution, rather than a method that relies on the register of members, which typically would include an element of fictitious profit. This is because the prices at which Investors subscribed for and redeemed their shares in the case of a fraudulent fund will include fictitious profits which have been improperly reported by the fund. If distributions are made by reference to the net cash invested by each investor, a further issue arises as to which method for making distributions on a net cash basis should be used. The one that is typically used is called the rising tide methodology. That in summary provides for a distribution to be made based on net cash investments subject to an adjustment involving catch-up payments to those investors who did not receive redemptions from the fund. Accordingly, the methodology aims to equalise the position of investors who did not make withdrawals and receive any redemptions prior to the collapse of the fund with the position of those who were lucky enough to make withdrawals and receive redemptions. It seeks to achieve this by first adjusting investors' net cash position by bringing the investors who did not receive redemptions prior to the collapse up to the same level (in terms of redemptions received) as those who did receive redemptions, and thereafter making distributions to everyone on a *pro rata* basis by reference to their adjusted net cash position. As a matter of Cayman law, there is a power under the Companies Act (2022 Revision) (*Companies Act*) and the Companies Winding Up Rules (*CWR*) given to the official liquidator of a solvent, open-ended investment fund to rectify the register of members. The JOLs consider that it may well be appropriate in this case to exercise that power to allow for a distribution by reference to net cash investments applying the rising tide methodology. The JOLs have noted that it is almost certainly the case that there will not be sufficient assets in the liquidation estate to meet the claims of all Investors in full, so that issues of distribution priority are of some practical importance.

- (c). the third issue is whether the subscriptions of the Late Subscribers were valid, and whether they become shareholders in return for their subscriptions or whether they are to be treated as beneficiaries under a trust of their subscription monies or unsecured creditors.



## The JOLs' discussions with Investors

17. Mr Johnson provided an account of the JOLs' engagement with Investors in Johnson 15 (at [7]-[12]) and exhibited (in exhibit CDJ-15B at pages 1-4) a copy of a confidential schedule (the *Investor Schedule*) which listed each of the Late Subscribers, the Late Redeemers, the Investors who were paid funds upon the redemption of shares prior to the appointment of the Receiver (*Prior Redeemers*) and the Unredeemed Investors known to the JOLs. Mr Johnson summarised the position as follows (underlining added):

- “7. *On 19 May 2022, pursuant to the [Order], the JOLs served copies of the Summons, Johnson 10, CDJ-10, and the [Order] on the members of the Liquidation Committee (LC)....*
8. *On the same day, the JOLs also sent emails to all Investors enclosing copies of the documents served on the LC members as well as a consent form for sharing details (and anonymised list of Investors) as well as a Notice of Appearance and Statement of Position Form..... The purpose of the consent form was to encourage participation amongst the Investors and to assist Investors with similar rights and/or interests to expedite the process of consideration and coordination of legal representation. The purpose of the Notice of Appearance and Statement of Position Form was to assist the JOLs and the participating Investors in the consideration and coordination of directions.*
9. *As at 29 August 2022, only fourteen Investors have provided completed consent forms. Those Investors have been provided with a confidential schedule (**Investor Schedule**) which includes contact details of other consenting Investors as well as categorisation and net investment information. It remains anonymised in respect of those Investors who have not consented to the sharing of their identity and contact details....*
10. *As at 29 August 2022, ten of the sixty-one Investors have provided Statements of Position,... Of those ten respondents, just six (three of whom are under mutual control) have instructed counsel to appear. The three affiliated Investors are all Late Redeemers and are identifiable as Investors LR1, LR2 and LR4 on the Investor Schedule. One other Late Redeemer intends to appear and is identifiable as Investor LR3. The other two participating Investors are affiliated (and thus currently represented by the same counsel) and are identifiable as Investors LS1 and UI7.*
11. *Four Investors have completed Statements of Position but have not (to date) expressed an intention to appear on the Application. The JOLs have communicated with these four Investors to ascertain whether they wish to engage counsel to appear*

*on the Application. All of these Investors have indicated that they have not instructed counsel because they are concerned about the costs of doing so and/or they support the relief for which the JOLs are advocating.*

12. *The Investors' responses as recorded in the Statements of Position are summarised in the table below [the table refers to issues 1-4, which are the issues as defined in the notice of appearance and statement of position document sent to Investors and reflect paragraphs 4-7 in the Amended Summons]:*

	Number of Investors in support	Number of Investors in opposition	Number of Investors neutral
Issue 1	6	4	0
Issue 2	4	6	0
Issue 3	2	4	4
Issue 4	1	4	5

18. The Investor Schedule revealed that there were nine Late Subscribers, six of whom had not responded to the JOLs' request to allow their identity to be disclosed; five Late Redeemers one of whom had not responded to the JOLs' request to allow their identity to be disclosed; nineteen Prior Redeemers, only two of whom had responded to the JOLs' request to allow their identity



to be disclosed and twenty eight Unredeemed Investors only five of whom had responded to the JOLs' request to allow their identity to be disclosed.

### Misrepresentation Orders

19. I shall refer to the draft orders set out in paragraphs 4 and 5 of the Amended Summons as the **Misrepresentation Orders** (and the issues raised by the application for the Misrepresentation Orders as the **Misrepresentation Issues**). The JOLs explained the background to and context of the application for the Misrepresentation Orders in Johnson 10 as follows:

- “24. *The first issue of universal application, which has potentially the most significant effect, is the manner in which the business of the DLI Group (including DLIFF) was conducted, and the associated repercussion for the rights of the Investors.*
25. *As can be seen from the Receivers' Report dated 13 November 2020 (the November 2020 Report), the Receiver's investigations have led him to conclude that the DLI Group was operated as a fraud from inception by Mr Ross. As is explained in more detail below, this conclusion is shared by me, in my capacity as the Cayman JOL, following a review by my team of the investigations undertaken by the Receiver.*
26. *Certain Investors have alleged claims based on misrepresentation, and some others have, more nebulously, asserted fraud against DLIFF and/or its former managers. The JOLs' provisional view is that most (or possibly all) of the Investors will be able to reasonably argue that they have claims based on misrepresentation and that such claims are payable in priority to any distribution of capital to Investors (and on a pari passu basis with the claims of the Late Redeemers, should those claims be maintained).*
27. *The JOLs' current view is that it is (at the very least) reasonably arguable that Investors representing at least 75% of the existing issued shares (by net investment value) have prima facie claims for damages for misrepresentation against DLIFF in connection with the inducement of their investments into DLIFF. However, as addressed below in more detail, it is unclear whether or not such claims are available as a matter of law, now that DLIFF has entered liquidation.*
28. *If claims based on misrepresentation are (a) available as a matter of law and (b) payable in priority to the return of capital to members (whether ahead of or pari passu with the debts of unsecured creditors or subordinated debts), this would have a significant impact on the distributions. It might also prompt the Late Redeemers to reformulate their claims.”*



20. The JOLs consider that the Misrepresentation Orders are needed in order to provide clarity and certainty in relation to the legal position of Investors who have asserted or wish to assert claims based in misrepresentation and the relative priority of such claims (if admitted).
21. Mr Johnson explained (Johnson 10 at [62]-[63]) that while many Investors had yet to make or allege claims based on misrepresentation, some had done so and others had asserted that the NAVs relied on and used by DLIFF were not binding by reason of internal fraud, by reference to the decision of the Privy Council in *Skandinaviska Enskilda Banken AB v Conway* [2019] UKPC 36. Despite this limited response, the JOLs considered that it was likely that most, if not all, of the Investors will be able credibly to argue that their investments were only made due to misrepresentation on the part of DLIFF. Therefore, the JOLs were satisfied that they would need to deal with a large number of proofs based on claims for damages for misrepresentation.
22. The JOLs noted that Investor claims based on misrepresentation will raise issues of both fact and law. As regards the facts, the JOLs have reviewed the Receiver's November 2020 report and undertaken their own investigation and considered whether there were fraudulent misrepresentations, whether they were communicated to investors and whether knowledge of the fraud could be attributed to DLIFF. They had concluded that there was a *prima facie* case that the significant majority of DLIFF's Investors received the types of misrepresentations identified in the Receiver's report prior to making their initial investments into DLIFF. They also considered there was at least a *prima facie* case that the knowledge of the main perpetrator of the fraud, Mr Ross, a director of DLIFF at all material times, would be attributed to DLIFF.
23. These factual issues will not need to be dealt with on the application for the Misrepresentation Orders. Instead, the application will raise two significant legal issues. The JOLs referred to these as availability and priority.
24. In relation to availability, the JOLs said that they had been advised that there was an open question under Cayman Islands law as to whether a shareholder who had been induced by a misrepresentation to subscribe for shares can claim damages against a company in liquidation. They noted that the English Courts at the highest level had held that a shareholder who had been

induced to subscribe for shares by reason of a fraudulent misrepresentation was unable to rescind the subscription agreement after the commencement of a winding up (*Houldsworth v City of Glasgow Bank* (1880) 5 App Cas 317 (HL) (*Houldsworth*)). However, they had been advised that it was arguable that the decision in *Houldsworth* was inconsistent with the effect of section 14 of the Contracts Act (which is in similar terms to section 2(1) of the English Misrepresentation Act 1967), which clearly permitted a claimant to sue for damages for misrepresentation without rescinding the contract and that *Houldsworth* was therefore no longer good law or could be distinguished on the basis that it pre-dated section 14 of the Contracts Act (and section 2(1) of the 1967 Act).

25. In relation to priority, the issue was whether any damages for misrepresentation, if admissible, were subordinated and ranked after the claims of other creditors. The answer to this question depended on the proper construction and effect of section 49(g) of the Companies Act and the relationship between that section and section 37(7) of the Companies Act.
26. Section 49(g) of the Companies Act deals with the priorities of certain types of claims and provides:

*“no sum due to any member of a company in that person's character of a member by way of dividends, profits or otherwise, shall be deemed to be a debt of the company, payable to such member in a case of competition between that person and any other creditor not being a member of the company; but any such sum may be taken into account for the purposes of the final adjustment of the rights of the contributions amongst themselves”*

27. The English equivalent to section 49(g) of the Companies Act was section 74(2)(f) of the English Insolvency Act 1986, and this section had been considered by the House of Lords in *Soden v British & Commonwealth Holdings plc* [1998] AC 298. The issue in that case concerned the priority within the liquidation of a claim by the company's shareholder for damages for misrepresentation. In particular, the shareholder alleged that misrepresentations made by the company had induced it to acquire the shares in the company from a third party. The House of Lords held that this claim did not fall within the scope of section 74(2)(f). However, it had been held in earlier cases, not overruled by the House of Lords in *Soden*, that where the shares were not acquired from a third party but were issued and allotted by the company itself, the section applied to the damages claim (see *Re Addlestone Linoleum Company* (1887) 37 Ch D 191 and in Australia in *Webb Distributors (Pty) Ltd v State of Victoria* (1993) 11 ACSR). The JOLs had

therefore concluded that it was likely that any claims based on misrepresentations by DLIFF in connection with the subscription for, and issue of, shares in DLIFF (save for those acquired from a third party) fell within the scope of section 49(g) and will therefore be subordinated to the claims of unsecured creditors and rank *pari passu* with those of the Late Redeemers.

28. The JOLs considered that the interests of the estate will be best served by the JOLs applying and advocating for the Misrepresentation Orders. Investors who wish to oppose the making of the Misrepresentation Orders will have the opportunity to do so. If the Misrepresentation Orders were made, the JOLs would then send out proof of debt forms to all Investors and allow those who wished to file an amended proof of debt in light of the Court's decision to do so. If upon review of the proofs of debt received, the JOLs considered that there were likely to be valid claims for damages for misrepresentation in amounts that exceeded, in aggregate, the value of the assets available for distribution, then the JOLs will change their solvency determination to insolvent.

### **Late Subscriber Contract Orders**

29. I shall refer to the orders set out in paragraphs 6 and 7 of the Amended Summons as the ***Late Subscribers Contract Orders*** (and the issues raised by the application for the Late Subscribers Contract Orders as the ***Late Subscriber Issues***). The JOLs considered that there was an issue as to whether the subscription contracts of Investors who held pre-existing investments in DLIFF and had provided cash to DLIFF in respect of additional subscriptions for shares with subscription dates of 1 January 2019 or 1 February 2019 (referred to as the ***Pre-existing Late Subscribers***) were properly and fully completed such that the subscription monies paid were available to DLIFF (or, alternatively, were not completed so that the monies were not available to DLIFF but instead held on trust by DLIFF for the benefit of the Pre-existing Late Subscribers). Essentially, they say, the question is one of contract formation.
30. Mr Johnson (in Johnson 10 ([116]-[138])) explained that the JOLs understood from DLIFF's constitutional documents, books and records that its practice was to create a new series of shares each month. For each new series, the initial subscription price was US\$1,000 per share. Each further subscription by an Investor would be for shares in the same series as that initially allotted to them, but the share price at subsequent subscriptions was calculated by reference to DLIFF's



NAV at the relevant time. The usual subscription practice for DLIFF was for Investors to make a subscription request and send the subscription funds to DLIFF, for receipt of funds to be acknowledged by DLIFF, and then for acceptance to be subsequently confirmed by DLIFF by the issue of a formal contract note (*Contract Note*) by email and/or via the Opus investor portal. All Late Subscribers paid their subscription monies in full and received confirmation from DLIFF in the form of Contract Notes. The Late Subscribers who made subscription payments for the first time (with effective subscription dates of 1 January 2019 or 1 February 2019) received fully-completed Contract Notes, but the Contract Notes issued to the Pre-existing Late Subscribers did not confirm the number of shares allotted. The JOLs understood that these Contract Notes did not specify the number of shares allotted because at that time the calculation of the NAV for 1 January 2019 and 1 February 2019 was not undertaken which, based on the JOLs' understanding of DLIFF's share allotment practices, was a necessary step for allotting shares of any previous series to a particular Investor.

31. After undertaking a further review, the JOLs concluded that it was likely that all of the subscriptions by the Late Subscribers, including by the Pre-existing Late Subscribers, had been properly completed such that the subscription monies paid by them had become assets of DLIFF. Nonetheless, the JOLs consider that the position is not clear and that the arguments are finely balanced. Therefore, they consider that it is necessary to have the Court deal with and decide the point.

### **The status of the Late Redeemers**

32. There is also an unresolved issue as to whether the Late Redeemers (including Eiffel) are creditors of DLIFF. Mr Johnson stated in Johnson 16 (at [9]) that the “*JOLs accept that, in principle, the Late Redeemers... are creditors of the Fund for the unpaid redemption proceeds. However, this is subject to the question of whether there was at the relevant time an Available Cash Limitation (as defined in [DLIFF’s confidential explanatory memorandum dated September 2018]) and, if there was, what effect this had on the redemptions (or attempted redemptions) made by the Late Redeemers....*” In their skeleton argument, the JOLs noted that “*The Available Cash Limitation (as described in [DLIFF’s confidential explanatory memorandum dated September 2018]) operates as a gating provision, limiting the obligation of*

*DLIFF to meet redemption requests in circumstances of illiquidity. On its face, it provides that unsatisfied redemption requests shall be deemed made for the next Redemption Day for the unsatisfied amount. Given the circumstances in which [DLIFF and its affiliated funds] went into receivership in early 2019, there is a live question as to the combined effect of the Available Cash Limitation provision and the suspension of redemptions on 11 February 2019.”*

33. It appears that the extent to which Late Redeemers have claims against the estate, and therefore whether they are creditors at all, depends on the resolution of a number of open issues concerning the construction of DLIFF’s confidential explanatory memorandum dated September 2018 (the *CEM*). The CEM may have imposed a limit on DLIFF’s liability to pay redemption proceeds at the relevant time which would reduce or extinguish the claims of Late Redeemers.
34. However, the JOLs consider that it is not necessary or appropriate to deal with this issue in their directions application. This is because the outcome of the application for the Misrepresentation Orders may result in the issue relating to the Late Redeemers being of no practical significance. As I understand it, the JOLs say that if DLIFF remains solvent (because the claims of Investors based on misrepresentation are held not to be admissible, or the quantum of the admitted claims for misrepresentation does not result in DLIFF being insolvent) then it will not matter whether the Late Redeemers are to be treated as creditors or Unredeemed Investors. Mr Johnson explained the point in Johnson 10 (at [139]-[145]) (underlining added):

“139. *As noted above, six Investors who submitted redemption requests effective after 30 November 2018 but before the Suspension on 8 February 2019 remain unpaid. Of these, one sought to redeem a specific number of shares, one sought to redeem by reference to a specific value, and four sought to redeem the entirety of their shareholding.*

140. *In aggregate, the Late Redeemers claim in excess of approximately US\$33m. The majority of these claims by value are based upon the last NAV for DLIFF struck, which was for redemptions effective 30 November 2018, and also applied to subscriptions effective 1 December 2018 (November 2018 NAV). The JOLs do not consider that the November 2018 NAV is applicable to the Late Redeemers’ redemptions, but this is a point disputed by those relying on the November 2018 NAV.*

141. *Because the JOLs consider that the issues specific to the claims of the Late Redeemers might be rendered otiose, I have not in this affidavit gone into any*

significant detail in relation to the issues that will require determination in relation to these claims. However, to assist the Court, I give a brief summary below of the core issues that might require resolution in the future.

142. The JOLs understand that the views of the majority (by value) of the Late Redeemers regarding the NAV applicable to their redemption requests can be summarised as follows:

142.1 The NAV applicable to their redemption requests is the November 2018 NAV, giving them claims in the aggregate of approximately US\$33m; and

142.2 Even if the primary position as stated above is incorrect, and the JOLs are bound to strike the NAV for 31 December 2018 and 31 January 2019, the JOLs cannot take into account information that was only available after the relevant date.

143. The JOLs do not agree with this analysis and consider that the JOLs will need to strike the NAVs for 31 December 2018 and 31 January 2019 in order to determine the claims of the Late Redeemers (and in doing so should take into account information now known about conditions that existed at those dates). However, even if the majority Late Redeemers' positions on the NAV were correct, the JOLs also consider that it will be necessary to determine what obligation, if any, the JOLs are under to give effect to the entirety of the redemption process under the Articles and the CEM, including an assessment of whether there was, at the time, an Available Cash Limitation, and if so, what the consequence of an Available Cash Limitation means for the claims of the Late Redeemers.

144. The JOLs understand that Late Redeemers might take issue with the notion that the provisions of the CEM are binding and instead argue that they are of no legal effect against the Investors. The JOLs would not agree with this position if it were adopted: indeed, it appears to the JOLs that it is quite possible that the combination of the redemption restrictions and the suspension provisions as set out in the Articles and the CEM means that the Late Redeemers might be more properly categorised as Unredeemed Investors.

145. As noted above, it might be that these issues are rendered otiose by the determination in relation to misrepresentation claims. However, in the event that these issues are required to be determined by the Grand Court, the JOLs consider that the parties will need to address the Grand Court in respect of, *inter alia*:

145.1 The extent to which the CEM is of legal effect as against the Investors;



- 145.2 *The proper interpretation of the redemption and suspension provisions of the Articles and the CEM; and*
- 145.3 *The appropriate methodology to be adopted in relation to the determination of the 31 December 2018 NAV and 31 January 2019 NAV”*

### **The Eiffel Summons**

35. The Eiffel Summons (as amplified by the draft order filed by Eiffel) seeks orders that:
- (a). the Amended Summons be determined as an *inter partes* proceeding as between the relevant classes of creditors and contributories pursuant to CWR O.11, r. 3(3).
  - (b). prior to the determination of the Priority Relief, but only if the JOLs have not accepted that the Late Redeemers are to be treated as creditors, the Court should determine (as an *inter partes* proceeding between the JOLs and the Late Redeemers) whether the Late Redeemers are to be treated and rank as creditors or members/contributories (the ***Preliminary Issue***).
  - (c). Eiffel be appointed as a representative party on behalf of the Late Redeemers in relation to the Preliminary Issue (to seek an order that the Late Redeemers be treated as creditors) and to oppose the making of the Misrepresentation Orders.
  - (d). the Court appoint a representative party to represent the Unredeemed Investors to argue in support of the Misrepresentation Orders.
  - (e). the Court also appoint such person as it sees fit to represent the Late Subscribers and the Unredeemed Investors in relation to a final determination of the Preliminary Issue and the other aspects of the Priority Relief.
  - (f). the Court shall give appropriate directions for the determination of the Late Subscriber Issues and the application for the Late Subscriber Contract Orders.

- (g). Eiffel’s costs of representing the Late Redeemers be paid from the assets of the liquidation estate as an expense of the liquidation, to be taxed on an indemnity basis if not agreed.
  - (h). Eiffel’s costs of and occasioned by the Eiffel Summons also be paid from the assets of the liquidation estate as an expense of the liquidation, to be taxed on an indemnity basis if not agreed.
36. As can be seen, Eiffel does not say who should be appointed to represent the Unredeemed Investors in relation to the application for the Misrepresentation Orders or who should seek and oppose the Late Subscriber Contract Orders (although it is to be inferred from Eiffel’s request that the Court appoint a representative of the Late Subscribers that Eiffel has in mind that such representative would argue for, and the representative of the Unredeemed Investors would oppose, the Late Subscriber Contract Orders).

### **Eiffel’s submissions**

37. CWR O.11, r. 3(3) states as follows:

*“The Court may direct that, when a sanction application gives rise to an issue in respect of the substantive rights as between the company and any creditor or contributory or any class thereof, it shall be adjudicated as an inter partes proceeding as between shareholders, creditors or any class of shareholders or creditors (as the case may be), for which purpose the Court may*

- (a) *make a representation order and/or*
- (b). *direct that the official liquidator’s role shall be limited in such way as the Court thinks fit....”*

38. Eiffel noted that I had discussed CWR O.11, r. 3(3) in the Ruling and had said as follows:

*“(g). in addition, and importantly in this context, CWR O.11, r. 3(3) makes it clear that a sanction application can deal with, and makes provision for sanction applications which relate to, the rights of creditors or contributories against the company. It states that ...*

- (h). *sanction applications seeking directions regarding the manner in which official liquidators are to exercise their powers and conduct the liquidation and which determine the rights of creditors or contributories in the liquidation are not uncommon. But they do need to be properly structured and prepared. Ideally, the affected creditors or contributories will have been consulted in advance and at least a preliminary indication obtained before the proceedings are launched as to whether all the affected creditors or contributories have the same or similar rights or whether there are separate rights and classes, whether creditors or contributories have indicated a willingness to act as representatives and whether more than one representative will need to be appointed to represent different classes of creditors or contributories.*
- (i) *as my brief summary above makes clear, the Summons seeks declaratory relief that “gives rise to [issues] in respect of the substantive rights as between the company and any creditor or contributory or any class thereof.” Careful consideration, as I have explained, therefore needs to be given as to how investors are to be allowed to participate and be represented in the proceedings. Careful consideration also needs to be given as to how the declarations are formulated.”*

39. Eiffel submitted that in the present case the orders sought by the JOLs by way of Priority Relief plainly gave rise to issues which will affect substantive rights as between DLIFF and its creditors and the application for the Priority Relief should therefore be adjudicated as an *inter partes* proceeding.
40. Eiffel argued that the approach and procedure proposed by the JOLs was unfair to those Investors who would be adversely affected by and would need to oppose the orders sought by the JOLs by way of Priority Relief. The JOLs’ approach could not be said to be in the interests of justice. In relation to the Misrepresentation Orders, which were the orders of greatest interest to Eiffel, the JOLs would be arguing for orders that favoured the Unredeemed Investors and their costs would be paid in full out of the estate, while those Investors who wished to oppose those orders would only be permitted to appear on an individual basis at their own risk as to costs. The JOLs would be taking sides and adopting a position in favour of one set of Investors. Eiffel submitted that this was unfair to them and to Investors who would be adversely affected by the Priority Relief and that the Court should ensure that the application for Priority Relief was considered in a neutral way with the interests of both sides of the argument being equally represented and with equivalent costs protection.

41. Eiffel submitted that in order to achieve a fair and balanced approach, the application should be constituted and the Court should give directions for the application to be conducted as an *inter partes* proceeding between the affected Investors, with representatives of such Investors being appointed by the Court as provided for by and in accordance with CWR O.11, r. 3(3) and GCR O.15, r.12. Eiffel was prepared to act as the representative of the Late Redeemers provided that it was entitled to recover its costs of doing so from the assets of the estate on an indemnity basis (see *Villedey 1* at [36]). Eiffel had the support of a substantial percentage in value of the Late Redeemers.
42. Eiffel also argued that the Eiffel Funds needed to know whether they would be admitted as creditors before being able to oppose the making of the Misrepresentation Orders. It was only if they were admitted as creditors (as opposed to being treated as Unredeemed Investors) that it would be in the interest of the Eiffel Funds to oppose the making of the Misrepresentation Orders. If the JOLs were unable to admit the Eiffel Funds or confirm their status as creditors the Court should do so and it was only fair that the issues, summarised above, raised by the JOLs as to the effect of redemption restrictions and the suspension provisions in DLIFF’s articles and the CEM be decided by the Court as a preliminary issue before the Eiffel Funds were asked to oppose the granting of and before the Court adjudicated on the application for the Misrepresentation Orders.
43. GCR O.15, r.12(1) governs the appointment of representatives and is in the following terms:
- “Where numerous persons have the same interest in any proceedings.....the proceedings may be begun, and, unless the Court otherwise orders, continued, by or against any one or more of them as representing all of as representing all except one or more of them....”*
44. Eiffel relied, in support of its application for a representation order, on the judgment of Chief Justice Smellie in *In re SPHinx Group* [2010] 2 CILR 1 (*SPHinx*). Eiffel submitted that the present case was on all fours with *SPHinx* and that similar orders to those made in *SPHinx* should be made here.
45. In that case the joint official liquidators of *SPHinx* applied to the Court (with investor support) (*inter alia*) for orders for the appointment of parties to represent certain classes of investors who were interested in the resolution of certain issues which had been identified for resolution by the

Court and for pre-emptive costs orders to cover the reasonable legal costs to be incurred by the representative parties. The issues related to the ownership of assets and responsibility for liabilities (since there had been co-mingling of the assets and liabilities of the SPhinx companies), issues as to the ranking of claims in the liquidations, including issues as to the status of certain shares, the suspension of redemptions, the redemption of shares and net asset value calculations, the validity of the redemption requests and whether misrepresentation claims by investors ranked as creditor claims. The Court granted the joint official liquidators' application. At [29] and [31] the Chief Justice said this:

*“being satisfied that the issues need to be resolved in an orderly sequence in order to enable the proper administration of the liquidation, it also becomes necessary to ensure that interested parties (investors/shareholders and creditors) who will be affected and bound by the court’s determination of the issues are made respondents to the respective issues so that they can be heard on the arguments. It is ultimately to this end that it is necessary and suitable that representative parties be appointed to represent parties having that commonality of interest.”*

.....

*The critical requirement for the appointment of a representative, it must be emphasized is that a number of persons have common interests and will benefit in common from the relief sought”*

46. Eiffel also drew the Court’s attention to the following passage in the Chief Justice’s judgment (at [34]) which Eiffel submitted demonstrated the undesirability of adopting the approach proposed by the JOLs in this case (underlining added):

*“As an alternative to the approach of appointing representative parties, it has been suggested by some blocking investors that the JOLs should take a position in relation to each of the issues and dissenting investors would be at liberty to challenge that position at their own risk as to costs. For among the obvious disadvantages that the approach would force the JOLs to take an adversarial position on one side or the other of the issues, it was not, to my mind, an acceptable approach. Another obvious disadvantage which that approach would create—compared with the appointment of representative parties—is that the proponents of the side opposite the JOLs would bear the risks of costs even while speaking for the benefit of all sharing the same interests. By contrast, it is accepted by all parties that representatives would have their costs of arguing the issues on the pre-emptive basis from the liquidation estate as a whole. I am persuaded that the circumstances presented here justify the making of representation orders.”*



47. Eiffel also argued that *dicta* in the judgment of Jones J in *Re Belmont Asset Based Lending Limited* [2011 (2) CILR 484] (**Belmont**) supported its submission that the JOLs had adopted the wrong approach in this case and that they should have either taken a decision with respect to the Eiffel Funds' claims and adjudicated the Eiffel Funds' proofs or made a sanction application, in relation to which they should remain neutral.
48. In that case a winding up order had been made on the petition of Bear Stearns as a contributory. It subsequently claimed to be an ordinary unsecured creditor of the company. On legal advice, the official liquidators had concluded that Bear Stearns should be admitted to proof as a creditor but they did not follow this advice. Instead, they made a sanction application by which they sought the direction of the Court that Bear Stearns be admitted to proof. In response, three shareholders issued a summons for directions and argued, *inter alia*, that the official liquidators should take no further part in the proceeding. At the hearing, the three shareholders were supported by three unpaid redeemed shareholders. The shareholders submitted that the official liquidators should have either adjudicated the proof or adopted a neutral position and made a sanction application. The Court made an order for directions that, *inter alia*, the sanction application be treated as an application by Bear Stearns against one of the shareholders, which agreed to act in a representative capacity on behalf of all six and that the official liquidators take no further part in the application. The official liquidators applied for a variation of that order. Jones J decided that although he was not persuaded that the official liquidators' continued participation in the application would serve any useful purpose, the direction that they take no further part in the sanction application was unnecessarily prescriptive. Accordingly, he decided to vary the order to provide that the official liquidators were authorised to take no further part in the application but if they participated, they would do so at their own risk as to costs. Eiffel relied on the following passage in Jones J's judgment (underlining added):

*“Secondly, it was submitted that the JOLs should have dealt with Bear Stearns’ proof of debt in one of two alternative ways. It is said that they should have adjudicated the proof, as it is their duty to do under CWR, O.16, r.1(4). If the JOLs had decided to admit the claim, then the shareholders would have been entitled to inspect the proof and the supporting documents, including any legal opinions (CWR, O.16, r.8), and make an application to the court for an order that it be expunged (CWR, O.16, r.20). Alternatively, if the JOLs considered that it was inappropriate for them to resolve the legal issues raised on this particular claim, they should have adopted a neutral position and made a sanction*

application, thus allowing each side of the argument to be put before the court in an inter partes proceeding between the competing stakeholders. I agree with these propositions. In fact, the JOLs have not adopted either course. On the one hand, they have not actually adjudicated the claim, with the result that the shareholders' right to inspect the proof and make an expungement application has not been triggered. On the other hand, they did not adopt a neutral stance. Instead, the JOLs have published a report in which they have stated, in unequivocal terms, their conclusion that Bear Stearns is entitled to be admitted to proof and they have issued a summons which seeks an order to this effect. The Six Shareholders felt that the JOLs were, in effect, "acting as Bear Stearns' advocate" on the sanction application and doing so at the expense of the estate. During the course of the original hearing on November 18th, the JOLs' counsel (Mr. Simon Dickson) told me that it was their intention to adopt a neutral position at the hearing and "to put both sides of the argument." Today, their counsel (Mr. Peter Hayden) said that the JOLs in fact intend to argue that Bear Stearns should be admitted to proof. The Six Shareholders say that Bear Stearns should be left to argue its own case and that it will serve no useful purpose for the JOLs to participate any further in this proceeding."

49. Eiffel argued that it should be appointed to represent the interests of the Late Redeemers for the following reasons:
- (a). the Eiffel Funds and Sirius had consented to Eiffel acting in a representative capacity on behalf of the Late Redeemers. Sirius is another Late Redeemer having redeemed all its shares with effect from 31 January 2019 (and had not received any prior redemption). The Eiffel Funds hold approximately 81.85% and Sirius holds approximately 13.49% by value of the claims of the Late Redeemers (which in aggregate amount to approximately US\$33 million - Villedy 1 at [17(a)]). As a result, a very substantial proportion of the Late Redeemers supported the Eiffel Summons and the appointment of Eiffel. It appeared that there were only two other Late Redeemers, identified as LR5 and LS7 in the Investor Schedule, with whom Eiffel had not been in contact and whose residual investments in that capacity were only approximately US\$1 million and US\$0.3 million respectively (see Villedy 1 at [18(e)]).
  - (b). there was a sufficient commonality of interest between all the Late Redeemers with respect to the application for the Misrepresentation Orders and the Preliminary Issue.
  - (c). the fact that consent had been given by the Eiffel Funds and Sirius demonstrated or at least was strong evidence that there was such a commonality of interest.

50. As regards its application for a pre-emptive costs order, Eiffel noted that the costs of a sanction application were governed by CWR O. 24, r. 9 which states as follows:

*“The Costs of Sanction Applications*

- (1) *This Rule applies to every sanction application under Order 11, including any application for the approval of the official liquidator's remuneration.*

.....

- (4) *In the case of a sanction application which is made or opposed by a creditor or contributory, the general rule is that –*

(a) *his costs of successfully making or opposing the application should be paid out of the assets of the company, such costs to be taxed on an indemnity basis if not agreed with the official liquidator; and*

(b). *no order for costs should be made against a creditor or contributory whose application or opposition is unsuccessful, unless the Court is satisfied that his position was wholly unreasonable or he is guilty of having misled the Court or otherwise acting improperly in connection with the application.*

- (5). *The Court shall make orders for costs in accordance with these general rules unless it is satisfied that there are exceptional circumstances and special reasons which justify making some other order or no order for costs”*

51. Eiffel also relied, in support of its application for a pre-emptive costs, on the Chief Justice’s judgment in *SPhinx*.

52. In his judgment, the Chief Justice had referred to and quoted from the classic judgment of Kekewich J in *Re Buckton* [1907] 2 Ch. 406 (***Re Buckton***) which set out guidance as to the costs orders to be made on applications involving trusts, which had been applied by analogy to liquidation cases. Kekewich J had said this:

*“In a large proportion of the summonses adjourned into Court for argument the applicants are trustees of a will or settlement who ask the Court to construe the instrument of trust for their guidance, and in order to ascertain the interests of the beneficiaries, or else ask to have some question determined which has arisen in the administration of the trusts. In cases of this character I regard the costs of all parties as necessarily incurred for the benefit of the estate, and direct them to be taxed as between solicitor and client and paid out of the estate*

...

*There is a second class of cases differing in form, but not in substance, from the first. In these cases it is admitted on all hands, or it is apparent from the proceedings, that although the application is made, not by trustees (who are respondents), but by some of the beneficiaries, yet it is made by reason of some difficulty of construction, or administration, which would have justified an application by the trustees, and it is not made by them only because, for some reason or other, a different course has been deemed more convenient. To cases of this class I extend the operation of the same rule as is observed in cases of the first class. The application is necessary for the administration of the trust, and the costs of all parties are necessarily incurred for the benefit of the estate regarded as a whole.*

*There is yet a third class of cases differing in form and substance from the first, and in substance, though not in form, from the second. In this class the application is made by a beneficiary who makes a claim adverse to other beneficiaries, and really takes advantage of the convenient procedure by originating summons to get a question determined which, but for this procedure, would be the subject of an action commenced by writ, and would strictly fall within the description of litigation . . . Whether he ought to be ordered to pay the costs of the trustees, who are, of course, respondents, or not, is sometimes open to question, but with this possible exception the unsuccessful party bears the costs of all whom he has brought before the Court.”*

53. The Chief Justice concluded that *SPhinx* was a first category case. He said that (underlining added):

“35. It was the common view expressed by the JOLs and by all the other parties on this hearing that, in the circumstances of this case, an order not just for their costs, but for the pre-emptive costs of the representative parties should be paid from the liquidation estate and that such orders should be made now. It was said as justification that it is in the interests of the proper administration of the estate as a whole—not just of the respective parties arraigned on one side or the other of the issues—that the issues are properly and fully ventilated in order that they may be finally determined. I accepted this argument for pre-emptive costs as well.

.....

39. In the present context, it is on the application of the liquidators that those interested in the liquidation estate are brought before the court “to ask to have some question(s) determined which have arisen in the administration of the estate” and “in order to determine the interests of the beneficiaries” inter se. The analogy with *In re Buckton*’s first category is therefore a good one, and the award of the

*representative parties' costs from the estate on the pre-emptive basis can thus be justified."*

54. Eiffel submitted that the present case was also a first category case. The resolution of the issues with which the Court was concerned here was for the benefit of the liquidation as a whole and not just the parties to the application. Both *Sphinx* and the present case concerned alleged misrepresentation claims. It was also plainly in the interests of the estate as a whole that the issues were properly and fully ventilated in order that they be finally determined. That could only be achieved by putting the representatives of the various classes of creditor on an even footing. The crucial point was that it was the JOLs and not the Late Redeemers who had taken the step of putting the issues before the Court in order to enable them to adjudicate upon claims. Given that the JOLs had initiated the proceedings, it was in the interests of the estate that all issues be properly and fully ventilated before the Court. This was not a case where the Late Redeemers had commenced proceedings for their own benefit and were seeking to argue for their own position. They had instead been forced into a process commenced by the JOLs and must be given the opportunity to respond.
55. This case, Eiffel argued, could be compared and contrasted with the facts of *In re Emergent Capital* [2012] (1) CILR 1 (*Emergent Capital*). In that case, Eiffel said, Jones J had made clear that if the Court's directions operated for the benefit of the entire estate, it was wrong in principle to impose the costs of the application on an individual contributory who opposed it (the situation here) but where two individual shareholders (as opposed to the JOLs) initiated proceedings seeking a determination as between themselves (not affecting the whole estate and without representation orders being made), this could justify a departure from CWR O.24, r.9(4).
56. In *Emergent Capital* official liquidators had made a sanction application by which they sought the directions of the court in respect of a dispute about the respective shareholdings of the company's only two shareholders (KTC and RAAL Ltd). Directions were given by Jones J. that the application take on the character of an *inter partes* action between KTC and RAAL Ltd (and the Court directed the service of pleadings and exchange of witness statements as if the matter were an action commenced by writ). It was agreed that the official liquidators would take no further part in the proceedings. Following a trial of that action, Jones J ordered that costs should

follow the event such that RAAL Ltd. was to pay KTC's costs, to be taxed on the standard basis if not agreed—the court was satisfied that there were exceptional circumstances within the meaning of CWR, O.24, r.9(5) that justified departing from CWR, O.24, r.9(4), which provided, *inter alia*, that a contributory's costs of successfully opposing a sanction application should be paid out of the assets of the company. In the exercise of its discretion, the court considered that KTC was entitled to the whole of its costs; it was successful on the critical issue of breach of fiduciary duty, the resolution of which necessarily involved wide ranging cross-examination of witnesses—the issues on which KTC lost probably did not add to the costs of the application in a material way. RAAL Ltd then applied for leave to appeal against the costs order. Jones J dismissed the application. In doing so he explained the approach to the award of costs that the Court should take when the Court gave directions for a sanctions application to be continued as an *inter partes* action between interested contributories. He said this (at [4] – [9]) (underlining and bold added):

- “4 The point of principle raised by counsel for RAAL turns on how one should characterize the application. If it is properly characterized as a sanction application, then the court should make orders for costs in accordance with the principles contained in CWR, O.24. Alternatively, if it is properly characterized as an inter partes action between KTC as applicant and RAAL as respondent, then the court should apply the principles contained in GCR, O.62, r.4.
- 5 As a matter of procedure, it is perfectly clear that the application is a sanction application within the meaning of CWR, O.11 and O.24. It was initiated by the amended summons issued by the official liquidators pursuant to their statutory powers and the end result was a direction that the official liquidators shall rectify the company's register of members and distribute the available assets to KTC and RAAL on the basis that they each own 50% of the issued share capital. It follows that the official liquidators were entitled to have their costs of the application paid out of the company's assets pursuant to CWR, O.24, r.9(2). If the application should continue to be treated as a sanction application, notwithstanding the consequences of the order for directions, then, prima facie, the court should have made orders for costs pursuant to r.9(4) ...
6. The principle underlying this rule is that sanction applications, made by official liquidators or stakeholders, are the mechanism whereby the court gives directions (which may be permissive or prescriptive) about the way in which the official liquidators should exercise or refrain from exercising their powers in the interests of all the creditors or shareholders as the case may be. The directions resulting from a sanction application take effect for the benefit of the estate as a whole. For this reason, r.9(4)(a) provides that an individual creditor or shareholder who

successfully makes or opposes a sanction application should have his costs of doing so paid out of the estate as an expense of the liquidation. Since the court's direction operates for the benefit of the creditor/shareholder class, it would be wrong in principle to impose the cost on the individual who successfully acted in their interest. If the individual's application/opposition was unsuccessful, r.9(4)(b) provides that he should not be ordered to pay the official liquidator's costs, unless the position which he adopted was wholly unreasonable or he is guilty of having misled the court or otherwise acted improperly. So long as he is acting properly in the interests of the estate, the court should not make any order for costs against him merely because his argument has been rejected.

7. If it had been appropriate to apply these rules in the circumstances of this case, I would have made an order that KTC's costs be paid out of the company's assets on an indemnity basis because it was "successful" and I would have made no order for costs against RAAL as the unsuccessful party, because it was not guilty of conducting its case in a way which was unreasonable or improper. It should be noted that there was no basis under r.9(4) for making an order that RAAL, as the unsuccessful party, should have its costs out of the assets. However, I was satisfied that there were exceptional circumstances and special reasons, within the meaning of r.9(5), which justified departing from r.9(4) altogether and making an order that RAAL pay KTC's costs on the standard basis.
8. As a matter of procedure and as a matter of form, the application was a sanction application. In substance it was not. In substance, the order for directions had the effect of converting it into an inter partes action between KTC as applicant and RAAL as respondent. They are the only parties with an interest. The official liquidators took no part in the application. KTC cannot sensibly claim to have been acting in the interests of "the estate." It was asserting its own cause of action for its own benefit. Likewise, RAAL cannot claim to have been defending the action on behalf of the company in the interests of the stakeholders generally. **RAAL is the only other shareholder.** It was defending KTC's claim in its own interest. In substance, the application was litigation between KTC and RAAL, by which the court determined their respective rights as against the company.
9. For the purposes of costs, it is plainly obvious in my judgment that r.9(5) enables the court to have regard to the substance of the matter and not merely its procedural form. The proposition that the conversion of the sanction application into an inter partes action between the only two parties in interest is not an exceptional circumstance or special reason for departing from the rules applicable to ordinary sanction applications is unarguable. It seems to me that the circumstances of this case make it the classic example in which the court should depart from the principles set out in r.9(4)(a) and (b). The application was akin to the circumstances addressed by r.8(2)(b). When the court directs that a contributory's winding-up petition be treated as an inter partes proceeding between two shareholders, the general rule is that none of the costs should be paid out of the assets of the company and the unsuccessful party should pay the costs of the successful party, to be taxed on the standard basis. In my judgment, exactly the same approach should be adopted when the court directs, as I did in this case, that a sanction application should be treated

*as an inter partes action between the only two shareholders. In my judgment, the proposition that I erred in principle by adopting this course is quite simply unarguable.”*

57. Eiffel noted that the JOLs, as I explain below, relied on the practice adopted in the Lehman *Waterfall* applications in support of their argument that a pre-emptive costs order was neither necessary nor justified in this case. Eiffel argued that those applications could and should be distinguished from the present case since the Lehman administrators had adopted a neutral position on the applications so that the creditors who appeared on the applications and who did not have the benefit of pre-emptive costs orders were not at a disadvantage, which Eiffel would be if the procedure proposed by the JOLs here were followed. Eiffel said that the role played by the Lehman administrators had been confirmed in the judgment of Lady Justice Gloster in the Court of Appeal on the appeal from the decision of Hildyard J in *Lehman 7* [2017] EWCA Civ 1462 (*Lehman 7 CA*) at [3]: “*The joint administrators of LBIE, whose application for directions in relation to the surplus gave rise to the current litigation, have remained neutral, participating in the proceedings only to the extent necessary to ensure that all the possible arguments are given a proper airing before the court.*”

### **The JOLs’ submissions**

58. The JOLs argued that their approach as set out in the Further Directions established a fair procedure that fitted, and was justified by the different positions of the various classes of Investors, the circumstances of this case. They submitted that a representation order and a pre-emptive costs order were neither necessary nor appropriate. They also argued that their proposed approach followed and was consistent with the practice recently adopted in other large insolvency proceedings in which similar issues had required resolution by the court, in particular the various *Waterfall* applications in the Chancery Division in England in the Lehman administration.
59. Mr Johnson set out at [14] of Johnson 15 the JOLs’ view of the status and effect of their application (underlining added):

*“As explained in Johnson 10, the JOLs are looking “to determine, in a cost-effective manner the threshold issues that the JOLs anticipate will need to be resolved to facilitate the determination of the respective rights of the Investors, and thus the distributions to them”. Further, the JOLs always envisaged that the relief granted would precede (but not replace) the process of adjudication, and to that extent we believe that the Application*



*should not be viewed as a final resolution of the rights between the Investors and DLIFF. It is the JOLs' view that, as a matter of law, the Investors would not be bound by the Court's decision insofar as any Investor is, in theory, free to appeal the JOLs' adjudication decision on its own claim. However, as a matter of practicality, the JOLs hope that the prior determination of the Court on the key issue(s) on notice to all Investors (albeit in the context of an application regarding the JOLs' exercise of their powers), will reduce the likelihood of any such appeals, particularly when any investor appealing the rejection of a proof of debt or applying to expunge an admitted proof of debt would be at risk on costs.*

60. The JOLs argued that it was not unusual for officeholders to take an active position on directions applications. This was the consistent position taken in the Lehman administration. The JOLs were already well versed in the issues and it would involve unnecessary expense and duplication for another party to replicate that work in order to argue the same position.
61. The JOLs cited and relied on a number of the judgments in the Lehman *Waterfall* proceedings (*Waterfall I* [2015] Ch 1 (***Waterfall I***), *Waterfall I* [2018] AC 465, *Waterfall II* [2016] EWHC 2131 (***Waterfall II***), *Waterfall II* [2017] EWCA Civ 1462 (***Waterfall CA***), *Lehman No 1* [2009] EWHC 2545 (***RAB Market Cycles***) and *Lehman No 7* [2018] 2 BCLC 171). As noted by Lord Justice Richards (as he then was) in *Waterfall II* (at [3]) “*As with earlier cases, all the issues are raised by the administrators on an application for directions, with various creditors with differing interests appearing as respondents and making submissions on the issues.*”
62. The JOLs submitted that it was not objectionable for the JOLs to advocate for the substantive relief sought. The position would be the same if no sanction application was made but the Investors instead made claims in the liquidation which the JOLs had adjudicated and rejected. On an appeal against the rejection, the JOLs would argue in support of the rejection and the Investors would argue in support of the admission of their claim. There would be an adversarial proceeding as between the JOLs and the relevant Investor and that Investor would be exposed as to costs.
63. The JOLs also argued that the procedure they had proposed *was* fair. It provided, in Mr Johnson’s words, “*a relative advantage*” over the alternative procedure that would apply under CWR O.16 if the JOLs just adjudicated the Investors’ proofs and left them to appeal the rejection if they wished to challenge the JOLs’ decision (see Johnson 15 at [32] and [33]). The JOLs argued that the costs regime applicable on a sanction application pursuant to CWR O. 24, r. 9(1) already gave

a creditor who opposed the application cost protection. It established a general rule to the effect that if successful such a creditor's costs would be paid out of the estate on an indemnity basis and if unsuccessful there would be no adverse order for costs. The Court could and would only decline to follow the general rule where it found that there were "*exceptional circumstances and special reasons which [justified] making some other order or no order for costs.*" The JOLs submitted that this rule gave Eiffel and other Investors who wished to oppose the application for Priority Relief substantial comfort. If their challenge was based on reasonable grounds and argued appropriately, they could expect, if successful, to be in the same position as if a pre-emptive costs order had been made and that, if unsuccessful, they would not be ordered to pay the JOLs' costs.

64. The JOLs said that in this case, as in the *Waterfall* litigation, there was no need to make a representation order since the intended purpose of the application was not to bind Investors as to the determination of their rights. Furthermore, such an order was not needed to ensure that all Investors had the opportunity to be heard, that issues were properly ventilated so as materially to reduce the prospects of an appeal against a rejected proof of debt (or application to expunge an admitted proof of debt) or for the application to achieve its purpose.
65. The JOLs also argued that a representation order would not be appropriate in this case because the economic interests of the Investors were not aligned in respect of the Priority Relief.
66. The starting point (or threshold) for any representation order was that the representing parties must have "*the same interest in a claim*" as the parties that they represented (citing *Jalla & Chujor v Shell ITSC Ltd & Shell NEPC Ltd* [2022] 2 All ER 1056 (**Jalla**) at [51], sub-paragraphs (b) & (c)) or, expressed another way, "*[the] critical requirement for the appointment of a representative, it must be emphasised, is that a number of persons have common interests and will benefit in common from the relief sought*" (citing *SPhinx* at [31]). There was also a fundamental requirement that membership of the represented class must be capable of being ascertained at the outset of the proceedings (citing *Jalla* at [51] sub-paragraph (a)).
67. In the present case, in relation to the Late Subscribers Contract Orders, the interests of the Late Subscribers were diametrically opposed to the interests of other Investors. If the Late Subscribers

Contract Orders were made the Late Subscribers would not enjoy priority over the other Investors (in respect of their late subscriptions). Accordingly, the application for the Late Subscribers Contract Orders involved a dispute between the Late Subscribers and the other Investors and there appeared to be a common interest between any Late Subscriber and the other Late Subscribers on the one hand and any other Investor and all other Investors on the other.

68. However, the position was more complicated in relation to the Misrepresentation Orders. The alignment of Investors' interests was, the JOLs argued, contingent on the outcome of the Subordinate Relief. It was therefore not possible to know whether any one Investor had the same interests as other Investors until the application for the Subordinate Relief had been determined. Because most Investors claimed in multiple but different capacities (and therefore wore different hats) a particular Investor may end up with a different outcome and therefore have a different interest from other Investors who shared some but not all of these capacities (and therefore wore some but not all of the same hats as the other Investors). For example, a Late Redeemer (some of whom had indicated an intention to oppose the making of the Misrepresentation Orders) who was also a Prior Redeemer might be better off if the relief was granted.
69. Mr Johnson explained the position as follows:

*“23. Regarding the requirement for common interests/benefitting in common, it is necessary to look beyond the initial categorisation of the Investors (adopted for simplicity of description) in Johnson 10 at paragraph 20.2 [Late Redeemers, Late Subscribers and Unredeemed Investors]. As noted in the footnote to that paragraph, those three sub-groups are not mutually exclusive. In addition, one further differentiating factor applies to some Investors in each of those 3 sub-groups. This is whether the particular Investor is one of those Investors who received funds in respect of prior redemptions of shares of DLIFF (at the prevailing NAV) prior to the onset of the Receivership (Prior Redeemers). In the event that the [Misrepresentation Orders are not made], then the rectification of the Register of Members becomes a live issue. As addressed in a little more detail in the following paragraphs, whether an Investor is a Prior Redeemer is likely to determine its view on the question of how the Register of Members should be rectified. However, if the [Misrepresentation Orders are made], this will likely eliminate the need for the rectification of the Register of Members. Accordingly, whether an Investor is also a Prior Redeemer can be expected to inform that Investor's view on the Misrepresentation [Orders]. The extent to which each Investor is in more than one category is apparent from the second column in the Investor Schedule...”*

24. Thus, it is far from clear that the [Misrepresentation Orders] will be similarly beneficial (or prejudicial) to all of the Late Redeemers, Late Subscribers or Unredeemed Investors. The consequence of the [Misrepresentation Orders] (if granted) is that the JOLs will invite proofs of debt from all Investors, and will not be able to reject those proofs simply on the basis that misrepresentation claims are not permitted as a matter of law because DLIFF is in liquidation. In the event that (roughly speaking) half of the Investors (by net investment value) assert Misrepresentation Claims which are ultimately admitted, this would have the effect of diluting the claims of the Late Redeemers (if they are also admitted). For this reason the Late Redeemers have an incentive to resist the [making of the Misrepresentation Orders].
25. However, the alignment of interests amongst the Late Redeemers on the Misrepresentation Issues presupposes the admission of the Late Redeemers' claims. For reasons touched upon in Johnson 10 at paragraph 142 to 145, but which can be elaborated upon if required, the JOLs consider that it is quite possible that those claims might be rejected, and that the Late Redeemers might, ultimately, be categorised as Unredeemed Investors. In that case, and if a Rising Tide approach is deemed to be an appropriate substitute for NAV reconstruction, the distribution to those Investors will be most significantly affected by whether or not they are also Prior Redeemers. Therefore, the position of the Late Redeemers (and in particular those who made prior redemptions, which constitutes the majority of the Late Redeemers by value) might turn out to be significantly better off if the relief in relation to the Misrepresentation Issue is granted.
26. As for the Late Subscribers, on their primary case the Misrepresentation Issues are of no consequence to them (at least insofar as they are Late Subscribers) because any such claims (if permitted) would be subordinate to their claims. However, if the relief on the Late Subscriber Issues is granted, they will all be Unredeemed Investors in relation to their respective Initial and/or Additional Subscriptions (as the case may be). Their interests on the Misrepresentation Issues are, in that capacity, driven by the extent to which they are also Prior Redeemers.
27. The interests of any sub-group of Investors determined by just one categorisation are, in the JOLs' opinion, too contingent to constitute common interests upon which representatives are properly and safely appointed. This could, in theory, be addressed, by splitting the groups to address the contingent outcomes but this would have the counter-productive outcome of increasing (not decreasing) the parties to the Application. In the JOLs' view, in order to have representatives for classes with truly common interests, it would be appropriate to sort the Investors into the following groups:
- (a). Late Subscribers only (Investors LS1 to LS3);
  - (b). Late Subscribers who are also Unredeemed Investors and Prior Redeemers (LS4, LS6, LS9);
  - (c). Late Subscribers who are also Unredeemed Investors only (LS5, LS8);

- (d). *Late Subscribers who are also Late Redeemers (LS7);*
- (e). *Late Redeemers who are also Prior Redeemers (LR1, LR2);*
- (f). *Late Redeemers who are neither Prior Redeemers nor Unredeemed Investors (LR3, LR4);*
- (g). *Late Redeemers who are also Unredeemed Investors (LR5);*
- (h). *Unredeemed Investors who are also Prior Redeemers (PR1 to PR19); and*
- (i). *Unredeemed Investors who are not Prior Redeemers (UI1 to UI28).*

28. *Another solution might be to treat the issues severally and sequentially, and split and re-constitute classes on an issue-by-issue basis, but this would appear to be a similarly unwieldy solution, and would be of limited effect in reducing the number of appropriate classes. For example, it seems that the Late Subscriber Issues could be sensibly determined as a preliminary question, with the Misrepresentation Issues determined as the secondary question (given that its resolution might well render the Subordinate Relief unnecessary as explained at paragraphs 49 to 51 of Johnson 10). This would have the effect of disposing of classes (a) to (d) listed above at an early stage, but classes (e) to (i) would still be required for the Misrepresentation Issues.*

29. *However, in either case, it seems that a representation order based upon classes of Investors with sufficiently common interests would require significant additional costs and delay (as opposed to simply proceeding with those Investors who have chosen to appear on the Application). Noting the observations of Smellie CJ In re SPhinx quoted above at paragraph 22 regarding the requirements of the interests of justice, it seems to the JOLs that the interests of justice do not, in these circumstances, require or justify the exercise of the Court's power to make representation orders."*

70. Accordingly, in summary, the JOLs maintain that the interests of Investors are splintered and depend on whether they have claims in one capacity, or a number of capacities, and on the currently unpredictable outcomes of the various open issues that remain to be resolved. So, to take one example, an Unredeemed Investor who is not a Prior Redeemer would benefit from the Misrepresentation Orders not being made. That is because if the Misrepresentation Orders are not made the question of rectification of the register of members would arise (rectification only being available if DLIFF is solvent) and this category of Unredeemed Investor is likely to benefit from that because it will receive, if the rising-tide methodology is applied, some distributions in priority to the Prior Redeemers. But the position may be different for an Unredeemed Investor who is a Prior Redeemer.

71. The JOLs submitted that the Eiffel Summons (and the evidence filed in support of it) suggested that the classes of Investors, for the purposes of determining the Preliminary Issue and the Priority Relief, should comprise the Late Redeemers, the Late Subscribers and the Unredeemed Investors. However, for the reasons given by the JOLs, this was an overly simplistic division, which would create classes where Investors did not have sufficiently similar interests. Accordingly, representation along the lines suggested in the Eiffel Summons failed to achieve the "unambiguous commonality" in relation to the Misrepresentation Orders that was required to justify the appointment of a representative.
72. The JOLs noted that only a limited number of Investors had come forward. The Investor Schedule revealed that there was no class of Investors where all the Investors in the class had come forward and been identified. Therefore all the Late Redeemers had not been identified and come forward. The Investor Schedule showed that two Late Redeemers, referred to as LR5 and LS7, had not made contact with the JOLs. There were a number of Late Redeemers who had not come forward and only a few of the Unredeemed Investors had done so. Therefore Eiffel did not have the consent to act as a representative from all members of the class that it wished to represent.
73. The JOLs also argued that a pre-emptive costs order should not be made. The authorities made it clear that the making of such an order was exceptional (because it displaced the normal discretion of the Court to award costs at the conclusion of the proceedings, taking into account all relevant factors at that stage) and there was no justification in this case for such an exceptional order.
74. The JOLs relied on the judgment of Hoffman LJ in the Court of Appeal decision in *McDonald v Horn* [1995] 1 All ER 961 (**McDonald**) at 970. He said as follows (underlining added):

*“The classic statement of the principles upon which the court acts is by Kekewich J, who was acknowledged in his time as a master of Chancery procedure, in Re Buckton.... While warning that it was 'well-nigh impossible to lay down any general rules which can be depended on to meet the ever varying circumstances of particular cases', he said that trust litigation could be divided into three categories. First, proceedings brought by trustees to have the guidance of the court as to the construction of the trust instrument or some question arising in the course of administration. In such cases, the costs of all parties are usually treated as necessarily incurred for the benefit of the estate and ordered to be paid out of the fund. Secondly, there are cases in which the application is made by someone*

*other than the trustees, but raises the same kind of point as in the first class and would have justified an application by the trustees. This second class is treated in the same way as the first. Thirdly, there are cases in which a beneficiary is making a hostile claim against the trustees or another beneficiary. This is treated in the same way as ordinary common law litigation and costs usually follow the event.*

.....

*Kekewich J acknowledged that it is often difficult to discriminate between cases of the second and third classes, but said ([1907] 2 Ch 406 at 415):*

*'... when once convinced that I am determining rights between adverse litigants I apply the rule which ought, I think, to be rigidly enforced in adverse litigation, and order the unsuccessful party to pay the costs.'*

*I should add that it is also sometimes difficult to discriminate between the first and third categories. Not all proceedings commenced by trustees for the determination of some question affecting entitlement to the fund are within the first category. Particularly in a case which does not involve the construction of a trust instrument but rather a dispute over the beneficial ownership of the trust property, the proceedings may be more akin to an interpleader"*

.....

*In Re Westdock Realisations [1988] BCLC 354 at 359 Browne-Wilkinson V-C said of an application for a pre-emptive order:*

*"Unless satisfied that after trial a judge would be likely to make an order that the costs of all parties are to come out of the fund it cannot in general be right to make such an order at this stage."*

*I respectfully agree. In fact, I would be inclined to put the matter rather more strongly. I think that before granting a pre-emptive application in ordinary trust litigation or proceedings concerning the ownership of a fund held by a trustee or other fiduciary, the judge must be satisfied that the judge at the trial could properly exercise his discretion only by ordering the applicant's costs to be paid out of the fund."*

75. The JOLs submitted that in this case, the underlying issues arising in respect of the Misrepresentation Orders and the Subscribers Contract Orders were issues that would normally fall to be determined as part of the adjudication process under CWR O.16. The directions they seek simply reflect the position that they would adopt under the adjudication process and the framing by the JOLs of these adjudication issues within a sanction application does not render the application congruent with either of the first two of the *Re Buckton* categories. Those opposing the making of the Misrepresentation Orders and the Subscribers Contract Orders would

be doing so to advance their own interests and this resulted in the application being closer to the third category in *Re Buckton*. Thus, the Eiffel Summons sought to utilise the procedure proposed by the JOLs (intended to save costs to the estate) to seek preliminary determination of issues that, absent the framing within a sanction application, would be determined in the costs-shifting context of CWR O.16.

76. There was no justification for extending the costs benefits that the Investors will obtain from the JOLs' adoption of the sanction order procedure, derived from CWR O. 24, r. 9(1). In addition, the JOLs were concerned that a pre-emptive costs order would create an environment where groups of Investors advanced arguments in their own interests without being at any material risk on costs, which, even with a costs-control mechanism in place, risked a serious escalation of costs and a reduction in the amount available for distribution.
77. The JOLs noted that it appeared that Eiffel had made it a condition of their appointment as a representative that a pre-emptive costs order be made. It would be a matter for Eiffel to decide, if the Court declined to make such an order, whether nonetheless to act as a representative if the Court made the requested representation order or to appear on the directions application if the Court also dismissed Eiffel's application for a representation order. If it, and other Investors, chose not to appear then the JOLs would be required to present to the Court the counter-arguments without the benefit of Investor participation. That would be undesirable but unavoidable if Investors chose not to participate.
78. The JOLs submitted that the authorities relied on by Eiffel were of no assistance to its case. Each case turned on its own facts and the facts in these cases were materially different from the facts of this case. *SPhinx* identified the test to be applied in deciding whether to make a representation order and the Chief Justice considered that it was satisfied in that case. In *SPhinx* there was no dispute between the parties as to the appropriateness of a representation order and a pre-emptive costs order. The official liquidators supported such orders being made. As a result, the Court did not have to and did not consider whether the test set out in *McDonald* was satisfied. In this case, the Court could not be satisfied that following the substantive hearing of the JOLs' application for the Priority Relief the Court will only be able properly to exercise its costs discretion by ordering that Eiffel's costs be paid out of the estate. Eiffel and Sirius constituted almost the entire



class of Late Redeemers and were acting in their own economic interests. In *Belmont* Justice Jones identified two procedural routes for adjudicating issues arising in a liquidation which affected investors and creditors but he was not saying that these were the only two routes available. The JOLs said that there was a third route, namely for the official liquidators to apply for directions on the basis proposed by the JOLs here. The procedure adopted in the Lehman *Waterfall* applications demonstrated that this was a legitimate approach. As a careful reading of the report of the arguments made by the administrators in those applications revealed (see for example the summary of the submissions made by the administrators counsel in *Waterfall I*, at pages 7-9 of the report), the administrators actively participated in and made submissions on a wide range of issues (so that the extract from the judgment of Lady Justice Gloster relied on by Eiffel had to be seen in context).

79. The JOLs also considered that there was no need for and that it would be inappropriate to order that the Preliminary Issue be dealt with before the Priority Relief. They relied on five points. First, it was preferable to deal with the Preliminary Issue after dealing with the application for the Misrepresentation Orders since that application may remove the need to adjudicate the Preliminary Issue at all. If the Misrepresentation Orders are made the Late Redeemers may be better off asserting and relying on claims for damages for misrepresentation rather than on their redemption claims. Secondly, it was impossible to remove all uncertainty and resolve all open issues for all Investors before dealing with the Priority Issues and Eiffel's approach merely shifted the uncertainty from one group of stakeholders to another. If the Preliminary Issue (dealing with the available cash limitation issue) was to go first, that would assist Eiffel because it would then know whether or not it was a creditor. But, Unredeemed Investors who could say that unless the outcome to the misrepresentation issues was known first, they would not know whether it was in their best interests to oppose the Preliminary Issue because unless they had claims as creditors established as part of the misrepresentation issues, they may have no real interest in opposing the Preliminary Issue (they could not work out what the economic impact would be of Eiffel being admitted as a creditor unless they knew whether they were creditors or just shareholders). Thirdly, dealing with the Preliminary Issue adds a further step (and therefore costs and delay) to the determination of the Amended Summons. There would be three rather than just two substantive issues to deal with. The Preliminary Issue would also raise fact-sensitive and evidential issues, certainly to a much greater extent than the issues raised by the Priority Relief (in order to

determine the available cash limitation issue, it would be necessary to reconstruct DLIFF's liquidity position and the other matters relevant to the definition of available cash). Fourthly, the resolution of the status of the Late Redeemers will not of itself assist the Court in determining the questions raised by the application for the Priority Relief. Finally, the resolution of the available cash limitation issue will also not provide the absolute commercial certainty apparently sought by Eiffel since it will not resolve the quantum of the claims of the Late Redeemers.

### **The Liquidation Committee**

80. The position of the LC was explained by Mr Kennedy in Kennedy 1. His affidavit was filed to deal with the procedural issues raised by the Eiffel Summons. Mr Kennedy explained that the LC understood that it acted in a representative capacity and had a duty to act solely with regard to what the LC objectively considered to be in the best interests of those interested in the estate as a whole. The LC agreed with the JOLs (see Johnson 15 at [39] to [40]) that it was not for the LC to weigh in on the substantive issues on the Amended Summons but that it could properly assist the Court by providing its views as LC on the procedural issues of representation orders and pre-emptive costs orders.

81. Mr Kennedy said that the LC accepted the JOLs' views on the question of whether representation orders should be made. While not opposed in principle to representation orders if they were shown to be likely to result in a reduction in costs and an increase in efficiency, having considered the position adopted by the JOLs and the arguments made by Eiffel, the LC were not persuaded that this would necessarily be the result in this case. The LC had noted that the JOLs had concluded that the interests of any sub-group of Investors determined by just one categorisation were too contingent to constitute common interests upon which representatives could properly and safely be appointed. The LC was concerned that, in these circumstances, representation orders may be unworkable and result in further disputes and an increase in costs. Furthermore, the LC noted with concern that Eiffel's position was that it was only prepared to act in a representative capacity if a pre-emptive costs order was made (see Villedy 1 at [36]). This position revealed that Eiffel's real aim was to orchestrate a situation where its costs were paid out of the estate. The LC did not believe that was appropriate for a representation order to be made if it was only being sought as a mechanism to seek a pre-emptive costs order. Mr Kennedy

also said that the LC was seriously concerned that the pre-emptive costs orders sought by Eiffel ran counter to the interests of the estate. The LC agreed with the JOLs' concerns (see Johnson 15 at [30]-[36]) and noted that the estate had already incurred significant costs in funding the JOLs to reach a professional independent opinion based on legal advice on the substantive issues for determination on the Amended Summons. The LC take the view that if a stakeholder or group of stakeholders wished to challenge the view taken by the JOLs they should do so at their own expense in the first instance and at risk on costs. Otherwise, the LC perceive that the estate would be paying twice. The LC did not consider this to be in the interests of the estate as a whole. Further, the LC was concerned that pre-emptive costs orders may incentivise those who are or may be lower in the distribution waterfall to litigate to try to improve their position at the expense of those who are higher in the waterfall. The LC was particularly concerned that, as noted by the JOLs (Johnson 15 at [31]), a pre-emptive costs order would create an environment in which groups of Investors were likely to advance arguments in their own interests without being at risk of an adverse costs order.

## **Discussion and decision**

### *The approach to be adopted by the Court*

82. It is helpful to begin by reviewing the different procedural routes by which issues of the kind raised by the Amended Summons can be brought before the Court in a winding up.
83. There are three main procedural routes. The different routes and their effects on the Court's approach to awarding costs can be summarised as follows:
  - (a). first, the official liquidators may adjudicate a creditor's proof and following rejection of the proof the creditor may appeal the rejection. CWR O.16 applies on such an appeal and costs will generally follow the event (CWR O.24, r.10(3)). The creditor is at risk as to costs. If it wins, it will recover its costs out of the estate and if it loses it will have to pay

the official liquidator's costs. The official liquidators will generally have their costs out of the estate (CWR O.24, r.10(2)).

- (b). second, the official liquidators may make a sanction application in which they apply for an order giving them permission to exercise their powers in a particular manner and an interested contributory or creditor may be joined as a respondent to make submissions on behalf of contributories or creditors in a similar position. CWR O.11 and CWR O.24, r.9(4) apply. Any contributory or creditor who opposes such a sanction application will, generally, if successful have its costs paid out of the estate and if unsuccessful not be required to pay the costs of the official liquidators. If there are exceptional circumstances and special reasons justifying doing so, the Court may disapply the general rules and make “*some other order or not [sic] [no] order for costs.*” (CWR O.24, r.9(5)). In *Emergent Capital Jones J* said (at [8]) that “*It should be noted that there was no basis under r.9(4) for making an order that [the unsuccessful contributory] should have its costs out of the estate.*” But while r.9(4) does not make provision for such an order the Court has the power to make such an order under r.9(5) if there are exceptional circumstances and special reasons for doing so.
- (c). thirdly, the official liquidators may make a sanction application in which they apply for an order giving them permission to exercise their powers in a particular manner and the application “*gives rise to an issue in respect of the [sic] substantive rights as between the company and any creditor or contributory or any class thereof*” (CWR O.11, r.3(3)). The Court may then direct that the proceeding is adjudicated as an *inter partes* proceeding as between shareholders, creditors or any class of shareholders or creditors, for which purpose the Court may make a representation order and give directions to the official liquidators as to the role (if any) they should take on the application (CWR O.11, r.3(3)(b) and (c)). If the Court gives such a direction and, to use Jones J's words in *Emergent Capital* (at [8]), “*in substance, the application [becomes] litigation between [the relevant parties]*” where neither of them can be said to have been acting in the interests of the estate then there are

exceptional circumstances and a special reason for the purpose of CWR O.24, r.9(5) and the Court may and should disapply the general rules set out in CWR O.24, r.9(4).

84. The JOLs wish to adopt and follow the second approach while Eiffel wishes to adopt and follow the third approach.
85. The decision as to which approach is most appropriate is a case management decision. It will depend on the nature of the issues in dispute, what is needed to ensure a fair resolution of the dispute in accordance with the overriding objective and to ensure that the parties in interest have an opportunity to be heard and that the liquidation estate only bears the costs of the proceedings where they are, and where those who appear are acting, for the benefit of the estate. There are two main questions – parties and costs. Who should be the parties to the proceedings and should the usual rule that costs follow the event apply or should the estate pay some or all of the parties' costs?
86. The starting point is to analyse the true substance and the proper characterisation of the issues in dispute. Where the claimant is a creditor or contributory who wishes to assert an adverse claim against the estate (which is therefore to the detriment of all other stakeholders) for its own benefit and not the benefit of the estate (and the claim is resisted for a similar reason), then the claimant (and the respondent) should bear their own costs and the normal rule that costs follow the event should apply. The proceedings have the character of ordinary commercial litigation. Where however an issue arises which affects all creditors or contributories with an interest in the estate and creditors or contributories are joined to take opposing positions to ensure that the Court hears full argument, they are acting for the benefit of the estate and not for, or at least not exclusively or primarily in, their own separate interests. In some, perhaps many, cases creditors or contributories who participate in proceedings at the instigation of official liquidators will have a number of interests and reasons for participating, in which case the Court is required to form a view as to purpose of the proceedings and the benefits derived by the estate from the relief sought and decide whether on balance the litigation should be constituted as an *inter partes* proceeding and whether the parties should have their costs paid by the estate.

87. CWR O.11, r. 3(3) deals with what I have labelled the parties point where the proceedings are commenced by official liquidators as a sanction application. The Court is given the power to direct adjudication as an *inter partes* proceeding “*when a sanction application gives rise to an issue in respect of [the] substantive rights as between the company and any creditor or contributory or any class thereof.*” This applies in the first category of case I have mentioned, namely where a creditor or contributory asserts an adverse claim against the estate for their own benefit and not the benefit of the estate. In *Emergent Capital Jones J* held that in such a case, the costs regime for ordinary hostile litigation should apply. The general rules set out in CWR O. 24, r. 9(4) were inapplicable in such a case. As Jones J said:

*“... the circumstances of this case make it the classic example in which the court should depart from the principles set out in r.9(4)(a) and (b). The application was akin to the circumstances addressed by r.8(2)(b). When the court directs that a contributory’s winding-up petition be treated as an inter partes proceeding between two shareholders, the general rule is that none of the costs should be paid out of the assets of the company and the unsuccessful party should pay the costs of the successful party, to be taxed on the standard basis. In my judgment, exactly the same approach should be adopted when the court directs, as I did in this case, that a sanction application should be treated as an inter partes action between the only two shareholders. In my judgment, the proposition that I erred in principle by adopting this course is quite simply unarguable.”*

88. Jones J drew an analogy with the procedural rule dealing with contributory’s winding-up petitions (now CWR O.3, r.12(b)), which requires the Court, when hearing a summons for directions, to give directions as to “*whether the proceeding should be treated as a proceeding against the company or as an inter partes proceeding between one or more members of the company as petitioners and the other member or members of the company as respondents.*” That rule is based on the company law principle that where the petition arises from a personal dispute between shareholders it is a misapplication of the company’s money to pay any costs of the proceedings except for those necessarily incurred in representing the company as a separate person. The analogy has some force in the context of proceedings arising during the winding up since it can also be said that the estate should not pay the costs of personal disputes between those with an interest in the estate (creditors or contributories), since funds in the estate should not be used for the benefit of individual creditors but only for the benefit of all stakeholders. But as Chief Justice

Smellie pointed out in *SPhinx* (see [36], [37] and 42]), the Court's practice with regard to costs of litigation in winding up proceedings, now codified in the CWR, is based on an analogy with the regulation of costs in trust cases. In those cases, the court has been willing in certain circumstances in trust proceedings to extend to beneficiaries an entitlement to costs out of the trust fund by analogy with that accorded to trustees (the trustee's right of indemnity). The circumstances where the beneficiaries are accorded special treatment are limited and guidance as to the approach to be adopted by the Court was set out in *Re Buckton*. Apart from these circumstances the rules which apply in ordinary hostile litigation govern beneficiaries' costs, so the general rule is that beneficiaries, if unsuccessful, will be ordered to pay the costs of the successful party, and if successful will obtain an order for costs.

89. CWR O.11, r. 3(3) is designed to apply to cases in *Re Buckton* category four. As is noted in Lewin on Trusts (20<sup>th</sup> ed., 2020) at [48-039]:

*“The categories of proceedings enumerated in Re Buckton are not closed. A fourth category has been recognised where proceedings are commenced by a trustee but have the characteristics of category (3). For not all proceedings commenced by a trustee for the determination of some question affecting entitlement to the trust fund are within Buckton category (1), particularly in a case which does not involve the construction of the trust instrument but rather a dispute over the beneficial ownership of the trust fund. One example of a category (4) case is where there is a hostile dispute between two persons who claim to be the true owner of the trust fund and the trustee intervenes by seeking the determination by the court of the construction of the trust deed. Another example is this. Suppose the trust fund consists of assets such as land incapable of payment into court under section 63 of the Trustee Act 1925 and a beneficiary who has become absolutely entitled to the trust fund under the original trusts has purportedly assigned his interest to some assignee who has given notice of the purported assignment to the trustees. Following a dispute between the beneficiary and the purported assignee as to whether the assignment was as a matter of law a valid one, but neither of them taking any proceedings to resolve the matter as between themselves, the trustee, being advised that there are real doubts as to the true beneficial ownership of the trust fund, commences proceedings to determine which of the rival claimants is the true beneficial owner from whom he might obtain a good discharge. Although in form the proceedings come within Buckton category (1), in substance the dispute comes within the third category, and the costs of the rival claimants should be governed by the principles of cases falling within the third category, for the proceedings are akin to an interpleader...”*

90. As Lewin points out (at [48-033]), cases in *Re Buckton* category three have the character of a hostile claim and the distinction, though one not easy to draw in practice, between this kind of litigation and litigation within the first two categories, is that the claim is brought not in substance for the benefit of the trust fund, but for the benefit of the claimant, and is resisted for a similar reason.
91. So, as it seems to me that, while the Court is given by the CWR considerable flexibility to order a procedure that meets the needs of the particular case, the Court should only make an order that the proceeding be adjudicated as an *inter partes* proceeding where, considering all relevant factors, the litigation is properly to be categorised as being in substance hostile litigation in which the dispute is exclusively or primarily between (or for the benefit of) stakeholders who are to be treated as litigating for their own benefit and not for the benefit of other stakeholders (creditors or contributories) or to assist in the administration of the winding up
92. *Emergent Capital* was clearly a case of this type. The only parties in interest were RAAL and KTC who were fighting over a share of the proceeds of sale of the company's only valuable asset. They both were willing and active participants in the litigation. The nature of dispute adjudicated in that case was made clear in Jones J's earlier judgment reported at [2011 (2) CILR 329]. The dispute was between RAAL and KTC (as the only shareholders) as to their respective shareholdings in the company RAAL claimed to own 99% and KTC claimed to own 50%) and consequently their entitlement to share in and receive distributions out of the proceeds of sale of the company's only valuable asset. Mr Justice Jones granted KTC's application and directed the liquidators to rectify the company's register of members to reflect that KTC and RAAL each owned 50% of the company's shares. The background facts were neatly summarised in the headnote of the CILR report as follows:

*“KTC, and respondent, RAAL Ltd., were companies created for the sole purpose of holding shares in Emergent Capital Ltd., pursuant to a joint venture between Mr. David, the major shareholder of the respondent, and the Kazal brothers, who owned the applicant. ECL's share capital was 50,000 shares of US\$1 each, of which 50 were issued to each of the parties. The relationship between Mr. David and the Kazal brothers deteriorated when the brothers refused to provide half of ECL's capital needs in return for their equal equity*



*share. By that time, Mr. David had provided approximately AUS\$5.8m. to ECL and its subsidiaries, whilst the brothers, through the applicant, had provided AUS\$600,000. Upon the Kazal brothers' refusal to provide more capital, Mr. David took steps to capitalize part of his shareholder loan. He convened a board meeting in the absence of the Kazal brothers, having given them notice of the meeting five days' beforehand, at which he, together with Mr. Mavro, who had been appointed as a director of ECL, passed a resolution to issue 49,900 shares at US\$1 each to the respondent in consideration for a corresponding reduction in the amount due on his shareholder loan account. The debt/equity swap transaction gave the respondent a 99.99% equity share in ECL, reducing the applicant's share from 50% to 0.01%. Upon discovering the transaction, the Kazal brothers brought a winding-up petition on the just and equitable ground and applied for the appointment of provisional liquidators. The Grand Court (Jones, J.) refused to appoint provisional liquidators upon the respondent's undertaking not to exercise any rights attaching to its shares without the consent of the applicant or leave of the court. At that time, ECL's only valuable asset was a wholly-owned subsidiary, Global Renewables Ltd. ("GRL"). The court permitted the sale of GRL, ordering that the proceeds be paid into court pending determination of the winding-up petition. After the sale, the parties agreed to the voluntary liquidation of ECL by a unanimous written resolution. The liquidators sought directions to determine the share dispute, but subsequently agreed for the matter to be dealt with inter partes, without its participation."*

93. In *Belmont*, it was clear that the admission of Bear Stearns as a creditor would prejudice the position of the redeemed but unpaid shareholders and other shareholders. Together they were the only parties in interest. After the official liquidators had issued a summons seeking a direction of the Court that Bear Stearns be admitted to proof, and even though Bear Stearns did not appear at the initial directions hearing, Bear Stearns subsequently agreed to act as applicant and as a representative of the redeemed but unpaid shareholders and the other shareholders agreed to act as respondents to an *inter partes* proceeding. Bear Stearns had claimed to be an ordinary unsecured creditor (although it had not submitted a proof of debt). If admitted, Bear Stearns' claim would rank ahead of all other parties (save for a few former service providers) including deferred creditors, i.e. redeemed but unpaid shareholders. Accordingly, the decision whether or not to admit Bear Stearns was highly significant from the point of view of the Fund's shareholders and unpaid redeemed shareholders. The consequence of admitting the claim was that the Fund would be insolvent and there would be no distribution to the shareholders. Nor would there be any distribution to the unpaid redeemed shareholders whose claims ranked behind those of the ordinary unsecured creditors. The six shareholders who intervened in the proceedings and objected to Bear Stearns' admission as a creditor would only be paid in full if Bear Stearns' claim was rejected. It was therefore clear that the real and only parties in interest were Bear Stearns on

the one hand and the deferred creditors and the shareholders on the other. Jones J, making a case management decision, concluded that the proper and most expedient course was to make a direction that the sanction application brought by the official liquidators be treated as an application by Bear Stearns (as applicant) against one of the shareholders which agreed to act in a representative capacity as respondent to determine whether, upon the true construction of the option agreement between Bear Stearns and the Fund, Bear Stearns was a creditor. Jones J also initially directed that the official liquidators take no further part in the proceedings, although he subsequently amended his order to state that they were authorised to take no further part in the application but if they participated, they would do so at their own risk as to costs.

94. It is also helpful to look again at the issues raised in *SPhinx*. That was a case, as I have noted above, in which the official liquidators chose to proceed by way of directions rather than an *inter partes* proceeding. There were a large number of issues and disputes. There were also a large number of creditors and investors such that it was impracticable to conduct a hearing involving all of them. The official liquidators applied for directions and considered that it was necessary, in the interests of the administration of and for the benefit of the liquidation estate, that the issues be resolved by the Court (in particular to facilitate the payment of an interim dividend) and that representative creditors and investors be appointed to represent the different distinct groups of creditors and investors on one side or the other of the issues, where they could properly be regarded as sharing the same interests (the report of the Chief Justice’s judgment does not identify the different classes who were to be represented). The various representative creditors and investors were willing to assist the official liquidators and participate in the proceedings.
95. The issues were explained and summarised by the Chief Justice as follows (underlining added):

*“The issues*

2. *The issues ... have been... identified as involving some 23 distinct questions (albeit within three broad categories).... The three broad categories give some insight into the complex nature of the issues:*
  - (a). *issues as to the ownership of assets and responsibility for liabilities. Has there been co-mingling of the assets and liabilities of the SPhinx companies*

*(excluding assets and liabilities arising as a consequence of any litigation instituted by the JOLs, the SPHinx companies or the trustee of the SPHinx Trust)? This category also covers issues as to the treatment of assets and liabilities for the purposes of claims in the liquidation, and the incidence of litigation costs, expenses and liabilities;*

- (b). issues as to the ranking of claims in the liquidations, including issues as to (i) the status of the “S shares”; (ii) the suspension of redemptions of June 14th, 2005; (iii) the redemption of shares and net asset value (“NAV”) calculations; (iv) the validity of the redemption requests; and (v) whether misrepresentation claims by investors rank as creditor claims; and*
- (c). how much money is available for interim payments, and whether there can be a declaration of interim dividends.*

- 3 Broadly speaking, the issues in category (a) have arisen because of alleged misconduct—mismanagement, gross negligence or fraud—in relation to the dealings with the assets and liabilities of the various SPHinx companies....*
- 4. A consequence of the alleged misconduct has been the co-mingling of funds as between the SMFF and other SPHinx entities ...*
- 5. A major accounting issue arises over the correct allocation of the US\$263m. loss of SMFF and its underlying segregated portfolios. Are the liabilities owed to investors in those portfolios to be ascribed strictly only to those portfolios or, because the funds of those portfolios may have become co-mingled with the funds of others, are such liabilities to be ascribable more broadly across the entire SPHinx liquidation estate?....*
- 6. Again, broadly speaking, these are some of the issues arising under category (a) which the JOLs have presented as requiring answers from the court to enable the proper administration of the SPHinx estate, and for which purposes the appointment of representatives should be made so that they may be fully and fairly argued. The immediate objective in the administration is the payment of an interim dividend. The JOLs have US\$525m. in hand but, as yet, more than four years into the liquidation, there has not been a distribution of dividends. It is plain, however, that that may not happen until the issues are resolved.*
- 7. As to the category (b) issues, these involve the status and ranking of a class of shares (“S shares”) which were issued to some investors in the special situation of their having given notice to redeem their investments in certain of the SPHinx companies. Although their notices were accepted, they were not completely redeemed by payment out and cancellation of their shares because redemptions were subsequently suspended by the directors purporting to act in keeping with the constitution of the funds.*
- 8. A question therefore arises as to the status of those investors: are they still shareholders in the respective SPHinx companies, or are they to be regarded as*

creditors to the extent of the value of their redemptions as allocated by NAV calculations sought to have been applied at the time of redemption? The calculations and declarations of NAV were also subsequently suspended. Another obvious question that arises in relation to S shareholders is the ranking of their claims: do they rank with ordinary shareholders as investors, as redeemed investors ahead of ordinary shareholders and behind third party creditors, or alongside third party creditors? Within this group of issues an overarching question will therefore be: was the suspension of redemptions and the suspension of NAV calculations valid?

9. From that summary of the category (b) issues (taken at risk of over-simplification), it will be readily apparent that these too will need to be resolved before there can be a declaration and payment of an interim dividend. And there is an obvious overlap with the category (a) issues in the areas where questions of co-mingling of assets within segregated portfolios or pooling of assets must be resolved.
10. As to the category (c) issues, a main question will be just how much of the US\$525m. now in hand should be regarded as available for interim distribution. This question arises, I am told, to a large extent because of the setting by this court of a monetary indemnity reserve of US\$117m. to meet the potential claims that indemnity claimants may have against the SPHinx liquidation estate. That reserve and the concerns which propelled it are the subject of a written judgment delivered herein on February 12th, 2010.
11. The reserve, at roughly a fifth of the presently available assets, gives rise to an obvious concern before any interim distribution may be made: how is the liability of the indemnity reserve to be allocated as against the various SPHinx entities? Should they be strictly allocated as against the entities having strict regard to liabilities for the respective grants of indemnities? Or should they be allocated more generally on the basis that the SPHinx estate as a whole should be responsible for honouring all indemnities granted to indemnity claimants? Here too, much will depend on whether there can be a disentangling and tracing of respective assets and liabilities or whether assets and liabilities across the SPHinx estate must be pooled.
- .....
20. Again, with the benefit of discussion, these were winnowed out from the 23 down to questions 1–4 and 8 in category (a)—of which 1 and 2 can first be resolved on the present state of the evidence (3, 4 and 8 requiring further financial information from the JOLs)—and 11–19 in category (b). It was recognized and agreed that questions 5–10 in category (a) and all of the questions in category (c) relate to the eventual treatment of assets and liabilities for distribution purposes and so must await the resolution of the earlier questions. Question 20 (the last in category (b)) uniquely raises an issue of potential liability of the SPHinx companies to certain investors who invested after the SMFF and PlusFunds losses were allegedly known to SPHinx management and who were not informed about those losses—in other words, potential investor misrepresentation claims. The issue raised by question 20 is therefore whether such potential misrepresentation claims should be regarded as

*ranking as creditor claims. No such claims have yet been brought or are any longer likely to be brought and so there is no perceived need at the moment to incur the costs of having that question answered through the court. Moreover, no such claims are likely to be brought because there appears to be an obvious answer to them.*

21. *On the long-standing authority of the House of Lords' decision in Houldsworth v. City of Glasgow Bank, the SPHinx companies having been placed into liquidation, an investor seeking rescission of his share purchase contract and restitutio in integrum on the grounds of misrepresentation may well no longer have available to him such remedies. For the SPHinx companies, having long since been placed in liquidation and all their assets and liabilities subject to the liquidation regime through the courts, such remedies are no longer possible. Investors must therefore resort only to such rights as their shares might afford them in the context of the liquidation of the SPHinx estates."*

96. As the three broad categories identified by the Chief Justice make clear, some issues related to disputes between the SPHinx companies (who was liable for what liability, including liabilities to indemnity claimants, and who owned which asset?); some related to the rights of holders of S class shares and their claims against SPHinx (and raised the question of whether they were still shareholders or had become creditors, and if creditors, how did their claims rank?) and some related to the claims of other investors as against the estate (with disputes arising in respect of the suspension of redemptions, the redemption of shares and the NAV calculations, the validity of the redemption requests and whether investors were entitled to claim as creditors based on misrepresentations). As in the present case, directions were sought regarding whether parties were shareholders or creditors and in relation to misrepresentation claims for damages. Interestingly, the Chief Justice Smellie noted (at [20]) that the issue was whether potential misrepresentation claims should be regarded as ranking as creditor claims, but that "*No such claims [had] yet been brought or are any longer likely to be brought and so there is no perceived need at the moment to incur the costs of having that question answered through the court. Moreover, no such claims are likely to be brought because there appears to be an obvious answer to them.*" The obvious answer, he said, was the decision in *Houldsworth*, the authority of which was not challenged in *SPHinx*. In any event, the Chief Justice accepted the official liquidators' view that it was in the interests of the estate to have all these issues determined by the Court by way of a directions application and that the representative creditors should have their costs paid out of the estate. The issues raised needed to be resolved in an orderly sequence in order to enable the proper administration of the liquidation (see [29]) and as Chief Justice Smellie said, there had been an application by the official liquidators pursuant to which "*those interested in the*

*liquidation estate [were] brought before the Court “to ask to have some question(s) determined which have arisen in the administration of the estate” and “in order to determine the interests of the beneficiaries” inter se. The analogy with [Re Buckton’s] first category is therefore a good one and the award of the representative parties’ costs from the estate on the pre-emptive basis can thus be justified” (see [39]).*

*The Court should consider the approach and procedure to be adopted in relation to the Misrepresentation Orders and the Late Subscribers Contract Orders separately and the Preliminary Issue in conjunction with the application for the Misrepresentation Orders*

97. When considering the present case, it is appropriate to consider the Misrepresentation Orders and the Late Subscribers Contract Orders separately (Eiffel’s only direct and expressed interest is in the former) and the application for the Court to order the determination of the Preliminary Issue in conjunction with the application for the Misrepresentation Orders.

#### *The Misrepresentation Orders*

98. The application for the Misrepresentation Orders is in substance being made for the benefit of the misrepresentation creditors. It raises a narrow range of issues and in principle opposes the interests of Investors who are making or wish to make claims for damages based on misrepresentation against the interests of all other Investors (both those who have been, or will be, admitted as creditors - for example, the Late Redeemers assuming that they will be admitted as creditors - whose creditor claims will be diluted by the damages claims and other Investors whose entitlement to a distribution as shareholders will be subordinated to those claims). This fact pattern is similar to that in *Re Belmont* where the dispute was between a party claiming to be a creditor and those who would be prejudiced by it being admitted as such. The consequence of admitting Bear Stearns’ claim was that shareholders would be prejudiced (they would receive nothing). It can be said that here the misrepresentation creditors are maintaining a hostile claim against the liquidation estate for their own benefit and the Late Redeemers, if they oppose the making of the Misrepresentation Orders, are also acting for their own benefit. On that basis, it can be said that an order that the application for the Misrepresentation Orders be adjudicated as an *inter partes* proceeding is justified and appropriate.

99. However, it seems to me that there are substantial countervailing factors. The determination as to whether to make the Misrepresentation Orders is to be made at an early stage in the liquidation. As the JOLs have explained, only a limited number of Investors have to date made claims in misrepresentation and so the financial consequences of making the Misrepresentation Orders remains unclear. As I have noted above, the JOLs state that if the Misrepresentation Orders are made, they will send out proof of debt forms to all Investors and allow those who wish to file an amended proof of debt in light of the Court's decision to do so. The JOLs will then need to review the proofs of debt received and consider the consequences. The JOLs at this stage therefore do not know the quantum of misrepresentation claims that will be made or whether DLIFF will be made insolvent as a result of such claims being admitted. Consequently, there is a material degree of uncertainty as to how different Investors and groups of Investors will be affected by the making of the Misrepresentation Orders. Furthermore, for the reasons given by the JOLs, the impact of the making of the Misrepresentation Orders will depend on whether an Investor is also a Prior Redeemer. If DLIFF remains solvent, Prior Redeemers may lose out because if a rising tide approach is adopted, distributions will be made first to other Investors to allow them to catch up and have their positions equalised with that of the Prior Redeemers. This uncertainty means that it is difficult to identify definitively the nature of the parties' interest in the dispute relating to the Misrepresentation Orders and to be satisfied that particular parties' interests will definitely and in all circumstances be served by supporting or opposing the making of the Misrepresentation Orders. This seems to me to be a reason for not ordering that the application for the Misrepresentation Orders be dealt with as an *inter partes* proceeding. Because of the uncertainty at this stage as to the impact on particular Investors or groups of Investors of the making of the Misrepresentation Orders, any individual Investor who participates in the proceedings, particularly those who oppose the application, can properly be treated as not acting just for themselves and their own benefit but for the purpose of facilitating the resolution of an issue that needs to be determined in order to allow the JOLs to make progress in the liquidation and to assist in the administration of the liquidation estate. The Investors who appear to oppose the making of the Misrepresentation Orders will be playing a role that will not necessarily reflect their actual, overall, interests in the winding up. In these circumstances, in a case involving what can be treated as an application sponsored by the JOLs to assist them in carrying out their functions, it would in my view not be appropriate to treat the dispute over the Misrepresentation Orders as involving only or primarily the separate interests of the misrepresentation creditors and those

selected to oppose the application, including a Late Redeemer such as Eiffel. The position is closer to *SPhinx* than to *Belmont*. The position would be different if the interests of particular Investors or groups of Investors were crystallised and clearly ascertainable.

100. I have considered whether the JOLs should be required to defer an application to the Court to decide the Misrepresentation Issues and instead first complete the process of reviewing and adjudicating on Investor proofs. They would then need to adjudicate proofs based on the legal advice they have received and leave it to the Investors to decide whether to challenge the JOLs' decision. Presumably, based on the position which the JOLs have explained to the Court on this application, the JOLs would admit the proofs of misrepresentation creditors and it would be left to other Investors to seek to expunge the admitted proof and challenge the right of misrepresentation creditors to be admitted. This approach would require Investors to assume the costs risk of litigating the Misrepresentation Issues such that if it was determined that misrepresentation creditors were entitled to prove, the costs of the challenge were likely to be borne by the Investors who chose to challenge the JOLs' decision rather than by the estate (which would have to bear the costs of the Investors who opposed the making of the Misrepresentation Orders, even if they were made, if a pre-emptive costs order was made on the JOLs' sanction application). I have decided that it would not be right to follow this course. First, it seems to me that the Court should give substantial weight to the views of the official liquidators as to the manner in which they should perform their functions and as to the best way in which to deal with difficult issues that arise in the administration of the estate. This does not mean that the Court cannot or should not override or refuse to follow the views of official liquidators but in my view it should be slow to do so. In the present case, it would be invidious to require the JOLs to adjudicate on proofs in circumstances where the legal advice they have received has raised real and substantial doubts as the applicable law and the JOLs have sought the Court's assistance by way of a directions application as to how they should act. If the Court were to refuse to assist and left the JOLs to form a view as to whether to admit or reject the proofs of misrepresentation creditors in circumstances of legal uncertainty the JOLs would of necessity be left to decide on whom to throw the burden of litigating the Misrepresentation Issues. If they admitted the proofs of the misrepresentation creditors, the costs risk would be put on the other Investors while if they rejected those proofs, the burden would be on the misrepresentation creditors. These consequences of the alternative approach seem to me to be very unsatisfactory. The JOLs have



found themselves in a difficult position and in effect need the Court to decide a test case so that they can decide how properly to exercise their powers to adjudicate on proofs. In the circumstances I think it would be wrong to require the JOLs to adopt a different approach and require them first to adjudicate proofs.

101. This view of the purpose of and issues raised by the application for the Misrepresentation Orders also supports the conclusion that the party joined to oppose the application should be treated as participating (at least to a material extent) for the benefit of the estate (by facilitating the JOLs' application and administration of the liquidation estate) and ultimately all Investors (whoever they may be) who will be better off if the Misrepresentation Orders are not made, and not just for its own benefit. As a result, that party should have its costs paid for out of the liquidation estate. It also follows that it would not be appropriate to make a representation order. The membership of each relevant class of Investors is insufficiently settled to allow the Court safely to establish which Investors (using the language of Smellie CJ in *SPhinx* at [31]) have a common interest and will benefit in common from the refusal to make the Misrepresentation Orders.

102. Eiffel has argued that the impact of the Misrepresentation Orders on Investors is sufficiently clear to allow the Court to identify Investors who would clearly benefit (the Unredeemed Investors) and Investors who would be prejudiced (the Late Redeemers) by the making of such orders and who therefore could be joined for the purpose of supporting and opposing the making of the Misrepresentation Orders. Eiffel submits that the Court is unable to adopt the rising tide methodology when determining the manner in which distributions are to be made so that Unredeemed Investors, whether they are Prior Redeemers or not, will have the same interest and be in the same position. But I am not satisfied that I should discount or ignore the concerns expressed by the JOLs on this point, which appear to me to be reasonable and based on their professional assessment as official liquidators as to the position of Investors. I also do not accept and am not satisfied that I can conclude at this stage that the Court will be unable to adopt the rising tide methodology. Furthermore, I would note that while Eiffel has strongly argued for the Misrepresentation Issues to be adjudicated as an *inter partes* proceeding between the Investor groups it has identified, it appears not to accept the consequences of adopting such an approach. If this approach were to be adopted, the Investors concerned would be acting in their own interests and the usual rules as to costs would need to be applied.

103. The JOLs consider that they need to, and that it is best if they, actively participate and argue for the making of the Misrepresentation Orders. They have not suggested that a misrepresentation creditor be joined to make the case for making the Misrepresentation Orders. This appears to be for a number of reasons. They submitted that by adopting this approach there would be substantial costs savings: the JOLs are already well versed in the Misrepresentation Issues and it would involve unnecessary expense and duplication for another party to replicate that work in order to argue in favour of the Misrepresentation Orders (particularly in circumstances where the JOLs consider, based on legal advice, that making the Misrepresentation Orders is the proper result). I also assume that the JOLs consider that they are best placed to take the lead in arguing in favour of the Misrepresentation Orders since the uncertainties regarding the impact of the Misrepresentation Orders on Investors make it difficult to find an Investor who could properly fill that role. Furthermore, no Investor has yet come forward and indicated a willingness to be joined, so that the JOLs consider that they must act as advocate on behalf of the misrepresentation creditors. Eiffel has however criticised the JOLs for failing to ask any of the Unredeemed Investors whether they would be prepared to be joined for the purpose of arguing in support of the Misrepresentation Orders and I note that Mr Johnson's evidence shows that a number of Investors have filed statements of position that indicate that they support the making of the Misrepresentation Orders (see the Investor Schedule referred to and extracted above).
104. On balance, I consider that it is appropriate for the JOLs to argue in support of the Misrepresentation Orders but they will need to consult with Investors who have made claims based on misrepresentations. This is appropriate where, as I have decided, the application for the Misrepresentation Orders can be characterised as necessary to facilitate the proper performance of the official liquidators' duties and for the benefit of the estate, and where the Investor joined to oppose the making of the Misrepresentation Orders will be entitled to be paid its costs out of the estate. I am prepared, as I have already confirmed, to accept the JOLs' evidence regarding the lack of alignment between and the difficulties at this stage in definitively ascertaining the interests of Investors with respect to the Misrepresentation Orders and so there is a proper basis for allowing the JOLs to step in and play an active role in the proceedings. I also give weight to the JOLs' views and take into account the fact that there will be material costs savings in adopting this approach. But I accept Eiffel's submission that it would have been unfair for the JOLs

actively to advocate for the Misrepresentation Orders at the expense of the estate while Eiffel (as a formal or informal representative of the Late Redeemers and those who would be prejudiced by the making of the Misrepresentation Orders) was required to oppose the making of those orders while at risk as to costs (even though the risk was substantially mitigated by the costs regime established by CWR O. 24, r. 9(4) and (5)). If the JOLs' active participation is justified because the application is not suitable to be adjudicated as an *inter partes* proceeding and is for the benefit of the estate, it would be wrong in principle to put the opposing party at a costs disadvantage and to deprive it of the costs protection to which parties are entitled when participating in proceedings at the request of the official liquidators for the benefit of the liquidation and the liquidation estate. It is beside the point that the opposing Investors would have had to take a costs risk if the JOLs had followed a different procedural path and the dispute had arisen after they had adjudicated a proof of debt by a misrepresentation creditor who had then sought to challenge the JOLs' admission of the claim. The JOLs wish to adopt the costs regime applicable after an adjudication of a proof in circumstances where they consider (and I have decided) that there are good reasons for delaying adjudication and where, as I have explained, the decision whether to admit or reject a proof in circumstances of legal uncertainty would itself, arguably arbitrarily, determine on which group of Investors the costs burden of litigating the Misrepresentation Issues would fall. This is one point on which I feel bound not to follow the JOLs' preferred approach.

105. Permitting the JOLs actively to argue for relief that affects the rights of Investors requires a sufficient reason to be found to justify a departure from the general rule. The general rule is that official liquidators should adopt a neutral stance where there is a dispute between creditors or contributories. As has repeatedly been made clear in the authorities to which I have already referred, as a general matter the proper role of the JOLs is to remain neutral when a dispute or issue arises as between creditors or contributories (see for example Smellie CJ in *SPhinx* at [34] and *Belmont* at [7]). The proper approach is well summarised in Lewin (dealing with the position of trustees where there are disputes involving trust beneficiaries) as follows (underlining added):

*“48-035 Leaving aside cases within Buckton category (3) where a claim is made against a trustee who has distributed the whole trust fund on an alleged misconstruction of the trust instrument or wrong view of the law, which have the character of hostile proceedings between the claimant and the trustees, generally the proper role of the trustee is a neutral one as between the*

*beneficiaries or persons who claim to be beneficiaries. Provided that a trustee conducts himself in the proceedings in this way, his right of indemnity in accordance with general principles is secure, though a trustee who takes the side of some beneficiaries against others, thereby acting for a benefit other than that of the trust fund, is at risk of being held to have acted unreasonably and so deprived of his right of indemnity, and may be ordered to pay the costs of the successful beneficiary under Part 44, rule 44.3(2) of the Civil Procedure Rules.*

48-036 *Being neutral should not necessarily be equated with being passive, especially in cases falling within Buckton categories (1) and (2). Since the objective in cases within these categories is to obtain the guidance of the court, the court may well be assisted by submissions from the trustees as to the principles of law or construction involved. Further, there are cases where the argument presented on behalf of beneficiaries is one-sided, and the court is assisted by hearing the contrary argument from counsel for the trustee. For example, if unborn beneficiaries are in a position of their own, the trustees are under a duty to address the court on their behalf and likewise where there is a class of beneficiaries with an opposing interest of whom none is willing to participate in the proceedings. A trustee who assists the court in this way will not be deprived of costs."*

106. This approach was followed in the Lehman *Waterfall* cases. The administrators remained neutral but not passive (see the passage from Lady Justice Gloster's judgment in *Lehman 7 CA* cited by Eiffel and quoted above). In those large and complex applications, the administrators played a critical role in coordinating and overseeing the applications and providing the court with assistance including by offering their own views on issues not fully addressed by the parties or the merits of the competing positions adopted by the parties. But they did not so in circumstances where they were advocating for one side in the dispute at the expense of the estate while the other side in the dispute had to argue their case while at risk as to costs. It is true that pre-emptive costs orders were not made and that the determination as to costs was made at the end of the proceedings in light of an assessment of the nature of the issues in dispute and the manner in which the proceedings were conducted. The approach taken by the court in relation to costs can clearly be seen in the judgment of Mr Justice Hildyard in respect of *Waterfall IIC* [2018] EWHC 924. This judgment was not cited by the parties in this application although it could usefully have been, as it helpfully deals with questions of characterisation and the general approach to costs which are relevant here.

107. As regards costs, the starting point is CWR O. 24, r. 9(4) and (5). These sub-rules are intended to be applied after the event since they refer to the outcome of the proceedings. The sub-rules fall to be applied after it is known whether the creditor or contributory who opposed the sanction application has been successful or unsuccessful, and at a time when the Court can properly assess whether there were exceptional circumstances and special reasons for departing from the general rules. However, the JOLs did not dispute that the Court has jurisdiction to make a pre-emptive costs order. The only question was whether it should do so in the circumstances of this case.
108. I accept that the Court should be cautious before making a pre-emptive costs order and departing from the general rule that costs follow the event. The Court will often only be in a position to determine the proper costs order after the relevant hearing, when it can see how the parties have conducted themselves and the extent of any one party's contribution to the resolution of dispute. I note in particular the discussion of the approach to be adopted by the Court both in *Sphinx* (in which Chief Justice Smellie referred to the judgment of Browne-Wilkinson J in *Westdock Realisations*) and *McDonald*. However, in this case it seems to me that a pre-emptive costs order is both justified and appropriate. The application for the Misrepresentation Orders involves, as the JOLs acknowledged, a limited and narrow range of issues so that the Court can at this stage make a reliable assessment of the manner in which the application will be dealt with and the role that Eiffel can be expected to play. I am satisfied that Eiffel's participation is necessary to enable the application to proceed and will be for the benefit of the estate, so that it will in any event be appropriate to make an order that Eiffel's costs be paid out of the estate. However, I consider that it is appropriate to make an order, as Chief Justice Smellie did in *SPHINX*, which adjusts the basis on which Eiffel's costs may be recovered and limits Eiffel's entitlement to the reasonable costs of its counsel and attorneys by reference to agreed hourly rates. Doing so will ensure that the costs burden on the liquidation estate can be managed and minimised, while ensuring that Eiffel's proper legal expenses for the counsel and attorneys of its choice are paid. This approach also takes into account the LC's concerns regarding the extra costs which the estate will be required to bear. But I do not consider that the LC's objection based on double payment was justified. The fact that the JOLs have incurred costs in obtaining legal advice on the misrepresentation claims does not justify a refusal to allow Eiffel to be paid its costs out of the estate where the JOLs have chosen not to adjudicate those claims (by for example admitting them) and have sponsored an application for their benefit to determine the difficult points of law that arise. Nor do I consider

that there is any risk that ordering that Eiffel's costs be paid out of the estate on the basis I have set out will incentivise Eiffel to run bad arguments, adopt a self-serving strategy to the detriment of the estate or run up excessive costs. The points in issue are, as I have said, narrow and relatively clear and the order will provide that Eiffel is entitled to its reasonable legal fees based on the specified hourly rates, thereby ensuring that fees unreasonably incurred will be subject to challenge.

109. I do not consider that Eiffel should be formally appointed as a representative of the Late Redeemers. I accept the JOLs' submissions on this point. This is neither necessary nor appropriate. It is not necessary since Eiffel can adequately perform the role of putting before the Court the arguments in opposition to the JOLs' application for the Misrepresentation Orders without being a formal representative (Eiffel will be able to consult with and obtain input from Sirius). There is also no need at this stage for the Late Redeemers and other Investors formally to be bound by the Court's decision. To use the language of Mr Justice Briggs (as he then was) in *RAB Market Cycles* (at [3] and [4]), the Court will have heard "*full adversarial argument*" on the issues arising so that "*the interests of all those [Investors] who would benefit from a conclusion that [the Misrepresentation Orders should not be made] have been sufficiently and rigorously advanced by the submissions made on behalf of [Eiffel], such that [the Court's] decision on [the JOLs'] application will be of value to the [JOLs], even if not, strictly, binding on every such person*". I accept that the Lehman *Waterfall* cases show that the Court will, in appropriate cases, adopt a pragmatic approach to the procedural aspects of sanction (or directions) applications and that there can be an effective and fair adjudication of disputes and the resolution of issues affecting the conduct of the liquidation without the need for representatives to be appointed. Having said that, it seems to me to be important that the Court's ruling will in practice resolve the core legal issues raised relating to misrepresentation claims. It would be most unfortunate, and I would regard the proposed procedure to be unacceptable, if the JOLs were not confident that the Court's decision on the Amended Summons would avoid subsequent re-litigation of those issues and facilitate the resolution of disputes in the liquidation. If this were not the case, then the time and expense involved in the proceedings would not be justified and it would be preferable to wait until *inter partes* proceedings with formal representatives could be conducted to definitively determine the issues.

110. Accordingly, in the circumstances it seems to me that the JOLs' sanction application (by way of an application for directions) in relation to the Misrepresentation Orders should be treated as one for the benefit of the JOLs and the estate that can properly be conducted without the need for an *inter partes* proceeding and that the JOLs may advocate in favour of the making of the Misrepresentation Orders and Eiffel can be joined as a party for the purpose of opposing the making of the Misrepresentation Orders on the basis that Eiffel's reasonable costs should, subject to fee rates for Eiffel's counsel and attorneys being agreed by the parties or subsequently determined by the Court, be paid by DLIFF as an expense of the winding up (following the *Sphinx* model). If following the substantive hearing of the application for the Misrepresentation Orders the parties are unable to agree the quantum of Eiffel's reasonable fees, the Court (by way of taxation) will determine them.

#### *The Preliminary Issue*

111. I also do not consider that it is necessary or appropriate to direct that the Preliminary Issue be determined prior to the hearing of the application for the Misrepresentation Orders. Eiffel will be assisting the JOLs and the estate in the determination of whether the Misrepresentation Orders should be made. Their reasonable legal expenses will be paid out of the estate. In these circumstances, they do not need to know definitively that they will be admitted as a creditor in the liquidation in order to justify their participation in these proceedings. Eiffel will obviously wish to be satisfied that their participation is worthwhile both because they will not be out of pocket and because opposing the making of the Misrepresentation Orders makes sense in view of their likely position in the winding up. But they should have no difficulty on these points in view of the costs order I propose to make and the position as explained by the JOLs (namely, that there are good grounds for concluding that the Late Redeemers are creditors subject to Available Cash Limitation issue and because success in their opposition is likely to make that issue irrelevant). It also seems to me that to delay a decision on the application for the Misrepresentation Orders by requiring a prior determination of the Preliminary Issue, when the Preliminary Issue may not need to be litigated at all, is undesirable and I note that after the final determination of the application for the Misrepresentation Orders there will be an opportunity for the parties to discuss and seek to resolve the open issues regarding the rights of Late Redeemers to be admitted as creditors, thereby possibly avoiding the need for litigation (it is not

clear to me that the opportunities for negotiation have yet been exhausted). I would also note that if Eiffel as a Late Redeemer insisted on commencing proceedings (after having obtained the requisite leave to do so) to establish its right to be admitted as a creditor (after a rejection of its proof by the JOLs or before the JOLs' adjudication of the proof if Eiffel sought an order that the JOLs adjudicate the proof and that it be admitted as a creditor), it would then be acting in and to protect its own interests and would not be entitled to have its costs paid out of the estate.

#### *The Late Subscribers Contract Orders*

112. As regards the Late Subscribers Contract Orders, the JOLs consider on balance that all Late Subscribers have become shareholders and that all subscription monies paid by them have become assets of the estate. But they wish to have these conclusions validated and confirmed by the Court before acting on them. They wish to be permitted to argue in support of the Late Subscribers Contract Orders. The issues arising appear to involve primarily questions of construction of the relevant documents together possibly with some questions of fact. The Late Subscribers Contract Orders raise the question as to whether the Late Subscribers are to be treated as shareholders or as parties seeking to recover their subscription monies either as beneficiaries of a trust of, or as creditors in respect of a claim for repayment of a sum equal to, those funds.
113. It appears, as noted above, that some Late Subscribers have come forward, including Sparkasse, but it is not clear, to me at least, whether any of them have indicated whether they wish to claim that they are not shareholders. However, I note from the table contained in Johnson 15 (set out above) that a number of Investors have indicated that they oppose the making of the Late Subscribers Contract Orders. It could be that some Late Subscribers consider that they would be better off if their subscription contracts were not completed, but as I say the position is not clear. At the hearing, Mr McGriele confirmed that Sparkasse (with the support of the Bedell Cristin Funds) was prepared to be joined as a party and as a representative of the Late Subscribers provided that a suitable pre-emptive costs order was made. However, Mr McGriele did not



indicate whether Sparkasse (and the Bedell Cristin Funds) wished to support or oppose the making of the Late Subscribers Contract Orders.

114. What is clear, is that the JOLs wish to have the issue resolved, that some Investors support while others oppose the making of the Late Subscribers Contract Orders and that Sparkasse is prepared to be joined as a party. Eiffel has sought an order that the application for the Late Subscribers Contract Orders be adjudicated as an *inter partes* proceeding between (I assume) a representative Late Subscriber and a representative Unredeemed Investor but does not itself wish to participate and has not indicated (as I noted above) what directions it considers to be appropriate.

115. It seems to me that there is a strong case for saying that the dispute over whether to make the Late Subscribers Contract Orders raises a hostile claim by the Late Subscribers to have their status as beneficiaries under a trust of their subscription monies or unsecured creditors confirmed and therefore that they should be at risk as to costs in pursuing the claim. Equally, those Investors who support the Late Subscribers Contract Orders, because they wish to benefit by having the Late Subscribers confirmed as shareholders, should be at risk as to costs. It can also be said that the commercial impact of the Late Subscribers Contract Orders is not subject to the same uncertainties as those that apply to the Misrepresentation Orders and therefore there is no sufficient justification for departing from the normal rule that the stakeholders seeking to assert their rights and those who oppose them should be at risk as to costs so that the losing party rather than the estate will be required to pay the costs of the proceedings. The JOLs, as I have noted, accepted that there is a material difference between the uncertainties regarding the commercial impact of the Misrepresentation Orders and the Late Subscribers Contract Orders (see [67] above) and that in relation to the Late Subscribers Contract Orders the interests of the Late Subscribers were diametrically opposed to the interests of other Investors.

116. There are however arguments that support a different and alternative approach. It is the JOLs who are sponsoring the application for the Late Subscribers Contract Orders in order to enable them to fulfil their functions and make progress in the liquidation and the JOLs will, on the basis of the decision I have just reached, already be actively participating in the proceedings relating

to the Amended Summons with respect to the Misrepresentation Orders. Therefore the application for the Late Subscribers Contract Orders can also be seen as one that in material respects is for the benefit of the official liquidators and the estate and it can be said that costs are likely to be saved if the same approach is adopted in respect of the Late Subscribers Contract Orders as is being adopted in relation to the Misrepresentation Orders. Furthermore, it can be said that it would be unfair to permit the Investor joined to oppose the making of the Misrepresentation Orders to have its costs paid out of the estate while the Investors joined to argue in support of and to oppose the making of the Late Subscribers Contract Orders should be required to participate in the proceedings on the basis that they are at risk as to costs. It is also unclear at this stage that any Late Subscribers or other Investors would be prepared to be joined if they were so at risk. Sparkasse has, as I have noted, indicated a willingness to be joined but only if its costs are to be paid out of the estate, although of course, it would have to rethink and decide whether it needed to participate in the application if I were to conclude that it would be wrong to make such an order.

117. I have concluded however that, on balance, the right approach is to have the application for the Late Subscribers Contract Orders adjudicated as an *inter partes* proceeding between a Late Subscriber and an Investor who is not a Late Subscriber. I appreciate that the JOLs consider that they need the guidance of the Court before deciding the Late Subscriber Issues and determining whether to treat the Late Subscribers as shareholders (and as I have said give considerable weight to the JOLs' views as to the procedure to be adopted and their need for the Court's assistance). However, it seems to me that if there is a material uncertainty as to the Late Subscribers' rights and status then the proper approach is for the JOLs effectively to interplead and for the issue and dispute to be litigated between the Late Subscribers and Investors who consider that the Late Subscribers should be treated as shareholders. It seems to me that the opposition to the application for the Late Subscribers Contract Orders does in substance, when properly characterised, involve a hostile claim by (or for the benefit of) the Late Subscribers in their own interests so that it would not be acceptable for the Late Subscribers to be paid out of the liquidation estate if they are unsuccessful. And any Investor who wishes to support the making of the Late Subscribers Contract Orders would be doing so in its own interests and should bear the costs of doing so if unsuccessful. There is no sufficient justification, as there is with respect to the Misrepresentation Orders, to justify a departure from the normal costs regime. The Misrepresentation Issues raise

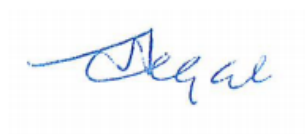
difficult points of law on which the JOLs are entitled to seek the guidance of the Court before adjudicating claims (effectively they raise test cases on the applicable law) so that the costs of Investors joined to the JOLs' application can properly be paid out of the liquidation estate. It seems to me that the position is different in respect of the Late Subscriber Issues. They give rise to case and fact specific disputes where the interests of Late Subscribers and other Investors are clearly defined and which should be resolved as between and at the expense of the affected and adverse parties. The solution for the JOLs, as I have said, is effectively to interplead.

118. Accordingly, the JOLs should invite a Late Subscriber (initially Sparkasse) to agree to be joined to argue in opposition to the Late Subscriber Contract Orders and an Investor who is not a Late Subscriber to agree to be joined to support the Late Subscriber Contract Orders, on the basis that the application for the Late Subscriber Contract Orders be adjudicated as an *inter partes* proceeding with costs to be determined in the usual way after the substantive hearing but with the expectation that the normal costs regime will apply and costs will follow the event.
119. I can see that the Investors who are not Late Subscribers may take the view that since the JOLs have indicated that on balance they are inclined to conclude that the subscription process for all Late Subscribers was validly completed and that they are to be treated as shareholders, they can stand back, allow the JOLs to confirm that this is how they intend to treat the Late Subscribers and leave it to the Late Subscribers to litigate to challenge that approach. But if they did that, and the Late Subscribers did seek orders that the Late Subscribers not be treated as shareholders, an Investor would then need to apply to be joined to defend their position and be at risk as to costs.
120. As I have said, I am reluctant to refuse to provide a procedural forum for providing the JOLs with the guidance they seek but the Court must act as the guardian of the liquidation estate and have regard to the views of affected Investors. Where there are uncertainties as to the substantive rights of those with claims against or as entitlements as shareholders to the estate, which in substance give rise to disputes between stakeholders, the costs of resolving such disputes should generally be for those stakeholders and not the estate and the JOLs should remain neutral as between them. If the approach which the JOLs have proposed with respect to the Late Subscriber Contract Orders was to be followed, the estate would be bearing the costs of the JOLs' participation in the application, which participation advocated and would be for the benefit of the Investors who are

not Late Subscribers and, in view, to maintain fairness as between Investors, it would be necessary to order that any Late Subscriber joined to oppose the making of the Late Subscriber Contract Orders should have its costs paid out of the estate. This approach, which I have permitted in relation to the application in relation to the Misrepresentation Orders, is exceptional and requires a clear and strong justification, which in my view does not exist in relation to the Late Subscriber Contract Orders.

*Counsel to file draft orders*

121. I shall invite counsel to prepare and seek to agree and then file for my approval a suitable form of order incorporating appropriate orders and further procedural directions. If the parties are unable to reach agreement they should file the forms of orders they seek with brief explanations of their respective positions and I shall then decide on the form of order to be made. I also invite the parties to seek to agree an appropriate order as to costs and, once again, if they are unable to do so they should file the forms of orders they seek with brief explanations of their respective positions. I appreciate that it may take a little time for the parties to review this judgment, consider their positions and consult with the LC and the Bedell Cristin Funds but I would ask that the forms of draft order that I have requested be filed as soon as practicable and in any event within 28 days of the handing down of this judgment.



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**Mr Justice Segal**

**Judge of the Grand Court, Cayman Islands (Financial Services Division)**

**10 November 2022**